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[Proposed Rules]  
[Page 57292-57296]  
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Proposed Rules  
Federal Register

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[[Page 57292]]

DEPARTMENT OF THE TREASURY

Office of the Comptroller of the Currency

12 CFR Part 32

[Docket No. 00-19]  
RIN 1557-AB82

Community Bank-Focused Regulation Review: Lending Limits Pilot Program

AGENCY: Office of the Comptroller of the Currency, Treasury

ACTION: Notice of proposed rulemaking.

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SUMMARY: The Office of the Comptroller of the Currency (OCC) is proposing to amend part 32, its regulation governing the percentage of capital and surplus that a national bank may loan to any one borrower. This proposal would implement a pilot program that would create new exceptions to the lending limit for 1-4 family residential real estate loans and loans to small businesses. The proposal also would modify the lending limit exemption for loans to or guaranteed by obligations of state and local governments. Only eligible banks will be permitted to make use of the new exceptions and use of the exceptions also will be subject to an application process. The proposal is being issued in response to the advance notice of proposed rulemaking that the OCC published to initiate its community bank-focused regulation review. The proposal is intended to remove unnecessary regulatory burden on community banks without impairing their safety and soundness. If the proposed pilot program is adopted as a final rule, the OCC will review national banks' experience with the new exceptions over the three year pilot period and determine whether to retain, modify or rescind the

exceptions.

DATES: Comments must be received on or before November 21, 2000.

ADDRESSES: Please direct your comments to: Communications Division, Office of the Comptroller of the Currency, 250 E Street, SW., Third Floor, Washington, DC 20219, Attention: Docket No. 00-19; Fax number (202) 874-5274 or Internet address: regs.comments@occ.treas.gov. Comments may be inspected and photocopied at the OCC's Public Reference Room, 250 E Street, SW., Washington, DC, between 9 a.m. and 5 p.m. on business days. You can make an appointment to inspect the comments by calling (202) 874-5043.

FOR FURTHER INFORMATION CONTACT: Stuart Feldstein, Assistant Director, Legislative and Regulatory Activities Division, (202) 874-5090; Deborah Katz, Senior Attorney, Legislative and Regulatory Activities Division, (202) 874-5090; or Heidi Thomas, Senior Attorney, Legislative and Regulatory Activities Division, (202) 874-5090.

SUPPLEMENTARY INFORMATION:

#### Background

On May 12, 1999, the OCC issued an advance notice of proposed rulemaking (ANPR) inviting comment on possible regulatory changes relating to lending limits, corporate activities and transactions, corporate governance, and capital requirements that could benefit community banks. 64 FR 25469. In issuing the ANPR, we recognized that community banks operate with more limited resources than larger institutions and may present a different risk profile. For example, many community banks have more direct ``hands-on'' oversight by senior management and a smaller range of operations such that less complex risk-management or compliance systems may be appropriate. In addition, differences between community banks and larger banks in operational structure and focus may have resulted in inefficient or uneven application of regulatory requirements. The purpose of our community bank-focused regulation review was to eliminate or modify regulatory requirements that impose unnecessary burden. In addition, we sought to identify regulations for which it may be appropriate to develop alternative, differential regulatory approaches that will minimize burden on community banks without jeopardizing their safety and soundness.

We received forty-one comment letters in response to the ANPR. Thirty-five of these letters commented on various aspects of the national bank lending limit. Twelve U.S.C. 84, the national bank lending limit, governs the percentage of capital and surplus that a bank may loan to any one borrower. OCC regulations implementing section 84 are set forth at 12 CFR part 32. Under section 84 and part 32, a national bank can make unsecured loans of up to 15 percent of its unimpaired capital and surplus to a single borrower, and extend an additional 10 percent of unimpaired capital and surplus to the same borrower, if the loan is secured by ``readily marketable collateral.'' Part 32 refers to these lending limits as ``the combined general limit.'' The statute and regulation also expressly provide other exceptions to and exemptions from the combined general limit for various types of loans and extensions of credit. Finally, the statute authorizes the OCC to establish lending limits ``for particular classes or categories of loans'' that are different from those expressly provided by its terms.'' 12 U.S.C. 84(d)(1).

A majority of commenters stated that the lending limits in section

84, as interpreted in part 32, are especially problematic for community banks because they do not provide enough flexibility for them to adequately serve their customers. Because of their small size, community banks can quickly reach their lending limits. Many commenters noted that the current lending limits have prevented them from continuing to lend to creditworthy customers, and that this has caused a loss in potential income, especially from valued customers whose credit needs have increased with the growth of their businesses. These commenters indicated that, as a result of the lending limits, they often must participate out larger loans to other banks, which can be very burdensome and time consuming for both the bank and the borrower. In addition, the commenters noted that when a community bank participates its loans, the bank risks losing its customer to the participant.

Many commenters also noted that States provide higher lending limits than those set forth in section 84 and part 32. Many of these commenters suggested that Federal lending limits be the same as those available for State banks so that national banks can compete on equal footing with other financial service providers in the markets where they compete.

[[Page 57293]]

A minority of commenters found the current lending limits appropriate and opposed any lending limit increase. Some of these commenters advocated the use of loan participations to support spreading risk.

#### Description of the Proposal

This notice of proposed rulemaking (NPRM) addresses suggestions by the commenters. Specifically, we are proposing to amend 12 CFR part 32 to create new lending limit exceptions for real estate and small business loans for national banks with main offices located in States where a limit higher than the current Federal limit applies, and to modify the lending limit exemption in Sec. 32.3(c) for loans to or guaranteed by general obligations of State and local governments. To ensure that national banks use this additional lending authority in a way that is consistent with safe and sound banking practices, the new exceptions will be available only to "eligible banks," and will be subject to an application process. Furthermore, an aggregate limit will restrict a bank's ability to make use of this new lending authority.

#### New Exceptions for 1-4 Family Residential Real Estate and Small Business Loans

##### 1. Categories of Loans Subject to Exceptions

In reviewing part 32, we considered a number of different categories of loans for which alternative lending limits may be appropriate. One-to-four family residential real estate and small business lending are lines of business common for community banks. Thus, providing additional lending authority in these areas is likely to be responsive to the concerns described by the majority of commenters who responded to the ANPR. Moreover, national banks have substantial and longstanding experience with lending in these areas. The safety and soundness issues presented by these types of loans are already issues that banks routinely address, so that banks can rely on their existing expertise to use this additional lending authority.

The exception for real estate applies only when a loan is secured by a perfected first-lien security interest in 1-4 family residential

real estate in an amount that may not exceed 80 percent of the appraised value of the collateral at the time the loan is made. The exception for small business loans, as proposed, extends additional lending authority for loans that could be unsecured, or secured in a manner that is not specified by regulation. As all of the other lending limit exceptions apply to secured loans only, either when there is specific collateral pledged or a guarantee offered, we invite comment on whether the exception for small business loans should require specific collateral.

The NPRM also requests comment on whether the definition of ``small business loan'' in the proposed regulation is appropriate. This definition is identical to that found in our CRA regulation, 12 CFR 25.12(u), which incorporates the definition of ``loans to small businesses'' from the instructions for preparation of the Consolidated Reports of Condition and Income. These include loans with original amounts of \$1 million or less, secured by nonfarm nonresidential properties, and certain commercial and industrial loans.

## 2. Additional Lending Authority

Under this proposal, a bank may extend another ten percent of its capital and surplus, in addition to the amounts permissible under the currently applicable lending limits, to a single borrower for certain real estate and small business loans, respectively, if a bank's main office is located in a State with a higher limit that applies to these categories of loans. The commenters strongly urged the OCC to provide lending limit parity between a national bank and a State bank in the State where the national bank is located. Some commenters specifically advocated that the OCC adopt the lending limit of their State.

A regulation that would provide exact parity between national banks and banks located in all fifty States would be very complicated, however, because State lending limits may involve higher general limits, a different method of calculating the percentage of bank capital and surplus that can be loaned to a single borrower, or different rules for combining loans to separate borrowers. We believe that providing exceptions in the two categories described to national banks with main offices located in States that apply a higher limit to these categories of loans addresses the parity concern without requiring an unduly complex calculation.

Moreover, in addition to the percentage limit, each of the exceptions contains a \$10 million dollar cap. The dollar cap will ensure that banks over \$1 billion receive no greater benefit, and cannot make larger loans in reliance upon these exceptions, than banks that are smaller in size.

## 3. Applicable Safeguards

The proposal incorporates a number of safeguards designed to ensure that a national bank's use of the additional authority provided by the new exceptions is consistent with safety and soundness. The first is the per borrower dollar limitation described in the preceding paragraph. The second is an aggregate lending cap on any loans, or portions thereof, to all of a bank's borrowers made in reliance upon the real estate and small business exceptions. The total amount of these loans, or portions of loans, together, cannot equal more than 100 percent of a bank's capital and surplus. This cap is similar to the statutory aggregate limit on loans to all bank insiders. See 12 U.S.C. 375b(5).

Third, only ``eligible banks'' can make use of these exceptions. To be an ``eligible bank'' for purposes of this part, the bank must be well capitalized, as defined in 12 CFR 6.4(b)(1),\1\ and must have a rating of 1 or 2 under the Uniform Financial Institutions Rating System, with at least a rating of 2 for the management component of this rating system. These criteria will ensure that only banks with

sufficient capital and good managerial oversight will be permitted to use the increased limits.

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\1\ Under 12 CFR 6.4(b), ``well capitalized'' means that the bank: (1) has a total risk-based capital ratio of 10.0 percent or greater; (2) has a Tier 1 risk-based capital ratio of 6.0 percent or greater; (3) has a leverage ratio of 5.0 percent or greater; and (4) is not subject to any written agreement, order or capital directive, or prompt corrective action directive issued by the OCC pursuant to section 8 of the Federal Deposit Insurance Act (FDI Act), the International Lending Supervision Act of 1983 or section 38 of the FDI Act, or any regulation thereunder, to meet and maintain a specific capital level of any capital measure.

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In addition, the proposed rule requires a bank to apply to its supervisory office and receive approval before using either of the new exceptions. To be deemed complete, the application must contain the following information. First, the bank must certify that it is an ``eligible bank.'' Second, the bank must cite to relevant State laws or regulations showing that its main office is located in a State where the State bank lending limit that applies to 1-4 family residential real estate or small business loans is higher than the limit for national banks. The citation may reference a higher general, specific or other limit that applies to 1-4 family residential real estate or small business loans. This requirement will limit use of the exceptions to national banks with main offices located in States where they are operating at a competitive disadvantage as compared to State banks. Third, the bank must provide the

[[Page 57294]]

OCC with a written resolution by the majority of its board of directors approving the use of these exceptions and confirming the terms and conditions for use of this lending authority. In this way, the board will be required to identify the policies and procedures that will govern the use of the exceptions. Last, the bank will have to provide a description of how the board intends to exercise its continuing responsibility to oversee the use of this lending authority, for example, requiring quarterly reports of all loans made under these exceptions. This provision emphasizes the continuing responsibility of the board to monitor use of the exceptions if the bank's application is granted. Finally, the supervisory office will still have the discretion to deny the bank's application based upon safety and soundness considerations.

OCC approval is effective for three years and may be renewed. Provided the bank remains eligible during the three year period, any loan made during the three year period will remain legal, even if the bank thereafter becomes ineligible.

If this proposal is adopted as a final rule, the OCC will evaluate national banks' experience with these new exceptions over the three year pilot period following the effective date of the rule and determine at that time whether to retain, modify or rescind the exceptions.

#### 4. Comments

In addition to requesting comments generally on all aspects of this proposal, we ask for comments on whether:

The categories of loans identified will alleviate the burden and mitigate some of the competitive disparity for community

banks;

Loans to small business should be secured by specific collateral in order to qualify for the exception;

The per borrower percentage limit and dollar caps for the exceptions are appropriate;

The aggregate limit is appropriate; and

Additional safeguards are warranted.

Exemptions for Loans Secured by State and Local Governments.

Part 32 provides that a loan or extension of credit made by a national bank to, or guaranteed by general obligations of a State or political subdivision is exempt from any lending limit. See 12 CFR part 32.3(c)(5). The phrase "general obligation," is defined in 12 CFR part 1. In addition, to obtain this exemption, this section currently requires the bank to obtain an opinion of counsel that the loan or extension of credit or guarantee is a valid and enforceable general obligation of the State or political subdivision.

However, the requirement for an opinion of counsel is not statutorily required. The OCC understands that requiring an opinion of counsel can be expensive and time consuming for community banks, particularly for those banks that make a substantial number of agricultural loans under the loan guarantee programs. Therefore, the proposed rule revises Sec. 32.3(c)(5) to allow a bank to either obtain an opinion of counsel or rely on the opinion of a State attorney general (or other State legal official with authority to opine on the obligation in question) on the validity and enforceability of the obligation, extension of credit, or guarantee in question.

Comment is invited on this modification as well as all aspects of this NPRM.

Solicitation of Comments on Use of Plain Language

Section 722 of the Gramm-Leach-Bliley Act, Pub. L. 106-102, sec. 722, 113 Stat. 1338, 1471 (Nov. 12, 1999), requires the Federal banking agencies to use plain language in all proposed and final rules published after January 1, 2000. We invite your comments on how to make this proposal easier to understand. For example:

Have we organized the material to suit your needs? If not, how could this material be better organized?

Are the requirements in the proposed regulation clearly stated? If not, how could the regulation be more clearly stated?

Does the proposed regulation contain language or jargon that is not clear? If so, which language requires clarification?

Would a different format (grouping and order of sections, use of headings, paragraphing) make the regulation easier to understand? If so, what changes to the format would make the regulation easier to understand?

What else could we do to make the regulation easier to understand?

Solicitation of Comments on Impact on Community Banks

The OCC also seeks comments on the impact of this proposal on community banks. The OCC recognizes that community banks may present a different risk profile than larger banks, and we intend this proposal to address that difference in risk. We invite comment specifically on whether the proposal achieves that objective.

Regulatory Analysis

## A. Paperwork Reduction Act

For purposes of compliance with the Paperwork Reduction Act of 1995, 44 U.S.C. 3501 et seq., the OCC invites comment on:

(1) Whether the proposed collection of information contained in this notice of proposed rulemaking is necessary for the proper performance of the OCC's functions, including whether the information has practical utility;

(2) The accuracy of the OCC's estimate of the burden of the proposed information collection;

(3) Ways to enhance the quality, utility, and clarity of the information to be collected;

(4) Ways to minimize the burden of the information collection on the respondents, including the use of automated collection techniques or other forms of information technology; and

(5) Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

Respondents are not required to respond to this collection of information unless the final regulation displays a currently valid Office of Management and Budget (OMB) control number.

The collection of information requirements contained in this notice of proposed rulemaking have been submitted to the OMB for review in accordance with the Paperwork Reduction of 1995 (44 U.S.C. 3507(d)). Comments on the collection of information should be sent to the Office of Management and Budget, Paperwork Reduction Project Number 1557-to be assigned, Washington, DC 20503, with a copy to Jessie Dunaway, Legislative and Regulatory Activities Division, Office of the Comptroller of the Currency, 250 E Street, SW, Mailstop 8-4, Washington, DC 20219.

The information collection requirements contained in 12 CFR part 32 are contained in section 32.3(b)(6)(iv). Under this section, the proposed regulation would require national banks to provide the OCC with certain information in connection with an application to receive approval from its supervisory office before using the exceptions to the lending limit for 1-4 family residential real estate loans and loans to small businesses for national banks. The likely respondents are national banks.

Estimated number of respondents: 2,140.

Estimated number of responses: 2,140.

[[Page 57295]]

Estimated burden hours per response: 26.

Estimated total burden: 55,640.

## B. Regulatory Flexibility Act Analysis

The Regulatory Flexibility Act (RFA) requires federal agencies either to certify that a proposed rule would not, if adopted in final form, have a significant impact on a substantial number of small entities or to prepare an initial regulatory flexibility analysis (IRFA) of the proposal and publish the analysis for comment. See 5 U.S.C. 603, 605. On the basis of the information currently available, the OCC is of the opinion that this proposal, if it is adopted in final form, is unlikely to have a significant impact on a substantial number of small entities, within the meaning of those terms as used in the RFA. Commenters are invited to provide the OCC with any information they may have about the likely quantitative effects of the proposal.

C. Executive Order 12866 Determination

The Comptroller of the Currency has determined that this proposed rule, if adopted as a final rule, would not constitute a ``significant regulatory action'' for the purposes of Executive Order 12866. Under the most conservative cost scenarios that the OCC can develop on the basis of available information, the impact of the proposal falls well short of the thresholds established by the Executive Order.

D. Unfunded Mandates Reform Act of 1995 Determinations

Section 202 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. 1532 (Unfunded Mandates Act), requires that an agency prepare a budgetary impact statement before promulgating any rule likely to result in a Federal mandate that may result in the expenditure by State, local, and tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year. If a budgetary impact statement is required, section 205 of the Unfunded Mandates Act also requires the agency to identify and consider a reasonable number of regulatory alternatives before promulgating the rule. However, an agency is not required to assess the effects of its regulatory actions on the private sector to the extent that such regulations incorporate requirements specifically set forth in law. 2 U.S.C. 1531.

The OCC has determined that this proposed regulation will not result in expenditures by State, local, and tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year. Accordingly, the OCC has not prepared a budgetary impact statement or specifically addressed the regulatory alternatives considered.

List of Subjects in 12 CFR Part 32

National banks, Reporting and recordkeeping requirements.

Authority and Issuance

For the reasons set forth in the preamble, part 32 of chapter I of title 12 of the Code of Federal Regulations is proposed to be amended as follows:

PART 32--LENDING LIMITS

1. The authority citation for part 32 continues to read as follows:

Authority: 12 U.S.C. 1 et seq., 84, and 93a.

2. In Sec. 32.2:

A. Paragraph (p) is redesignated as paragraph (s);

B. Paragraph (o) is redesignated as paragraph (q);

C. Paragraphs (i) through (n) are redesignated as paragraphs (j) through (o); and

D. New paragraphs (i), (p) and (r) are added to read as follows:

Sec. 32.2 Definitions.

\* \* \* \* \*

(i) Eligible bank means a national bank that:

(1) Is well capitalized as defined in 12 CFR 6.4(b)(1); and

(2) Has a composite rating of 1 or 2 under the Uniform Financial



Institutions Rating System in connection with the bank's most recent examination or subsequent review, with at least a rating of 2 for management, if that rating is given.

\* \* \* \* \*

(p) Residential real estate loan means any loan or extension of credit that is secured by a perfected first-lien security interest in 1-4 family residential real estate in an amount that does not exceed 80 percent of the appraised value of the collateral at the time the loan or extension of credit is made.

\* \* \* \* \*

(r) Small business loan means any loan or extension of credit included in ``loans to small businesses'' as defined in the instructions for preparation of the Consolidated Report of Condition and Income.

\* \* \* \* \*

3. In Sec. 32.3, a new paragraph (b)(6) is added and paragraph (c)(5) is revised to read as follows:

Sec. 32.3 Lending limits.

\* \* \* \* \*

(b) \* \* \*

(6) Loans for residential real estate and small businesses. (i) An eligible national bank may extend residential real estate loans to a borrower in an amount that does not exceed 10 percent of its capital and surplus or \$ 10 million, whichever is less, in addition to the amount allowed under the bank's combined general limit, if the main office of the bank is located in a state where the state bank lending limit that applies to residential real estate loans is higher than the limit for national banks.

(ii) An eligible national bank may extend small business loans to a borrower in an amount that does not exceed 10 percent of its capital and surplus or \$10 million, whichever is less, in addition to the amount allowed under the bank's combined general limit, if the main office of the bank is located in a state where the state bank lending limit that applies to small business loans is higher than the limit for national banks.

(iii) The total of all portions of a national bank's loans and extensions of credit made pursuant to the exceptions provided in paragraphs (b)(6)(i) and (ii) of this section may not exceed 100 percent of the bank's capital and surplus.

(iv) A national bank must submit an application to, and receive approval from its supervisory office before using the exceptions in paragraphs (b)(6)(i) and (ii) of this section. The supervisory office may approve a completed application if it finds that approval is consistent with safety and soundness. To be deemed complete, the application must include:

(A) Certification that the bank is an ``eligible bank'' as defined in Sec. 32.2(i);

(B) Citations to relevant state laws or regulations;

(C) A copy of a written resolution by a majority of the bank's board of directors approving the use of the limits provided in paragraphs (b)(6)(i) and (ii) of this section, and confirming the terms and conditions for use of this lending authority; and

(D) A description of how the board intends to exercise its continuing responsibility to oversee the use of this lending authority.

(v) Provided that a bank remains an ``eligible bank,'' OCC approval of the bank's authority to use the exceptions in paragraphs (b)(6)(i) and (ii) of this section is effective for three years and may be

renewed.

\* \* \* \* \*

(c) \* \* \*

(5) Loans to or guaranteed by general obligations of a State or political subdivision. (i) A loan or extension of credit to a State or political subdivision that constitutes a general obligation of

[[Page 57296]]

the State or political subdivision, as defined in part 1 of this chapter, and for which the lending bank has an opinion of counsel or the opinion of that State Attorney General, or other State legal official with authority to opine on the obligation in question, that the loan or extension of credit is a valid and enforceable general obligation of the borrower; and

(ii) A loan or extension of credit, including portions thereof, to the extent guaranteed or secured by a general obligation of a State or political subdivision and for which the lending bank has an opinion of counsel or the opinion of that State Attorney General, or other State legal official with authority to opine on the guarantee or collateral in question, that the guarantee or collateral is a valid and enforceable general obligation of that public body.

\* \* \* \* \*

Dated: September 15, 2000.

John D. Hawke, Jr.,

Comptroller of the Currency.

[FR Doc. 00-24280 Filed 9-21-00; 8:45 am]

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