

Key Differences Among National Bank, Federal Savings Association, and Covered Savings Association Requirements

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Note: See also the companion document titled “[Comparison of the Powers of National Banks and Federal Savings Associations](#)” on the OCC website.

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Foreword

This document is designed to generally describe differences in the statutory and regulatory requirements applicable to national banks and federal savings associations (FSAs). It provides a brief guide to some of the key differences rather than a comprehensive analysis of all of the statutes and regulations or policies applicable to, or the powers of, these institutions.

This document also indicates which statutes and regulations discussed in this document are applicable to covered savings associations.¹

This document does not provide official legal interpretations or create any rights or obligations.

¹ Section 5A of the Home Owners' Loan Act (12 USC 1464a), as implemented by 12 CFR 101, authorizes FSAs with total assets of \$20 billion or less, as reported to the Comptroller as of December 31, 2017, to engage in national bank powers and operate as "covered savings associations." A covered savings association has the same rights and privileges as a national bank and is subject to the same duties, restrictions, penalties, liabilities, conditions, and limitations. A covered savings association retains its FSA charter, however, and is treated as an FSA for purposes of governance and for other purposes described in the final rule. For additional information, see OCC Bulletin 2019-25, "Covered Savings Associations."

I. General Powers and Operational Requirements

Lending/Investment Powers

National banks and FSAs have different lending and investment powers. The chart below lists a few of those differences. The table is not all-inclusive and does not contain all the qualifications and conditions that may place additional limitations on these lending and investment powers. Further, additional limits may be applicable under other statutes and regulations, such as 12 USC 84 and 12 CFR 32 (lending limits to one borrower), and, for certain national banks and FSAs, 12 CFR 44 (Volcker rule). For additional information on national bank lending and investment powers, see 12 USC 24(Seventh), 24(Eleventh), and 371, and 12 CFR 1. For additional information on FSA lending and investment powers, see 12 USC 1464(c) and 12 CFR 160. Another useful source is the document entitled “Comparison of the Powers of National Banks and Federal Savings Associations” available on the OCC website.

The following table contains limits on loan/investment categories.

Category	National bank limit	FSA limit	Covered savings association limit
Asset-Backed Securities	No limit for mortgage-backed securities that qualify as certain Type IV securities (12 CFR 1.3(e)). Other asset-backed securities that qualify as Type V securities have a per issuer limit of 25% of the bank’s capital and surplus (12 USC 24(Seventh) and 12 CFR 1.3(f)).	No limit for mortgage-backed securities. For other asset-backed securities, aggregate limit and eligibility to invest depend upon the type of asset that is securitized (12 USC 1464(c)(1)(R) and 12 CFR 160.30).	See national bank limit.
Commercial loans	No limit (12 USC 24(Seventh)).	20% of total assets, provided that amounts in excess of 10% of total assets may be used only for small business loans (12 USC 1464(c)(2)(A); 12 CFR 160.30). Exceptions exist for certain loans to insured financial institutions, brokers, and dealers (12 USC 1464(c)(1)(L) and 12 CFR 160.30).	See national bank limit.
Commercial paper and corporate debt securities	Per issuer limit of 10% of capital and surplus for a Type III security. Generally, aggregated with Type II securities of the same issuer (12 USC 24(Seventh) and 12 CFR 1.3(c)–(d)).	35% of total assets, combined with consumer loans ^a (12 USC 1464(c)(2)(D) and 12 CFR 160.30 and 160.40),	See national bank limit.

^a FSAs may invest amounts in excess of 30 percent of assets, in the aggregate, only in obligations purchased by the FSA directly from the original obligor and for which the FSA does not pay any finder, referral, or other fee.

Category	National bank limit	FSA limit	Covered savings association limit
Community development loans and equity investments	Aggregate investment limit is 5% of capital and surplus, but may invest up to 15% of capital and surplus with OCC approval (12 USC 24(Eleventh) and 12 CFR 24).	Aggregate limit of 5% of total assets, provided that equity investments do not exceed 2% of total assets ^b (12 USC 1464(c)(3)(A) and 12 CFR 160.30). In addition, FSA regulations allow de minimis investments, up to an aggregate limit of the greater of 1% of total capital or \$250,000, for investments that are permissible for a national bank under 12 CFR 24 (12 CFR 160.36). Also, FSA service corporations may make investments that are permitted under 12 CFR 24, subject to limits discussed in "Service Corporations" (12 USC 1464(c)(4)(B) and 12 CFR 5.59(f)(8)).	See national bank limit.
Construction loans without security	No limit (12 USC 24(Seventh)).	Aggregate limit of the greater of total capital or 5% of total assets (12 USC 1464(c)(3)(C) and 12 CFR 160.30).	See national bank limit.
Consumer loans	No limit (12 USC 24(Seventh)).	Aggregate limit of 35% of total assets, combined with commercial paper and corporate debt securities ^c (12 USC 1464(c)(2)(D) and 12 CFR 160.30).	See national bank limit.
Nonconforming loans, secured primarily by residential or farm real property	No limit (12 USC 24(Seventh)).	5% of total assets (12 USC 1464(c)(3)(B) and 12 CFR 160.30).	See national bank limit.

^b See Office of Thrift Supervision Op. Chief Counsel (May 10, 1995). Modifications to this letter resulting from statutory and regulatory changes and other information regarding FSA public welfare investing authority are detailed in the Community Affairs Public Welfare Investments Resource Directory on the OCC website.

^c FSAs may invest in amounts in excess of 30 percent of assets, in the aggregate, only in loans made by the FSA directly to the original obligor and for which the FSA does not pay a finder, referral, or other fee.

Category	National bank limit	FSA limit	Covered savings association limit
Nonresidential real property loans	No limit (12 USC 24(Seventh)).	400% of total capital, unless a higher amount is permitted by the OCC ^d (12 USC 1464(c)(2)(B) and 12 CFR 160.30).	See national bank limit.
Service corporations ^e	No authority ^f	3% of total assets, provided that any amounts in excess of 2% of total assets shall be used primarily for community, inner city, or community development purposes (12 USC 1464(c)(4)(B) and 12 CFR 5.59 and 160.30).	No authority.
Small business investment companies	5% of capital and surplus (15 USC 682(b)(1)).	5% of total capital (15 USC 682(b)(2), 12 USC 1464(c)(4)(D), and 12 CFR 160.30).	See national bank limit.
Small business-related securities	None, provided securities are fully secured by interests in a pool of loans to numerous obligors (12 USC 24(Seventh) and 12 CFR 1.3(e)).	None, provided securities are of investment grade, and represent an interest in promissory notes or leases of personal property evidencing obligations of a small business concern. (12 USC 1464(c)(1)(S) and 12 CFR 160.30).	See national bank limit.
State and local government obligations	None, for general obligations of state and local governments that are Type I securities. Well capitalized banks may invest in revenue bonds without limit (12 CFR 1.3(a)). A per issuer limit of 10% of capital and surplus if a Type II or Type III security (12 USC 24(Seventh); for Type II limit, see 12 CFR 1.3(b); for Type III limit, see 12 CFR 1.3(c)–(d)).	None for general obligations. A per issuer limitation of 10% of the FSA's capital for other obligations. (12 USC 1464(c)(1)(H) and 12 CFR 160.30). See 12 CFR 160.42 for additional details.	See national bank limit.

^d The OCC may permit an FSA to exceed the 400 percent limitation if the OCC determines that the increased authority poses no significant risk to the safe and sound operation of the FSA and is consistent with prudent operating practices. An FSA seeking to exceed the 400 percent limit must file a request with the OCC.

^e Pursuant to 12 CFR 5.59(d)(4), a "service corporation" is an entity that satisfies all of the requirements for service corporations in 12 USC 1464(c)(4)(B) and 12 CFR 5.59, and that is designated by the investing FSA as a service corporation pursuant to 12 CFR 5.59.

^f But see the later discussion regarding bank service companies, subsidiaries, and non-controlling investments.

Legal Lending Limit/Loans to One Borrower

National Banks and Federal Savings Associations (12 USC 84 and 1464(u); 12 CFR 32)

Generally, national banks and FSAs are subject to the same lending limits for loans to one borrower or related borrowers that are financially dependent. In general, this limit totals 15 percent of a national bank's or FSA's capital and surplus plus an additional 10 percent of capital and surplus if the amount that exceeds the 15 percent general limit is fully secured by readily marketable collateral (together, the combined general limit). (See 12 USC 84 for national banks, 12 USC 1464(u) for FSAs, and 12 CFR 32 for both charters). Additional provisions apply to FSAs, described below.

Federal Savings Association

- If an FSA's aggregate lending limit is less than \$500,000, notwithstanding that limitation, the FSA may have total loans and extensions of credit, for any purpose, to one borrower outstanding at one time in an amount not to exceed \$500,000. (12 CFR 32.3(d)(1))
- An FSA may make loans to one borrower to develop domestic residential housing units, not to exceed the lesser of \$30 million or 30 percent of the FSA's unimpaired capital and unimpaired surplus, including all amounts loaned under the general lending limit, provided that the following conditions are met:
 - The FSA is, and continues to be, in compliance with its capital requirements;
 - The OCC permits the FSA to use the higher limit (subject to any conditions imposed by the OCC);²
 - Loans and extensions of credit made pursuant to this provision to all borrowers do not, in aggregate, exceed 150 percent of the FSA's unimpaired capital and unimpaired surplus; and
 - Loans and extensions of credit made pursuant to this provision comply with the applicable loan-to-value requirements.

The authority of an FSA to make a loan or extension of credit to one borrower to develop domestic residential housing units ceases immediately upon the FSA's failure to comply with any one of the requirements set forth in the regulation or any conditions imposed by the OCC to use a higher limit. (12 CFR 32.3(d)(2)(ii))

- An FSA may invest up to 10 percent of unimpaired capital and unimpaired surplus in addition to the combined general limit in the obligations of one issuer evidenced by commercial paper or corporate debt securities that are investment grade. (12 CFR 32.3(d)(3))

²An FSA must submit an application to, and receive approval from, the appropriate OCC supervisory office before using the higher limit set forth under 12 CFR 32.3(d)(2)(i). The supervisory office may approve a completed application if it finds that approval is consistent with safety and soundness. An application by an eligible savings association to use the higher limit is deemed approved as of the 30th day after the application is received by the OCC, unless before that date the OCC informs the savings association it must obtain prior written approval from the OCC. (12 CFR 32.2(d)(2)(iv))

Covered Savings Associations

A covered savings association must comply with the lending limits established for national banks in 12 USC 84 and 12 CFR 32 and not the additional provisions applicable solely to FSAs.

Qualified Thrift Lender

National Banks

A national bank is not required to be a qualified thrift lender (QTL).

Federal Savings Associations (12 USC 1467a(m))

An FSA must be a QTL. An FSA that fails to become or remain a QTL is deemed to have violated section 5 of the Home Owners' Loan Act (HOLA).³ To be a QTL, an FSA must meet either the HOLA QTL Test (12 USC 1467a(m)) or the Internal Revenue Service tax code Domestic Building and Loan Association Test (DBLA Test) (26 CFR 301.7701-13A).

Under the QTL Test, an FSA must hold qualified thrift investments⁴ equal to at least 65 percent of its portfolio assets (12 USC 1467a(m)(4)). An FSA ceases to be a QTL when its ratio of qualified thrift investments (numerator) divided by its portfolio assets (denominator) falls, at month-end, below 65 percent for four months within any 12-month period.

Under the DBLA Test, an FSA must meet (1) a “business operations test” and (2) a “60 percent of assets test.”

- The “business operations test” requires the business of a DBLA to consist primarily of acquiring the savings of the public and investing in loans.
- The “60 percent of assets test” requires that at least 60 percent of a DBLA’s assets must consist of assets that associations normally hold, except for consumer loans that are not educational loans.

An FSA may use either the QTL Test or the DBLA Test to qualify as a QTL and may switch from one test to the other. (See the “Qualified Thrift Lender” booklet of the *Comptroller’s Handbook* for more information).

³ See 12 USC 1467a(m)(3)(B)(i)(IV).

⁴ Qualified thrift investments include loans to purchase, refinance, construct, improve, or repair domestic residential or manufactured housing; home equity loans; educational loans; small business loans; loans made through credit cards or credit card accounts; securities backed by or representing an interest in mortgages on domestic residential or manufactured housing; and FHLB stock. For a complete list, see 12 USC 1467a(m)(4)(C).

12 USC 1467a(m) provides that an FSA that fails to become or remain a QTL is subject to the following restrictions:

- Restrictions effective immediately:
 - The FSA shall not make any new investments or engage in any new activity not allowed for both a national bank and an FSA;
 - The FSA shall not establish any new branch office unless the branch is allowable for a national bank; and
 - The FSA shall not pay dividends unless the dividends (1) are allowable for a national bank, (2) are necessary to meet obligations of a company that controls the FSA, and (3) receive OCC and Board of Governors of the Federal Reserve System (Federal Reserve Board) approval.
- Additional restrictions effective after three years:
 - If an FSA fails to requalify as a QTL within three years, the FSA must dispose of or not engage in any activity unless the investment or activity is allowed for both a national bank and an FSA.

These restrictions are not applicable if the FSA requalifies as a QTL. An FSA may, however, requalify as a QTL only once. Failure to maintain QTL status after requalification permanently subjects an FSA to these restrictions.

An FSA's failure to meet the requirements of 12 USC 1467a(m) may have consequences under other provisions of HOLA as well. 12 USC 1464(r)(1) prohibits an FSA from establishing, retaining, or operating a branch office outside the state in which the FSA's home office is located unless the FSA meets the QTL Test or the DBLA Test.⁵ In addition, 12 USC 1467a(c) bases exceptions from certain savings and loan holding company activities restrictions on, among other things, satisfaction of the QTL requirements.⁶

The OCC may grant temporary and limited exceptions from compliance with the QTL Test when extraordinary circumstances exist⁷ or to significantly facilitate an acquisition of a troubled institution under 12 USC 1823(c) or (k). (See the "Qualified Thrift Lender" booklet of the *Comptroller's Handbook* for more information.)

Covered Savings Associations

A covered savings association is not required to be a QTL.

⁵ 12 USC 1464(r)(2) provides certain exceptions from this restriction.

⁶ See 12 USC 1467a(c)(3)(B)(ii) and 12 USC 1467a(c)(9)(C)(i).

⁷ An example of an extraordinary circumstance is when the effects of high interest rates reduce mortgage demand to such a degree that an insufficient opportunity exists for an association to meet the QTL requirement. See 12 USC 1467a(m)(2)(A). Also, the OCC may facilitate an FSA's efforts to assist communities affected by a natural disaster by temporarily waiving the QTL requirement to allow a capital compliant FSA to help rebuild non-QTL businesses. See OCC Bulletin 2012-28, "Supervisory Guidance on Natural Disasters and Other Emergency Conditions."

Dividends/Capital Distributions

National Banks

(12 USC 56, 59, 60(b), and 1831o(d)(1)(A); 12 CFR 5.46 and 5.64(c)(1))

Dividends. Directors of a national bank may declare and pay dividends of as much of the undivided profits as they judge to be expedient, subject to the following restrictions:

- Unless approved by the OCC, a national bank may not declare a dividend if the total amount of all dividends (common and preferred), including the proposed dividend, declared by the national bank in any current year exceeds the total of the national bank's net income of the current year to date, combined with the retained net income of current year minus one and current year minus two, less the sum of any transfers required by the OCC and any transfers required to be made to a fund for the retirement of any preferred stock.⁸ (12 USC 60(b) and 12 CFR 5.64(c)(1))
 - Requests for prior approval of a dividend under 12 USC 60(b) are submitted to the supervisory office. There is no specified time frame by which the notice must be filed; the board, however, cannot declare the dividend until it receives OCC approval. See the "Capital and Dividends" booklet of the *Comptroller's Licensing Manual*.
- If a national bank has sustained losses at any time that equal or exceed its undivided profits (i.e., retained earnings), the bank is prohibited from paying a dividend (12 USC 56). This rule, however, does not prevent the bank from making a reduction of permanent capital pursuant to 12 USC 59 (see reduction of permanent capital discussion below).
- A national bank may not declare or pay any dividend if, after making the dividend, the national bank would be "undercapitalized" as defined in 12 CFR 6 (12 USC 1831o(d)(1)(A)).

Reduction in permanent capital. In addition to dividends, a national bank has the option of reducing permanent capital. "Permanent capital" is defined as the sum of capital stock and capital surplus. "Capital surplus" is defined as the total of (1) the amount paid in on capital stock in excess of the par or stated value; (2) direct capital contributions representing the amounts paid in to the national bank other than for capital stock; (3) the amount transferred from undivided profits; and (4) the amount transferred from undivided profits reflecting stock dividends. (12 USC 59 and 12 CFR 5.46)

A national bank must obtain the necessary shareholder approval required by statute for any change in its permanent capital. A national bank must submit an application to the OCC licensing office and obtain prior OCC approval for any reduction of its permanent capital. The application must contain the information required by 12 CFR 5.46(i)(1).

⁸ This requirement is essentially the same as one of the criteria triggering an application for an FSA.

Federal Savings Associations (12 CFR 5.55)

When an application is required. If an FSA meets any of the following criteria, it must file an application with the supervisory office at least 30 days before the proposed declaration of dividend or approval of the proposed capital distribution by its board of directors:

- The FSA is not an eligible savings association under 12 CFR 5.3(g).
- The total amount of all capital distributions (including the proposed capital distribution) for the applicable calendar year exceeds the FSA's net income for that year to date plus retained net income for the preceding two years.
- The FSA would not be at least adequately capitalized, as set forth at 12 CFR 6.4, following the distribution.⁹
- The proposed capital distribution would violate a prohibition contained in any applicable statute, regulation, or agreement between the FSA and OCC, or violate a condition imposed on the FSA in an OCC-approved application or notice.

When a notice is required. If an FSA meets any of the following criteria and is not required to file an application as described in the previous section, it must file a notice with the supervisory office at least 30 days before the proposed declaration of dividend or approval of the proposed capital distribution by its board of directors:

- The FSA would not be well capitalized, as defined at 12 CFR 6.4, or would otherwise not remain an eligible savings association following the distribution.
- The proposed capital distribution would reduce the amount, or retire any part, of the FSA's common or preferred stock or retire any part of debt instruments, such as notes or debentures included in capital under 12 CFR 3 (other than regular payments required under a debt instrument approved under 12 CFR 5.56).
- The FSA's proposed capital distribution is payable in property other than cash.
- The FSA is a direct or indirect subsidiary of a mutual savings and loan holding company.
- The FSA is a direct or indirect subsidiary of a company that is not a savings and loan holding company.

The notice is deemed to be approved if the OCC fails to act within 30 calendar days of receipt of the notice.

When an informational submission is required. If an FSA is filing a notice of a proposed dividend with the Federal Reserve Board solely under 12 USC 1467a(f) and not also under 12 USC 1467a(o)(11), and neither an application under 12 CFR 5.55(e)(1) nor a notice under 12 CFR 5.55(e)(2) is required, the FSA must provide an informational copy to the OCC of the notice filed at the same time the notice is filed with the Federal Reserve Board. This informational copy is separate from any notice or application required by the OCC's capital distribution regulations. The OCC requires this informational copy so that it may respond to

⁹ See 12 USC 1831o(d)(1)(A), which provides that an FSA may not declare or pay any dividend, if, after making the dividend, the FSA would be undercapitalized.

requests from the Federal Reserve Board to comment on such filings.¹⁰ Although no formal OCC action is necessary with respect to the informational submissions, the supervisory office generally will comment to the Federal Reserve Board regarding these submissions within the requested period. The OCC will evaluate these submissions under the same standards that apply to OCC review of capital distribution applications and notices.

When no filing is required. If an FSA does not meet any of the criteria listed above, it does not need to file an application, notice, or information statement with the OCC before making a capital distribution.

See 12 CFR 5.55(d)(3) for the definition of “capital distribution”; 12 CFR 5.55(f) for the required contents of the application or notice; and 12 CFR 5.55(h) for factors the OCC considers in reviewing the application or notice. The application or notice may include a schedule proposing capital distributions over a specified period not to exceed 12 months.

Covered Savings Associations

A covered savings association must comply with the rules and regulations applicable to FSAs when declaring and paying dividends.

Issuance of Subordinated Debt

National Banks (12 CFR 5.47)

A national bank that is not an eligible bank, as defined in 12 CFR 5.3(g), must receive prior OCC approval to issue subordinated debt. In addition, an eligible national bank must receive prior OCC approval to issue subordinated debt if the bank will not continue to be an eligible bank after the transaction, the OCC has notified the bank that prior approval is required, or prior approval is required by law (12 CFR 5.47(f)(1)(i)). A national bank must comply with the Securities Offering Disclosure Rules in 12 CFR 16. (12 CFR 5.47(d)(3)(iii))

All national banks must notify the OCC within 10 days of issuance of the subordinated debt that is to be included in regulatory capital (12 CFR 5.47(f)(1)(ii)). In order to be included in capital, the subordinated debt must meet the requirements of 12 CFR 3.20(d) and of 12 CFR 5.47.¹¹

For prepayment of subordinated debt not included in tier 2 capital, an eligible bank must receive prior OCC approval pursuant to 12 CFR 5.47(f)(1)(i)(A) or (B), as appropriate. All national

¹⁰ The Federal Reserve Board has stated that it intends to seek comment from the OCC supervisory office regarding filings under 12 USC 1467a(f) and to request the supervisory office’s comments within 15 days of receipt of its request.

¹¹ A national bank may not include subordinated debt as regulatory capital unless the bank has filed the required notice with the OCC and received notification from the OCC that the subordinated debt issued by the bank qualifies as regulatory capital.

banks with subordinated debt included in tier 2 capital must receive prior OCC approval to prepay the subordinated debt pursuant to 12 CFR 5.47(f)(2)(ii) and (g)(1)(ii)(A).

Federal Savings Associations (12 CFR 5.56 and 163.80(e))

Under 12 CFR 163.80(e), if an FSA intends to issue debt securities with maturities greater than one year and the FSA does not meet its capital requirements under 12 CFR 3, it must file with the appropriate OCC licensing office a notice of intent to issue such securities at least 10 business days before issuance. The OCC has 10 business days after receipt of the filing to object to the issuance of the securities and shall object if the terms or covenants would impose unreasonable burdens on or control over the association's operations.

An FSA that proposes to include subordinated debt in regulatory capital must file an application under 12 CFR 5.56. The subordinated debt must meet the requirements set forth in 12 CFR 5.56(d), including the requirements of 12 CFR 3.20(d). If the subordinated debt securities will not be included in tier 2 capital, the FSA must comply with 12 CFR 160.80. In addition, an FSA that proposes to prepay subordinated debt that is included in capital must file an application under 12 CFR 5.56(b)(2). An FSA must also comply with the Securities Offering Disclosure Rules in 12 CFR 16. (12 CFR 5.56(b)(1)(iii))

Covered Savings Associations

A covered savings association must comply with the rules applicable to FSAs for the issuance of subordinated debt securities and mandatorily redeemable preferred stock.

Investment in Bank Premises

National Banks (12 USC 29 and 371d; 12 CFR 5.37 and 7.1000(c))

Under 12 CFR 5.37, a national bank that is not well capitalized and not assigned a composite rating of 1 or 2 must submit an application to the appropriate supervisory office if an investment in banking premises (or in the stock, bonds, debentures, or other obligations of a corporation holding the premises of the institution) would cause the national bank's aggregate investment in premises to exceed the amount of capital stock of the national bank. For national banks, 12 CFR 5.37(c)(2) defines capital stock as the amount of common stock outstanding and unimpaired plus the amount of perpetual preferred stock outstanding and unimpaired.

National banks that are rated composite 1 or 2 and are well capitalized both before and after the investment are generally not required to obtain prior OCC approval when the national bank's aggregate premises investment is 150 percent of capital and surplus or less. A national bank may invest in corporations holding bank premises pursuant to 12 USC 371d and 12 CFR 5.37.

A national bank that is not required to obtain advance approval under this provision is required to notify the appropriate supervisory office of the investment or loan within 30 days after the investment or loan is made.

Federal Savings Associations (12 CFR 5.37 and 7.1000(c))

Under 12 CFR 5.37, an FSA that is not well capitalized and assigned a composite rating of 1 or 2 must submit an application to the appropriate supervisory office if an investment in banking premises (or in the stock, bonds, debentures or other obligations of a corporation holding the premises of the institution) would cause the FSA's aggregate investment in premises to exceed the amount of capital stock of the FSA. For stock FSAs, 12 CFR 5.37(c)(2) defines capital stock as the amount of common stock outstanding and unimpaired plus the amount of perpetual preferred stock outstanding and unimpaired. For mutual FSAs, however, the regulation defines capital stock as the amount of the FSA's retained earnings.

FSAs that are rated composite 1 or 2 and are well capitalized both before and after the investment are generally not required to obtain prior OCC approval when the FSA's aggregate premises investment is 150 percent of capital and surplus or less. If an FSA, however, proposes to establish or acquire a subsidiary to make an investment in bank premises (or invest in bank premises through an existing subsidiary that has not previously invested in bank premises), the FSA is required to file with the OCC in advance of making the investment (12 CFR 5.38 [operating subsidiaries] and 12 CFR 5.59 [service corporations]). In addition, an FSA that invests in bank premises through a service corporation must comply with the quantitative limitations in 12 CFR 5.37(d) and, to the extent applicable, 12 CFR 5.59.

An FSA that is not required to obtain advance approval under this provision is required to notify the appropriate supervisory office of the investment or loan within 30 days after the investment or loan is made.

Covered Savings Associations

A covered savings association must comply with the rules and requirements applicable to national banks. Mutual covered savings associations must comply with the definition of capital stock for mutual FSAs, meaning that "capital stock" is the amount of the institution's retained earnings.

Other Real Estate Owned

National Banks (12 USC 29; 12 CFR 34.82, 34.83, and 34.86)

12 USC 29, implemented by 12 CFR 34.82, provides that a national bank shall dispose of other real estate owned (OREO) at the earliest time that prudent judgment dictates, but no later than five years (with a possible extension of up to an additional five years). A national bank that

wants an extension of the five-year holding period must file a request with, and receive approval from, the appropriate supervisory office.

12 CFR 34.83 describes what transactions qualify as a disposition of OREO and requires that a national bank make diligent and ongoing efforts to dispose of each parcel of OREO and maintain documentation adequate to reflect those efforts.

12 CFR 34.86 describes the process by which a national bank may make additional advances to complete an OREO project that is a development or improvement project. The regulation specifies that a national bank shall notify the supervisory office 30 days before implementing a development or improvement plan for OREO when the sum of the plan's estimated cost and the bank's current recorded investment amount (including any unpaid prior liens) exceeds 10 percent of the bank's capital and surplus. The required notification must demonstrate that the additional expenditure is consistent with the conditions and limitations set forth at 12 CFR 34.86(a). The OCC has 30 days to review the notice. Unless otherwise informed by the OCC, the bank may implement the plan on the 31st day (or sooner if notified by the OCC), subject to any conditions imposed by the OCC.

See the "Other Real Estate Owned" booklet of the *Comptroller's Handbook* for additional information.

Federal Savings Associations

Currently¹² there is no statutory or regulatory OREO holding period for FSAs.¹³ Management should make a good-faith effort to dispose of OREO, especially OREO that has been held for five years or more. The OCC generally expects that five years is sufficient to dispose of OREO and that an FSA will dispose of OREO within that period unless the FSA provides a well-supported reason demonstrating the need for additional time and an acceptable disposition plan. If the supervisory office determines that the property is being held as an investment, the supervisory office may advise the FSA that it does not have the authority to hold the asset unless the FSA provides an acceptable rationale for its ability to hold the asset as an investment under other authority in HOLA.

No regulation currently governs an FSA's additional expenditures on OREO. The "Other Real Estate Owned" booklet of the *Comptroller's Handbook*, however, indicates that an FSA's inherent or implied salvage powers permit an FSA to hold, operate, and invest additional funds in property acquired as result of, or in lieu of, foreclosure before resale of the property. These powers enable an FSA to take whatever steps may be necessary, including exceeding its legal lending limit, to salvage an investment, provided the steps taken are an integral part of a reasonable and bona fide salvage plan and do not contravene a specific legal prohibition. An

¹² Pursuant to a proposal issued by the OCC on April 24, 2019, the rules for FSA OREO may change. See 79 Fed. Reg. 17094.

¹³ Although 12 CFR 167 provided that an FSA's OREO that was not disposed of within five years or approved for a longer holding period was defined as an investment in real property and deducted from capital, 12 CFR 3 superseded 12 CFR 167 and does not include a similar provision.

FSA that intends to make a salvage powers investment in excess of its lending limit must file a request with, and receive no objection from, its OCC supervisory office. The supervisory office will take into consideration the risks posed by a proposed salvage plan, an FSA's past history of salvage operations, and the financial condition of the FSA and its ability to undertake the risks attendant to salvage operations. Furthermore, when reviewing a proposed salvage plan, the supervisory office will consider whether the plan meets the following criteria:

- Is it necessary to enable the FSA to salvage its existing investment?
- Is it necessary to protect the value of the foreclosed property (e.g., the additional investments will result in a more marketable property)?
- Is it in the best interest of the FSA?
- Will it reduce the risks associated with the foreclosed property?
- Is it for nonspeculative purposes?

See the "Other Real Estate Owned" booklet of the *Comptroller's Handbook* for additional information on salvage powers.

Covered Savings Associations

A covered savings association must comply with the national bank rules and requirements regarding OREO.

Real Estate Development

National Banks

National banks generally are not permitted to engage in real estate development (but see OCC precedent for full utilization of property acquired for bank premises or to recover the full value of OREO).

Federal Savings Associations (12 USC 1464(t)(5); 12 CFR 5.59(f)(5) and (g))

Subject to the limitations of 12 CFR 5.59(g), a service corporation of an FSA is permitted to hold real estate for investment and engage in real estate development. The term "real estate development" refers to the development of land or other real estate for sale or lease in which the related organization has an ownership (equity) interest or actively manages the property. OREO, repossessed assets, and real estate held for use by a savings association or its subsidiary are not included in the definition of real estate development.

An FSA's investment in (and loans to) a service corporation that engages in real estate development must be excluded from total assets and regulatory capital. (12 USC 1464(t)(5))

Covered Savings Associations

A covered savings association must comply with any rules or limitations on real estate development applicable to national banks.

Asset Classification

National Banks

(12 CFR 30, appendix A, II(G))

For national banks, the classification of problem assets and the adequacy of valuation allowances are governed by the safety and soundness standards in 12 CFR 30, appendix A, II(G). Depending on the circumstances, risk rating inaccuracies or an inadequate valuation allowance may be an unsafe or unsound practice.

Federal Savings Associations

(12 CFR 160.160)

12 CFR 160.160 provides that each FSA must evaluate and classify its assets on a regular basis in a manner consistent with, or reconcilable to, the asset classification system used by the OCC. If examiners classify problem assets during an examination, the FSA must recognize such examiner classifications in subsequent reports to the OCC. Based on the evaluation and classification of its assets, each FSA shall establish adequate valuation allowance or charge-offs, as appropriate, consistent with generally accepted accounting principles (GAAP) and the practices of the federal banking agencies.

Covered Savings Associations

A covered savings association must comply with the requirements applicable to national banks.

Authority to Pledge Assets to Secure Public or Private Deposits

National Banks

(12 USC 90 and 92a; 25 USC 156 and 162a)

National banks are prohibited from pledging assets to secure private deposits (*see Texas & Pacific Railway Co. v. Portorff*, 291 U.S. 245 (1934)), unless otherwise permitted by law (see, e.g., 12 USC 90 [for deposits of public funds]; 12 USC 92a [for trust funds]; and 25 USC 156 and 162a [for Native American funds]). (12 CFR 31, appendix A)

Federal Savings Associations

(12 USC 1464(b)(2) and 1464(n); 12 CFR 145.16)

FSAs have statutory authority to give security; act as surety; and issue notes, bonds, debentures, other obligations, or other securities to the extent authorized by the OCC (12 USC 1464(b)(2)). An FSA may give bond or security for deposits of public monies or investments in the FSA by a

governmental unit if required to do so by state law and, subject to certain conditions, may pledge collateral (12 CFR 145.16). FSAs have the authority to pledge assets to secure the deposits of public and private depositors (see, e.g., memorandum from OTS Chief Counsel (January 29, 1991)). In addition, 12 USC 1821(a)(2)(C) and 1464(n) recognize the authority of FSAs to give or pledge securities. Thus, FSAs may pledge assets to secure the deposits of both public and private depositors.

Covered Savings Associations

A covered savings association must comply with the requirements applicable to national banks regarding pledging security for deposits.

Interest-Rate Risk Management Procedures

National Banks

(12 CFR 30, appendix A, II(E))

For national banks, interest-rate risk management issues are governed by the safety and soundness standards in 12 CFR 30, appendix A, II(E). Depending on the circumstances, weaknesses or deficiencies in interest-rate risk management procedures may be an unsafe or unsound practice.

Federal Savings Associations

(12 CFR 163.176)

In addition to the safety and soundness standards in 12 CFR 30, appendix A, II(E), 12 CFR 163.176 provides that FSAs must take the following actions:

- The board of directors or a committee of the board must review the FSA's interest-rate risk exposure and devise a policy for the FSA's management of that risk.
- The board must adopt a formal policy for the management of interest-rate risk. FSA management must establish guidelines and procedures to ensure that the board's policy is successfully implemented.
- FSA management must periodically report to the board regarding implementation of the FSA's policy for interest-rate risk management and must make that information available upon request of the OCC.
- The board must review the results of operations at least quarterly and shall make such adjustments as it considers necessary and appropriate to the policy for interest-rate risk management, including adjustments to the authorized acceptable level of interest-rate risk.

Covered Savings Associations

A covered savings association must comply with the requirements applicable to national banks.

Federal Reserve System/Federal Home Loan Bank Membership

National Banks

(12 USC 222 and 1424(a))

12 USC 222 requires national banks to be Federal Reserve System member banks. National banks may be members of the appropriate Federal Home Loan Banks. (12 USC 1424(a))

Federal Savings Associations

(12 USC 221 et seq., 1424, and 1464(f))

An FSA cannot be a member bank of the Federal Reserve System. FSAs nevertheless have access to nearly all Federal Reserve Bank services, including, for example, access to the discount window, use of the Federal Reserve Bank for the transfer of funds, and participation in Federal Reserve Bank check clearing and collection facilities. (12 USC 221 et seq.)

FSAs may be members of the appropriate Federal Home Loan Banks. (12 USC 1464(f) and 1424(a))

Covered Savings Associations

A covered savings association may be a member of the appropriate Federal Home Loan Bank. A covered savings association should check with the Federal Reserve Board for information on membership in the Federal Reserve System.

II. Insider Issues

Extensions of Credit to Insiders and Transactions With Affiliates (Regulation O and Regulation W)

(12 USC 371c, 371c-1, 375a, and 375b; 12 CFR 31, 215, and 223)

National banks, FSAs, and their insiders are subject to the insider lending restrictions and reporting requirements of 12 USC 375a and 375b, and 12 CFR 215 (Regulation O).¹⁴ (12 CFR 31.2)

Both national banks and FSAs are subject to the affiliate transaction requirements of 12 USC 371c and 371c-1 and 12 CFR 223 (Regulation W) (12 CFR 31.3).¹⁵ In addition, FSAs are subject to the following additional restrictions when engaging in transactions with affiliates:

- An FSA is prohibited from making a loan or extension of credit to an affiliate, unless the affiliate is engaged only in activities that the Federal Reserve Board, by regulation, has determined to be permissible for bank holding companies under 12 USC 1843(c); and
- An FSA is prohibited from purchasing or investing in securities issued by an affiliate, other than with respect to shares of a subsidiary. (12 USC 1468(a)(1) and 12 CFR 223.72(c))

Covered Savings Associations

A covered savings association must comply with Regulations O and W but should check with the Federal Reserve Board for the application of charter-specific provisions of the rules.

Employment Contracts

National Banks

At national banks, employment contract issues are governed by the safety and soundness standards of 12 USC 1818 and 12 CFR 30; the prohibition on unsafe and unsound compensation in appendix A to 12 CFR 30; and the prompt corrective action restrictions on compensation to senior executive officers in 12 CFR 6.6(a)(3). Depending on the circumstances, the provisions of an employment contract may be an unsafe or unsound practice.

Federal Savings Associations (12 CFR 163.39)

12 CFR 163.39(a) provides that an FSA may enter into an employment contract with its officers and other employees only in accordance with the regulation's requirements. Specifically, all

¹⁴ See 12 USC 1468(b), which provides that 12 USC 375a and 375b shall apply to every savings association in the same manner and to the same extent as if the savings association were a member bank.

¹⁵ See 12 USC 1468(a), which generally provides that 12 USC 371c and 371c-1 shall apply to every savings association in the same manner and to the same extent as if the savings association were a member bank, but adds the two additional restrictions listed in the main text.

employment contracts must be in writing and approved by the board of directors. An FSA may not enter into an employment contract with any of its officers or other employees if such contract would constitute an unsafe or unsound practice. The making of such an employment contract would be an unsafe or unsound practice if such contract could lead to material financial loss or damage to the FSA or could interfere materially with the exercise by the members of its board of directors of their duty or discretion provided by law, charter, bylaw, or regulation as to the employment or termination of employment of an officer or employee of the FSA. This may occur, depending upon the circumstances of the case, where an employment contract provides for an excessive term.

See 12 CFR 163.39(b) for list of required provisions that each employment contract must contain.

FSA employment contracts also are governed by the safety and soundness standards of 12 USC 1818 and 12 CFR 30; the prohibition on unsafe and unsound compensation in appendix A to 12 CFR 30; and the prompt corrective action restrictions on compensation to senior executive officers in 12 CFR 6.6(a)(3).

Covered Savings Associations

A covered savings association must comply with the requirements applicable to national banks.

Conflicts of Interest

National Banks

National bank directors and officers are not subject to a general regulation regarding conflicts of interest. They do, however, owe a common law fiduciary duty of loyalty to the bank. The duty of loyalty requires directors and management to act in the best interest of the bank and to ensure that insiders do not abuse their positions by benefiting personally at the bank's expense. In general, a conflict of interest exists when the personal or business interests of insiders are inconsistent with the continued safe and sound operation of the bank or with a business opportunity of the institution. Insiders should avoid placing themselves in a position that creates a conflict of interest or the appearance of a conflict of interest. Management and members of the board must fully disclose any personal interest that they have in matters affecting the bank and must ensure that these business and personal relationships with the bank are always at arm's length. Disinterested directors should approve transactions involving the interests of other affiliated parties, and the interested party should abstain from voting and deliberating on any matter involving their own interest. See the "Insider Activities" booklet of the *Comptroller's Handbook* and *The Director's Book*.

National banks that are authorized to exercise fiduciary powers pursuant to 12 USC 92a are subject to limitations on conflicts of interest contained in 12 CFR 9.12.

Federal Savings Associations (12 CFR 163.200)

In addition to the common law fiduciary duty of loyalty (discussed in the section for national banks), FSAs are subject to a regulation governing conflicts of interest, 12 CFR 163.200. Pursuant to this rule, directors, officers, and employees of an FSA, as well as individuals who have the power to direct its management or policies or otherwise owe a fiduciary duty to the FSA

- must not advance their own personal or business interests, or those of others with whom they have a personal or business relationship, at the expense of the FSA; and
- must, if they have an interest in a matter or transaction before the board of directors,
 - disclose to the board all material nonprivileged information relevant to the board’s decision on the matter or transaction, including the existence, nature, and extent of the person’s interest and the facts known to the person as to the matter or transaction under consideration;
 - refrain from participating in the board’s discussion of the matter or transaction; and
 - recuse themselves from voting on the matter or transaction (if the person is a director).

Furthermore, FSAs that are authorized to exercise fiduciary powers pursuant to 12 USC 1464(n) are subject to limitations on conflicts of interest contained in 12 CFR 150.330–150.370.

Covered Savings Associations

A covered savings association is required to comply with the rules applicable to FSAs, including the common law duty of loyalty to the institution.

Usurpation of Corporate Opportunity

National Banks

Although national bank directors and officers are not subject to a regulation regarding usurpation of corporate opportunity, they do owe a fiduciary duty of loyalty to the bank (see the “Conflicts of Interest” discussion). Furthermore, the “usurpation of corporate opportunity” doctrine, a part of the duty of loyalty, prevents insiders from improperly taking business opportunities away from the bank. See the “Insider Activities” booklet of the *Comptroller’s Handbook* and *The Director’s Book*.

Federal Savings Associations (12 CFR 163.201)

Pursuant to 12 CFR 163.201, FSA directors, officers, or individuals who have the power to direct the management or policies or otherwise owe a fiduciary duty to the FSA must not take advantage of corporate opportunities belonging to the FSA. A corporate opportunity belongs to the FSA if

- the opportunity is within the corporate powers of the FSA or a subsidiary of the FSA; and

- the opportunity is of present or potential practical advantage to the FSA, either directly or through its subsidiary.

The OCC will not deem an individual to have taken advantage of a corporate opportunity belonging to the FSA if a disinterested and independent majority of the FSA's board of directors, after receiving a full and fair presentation of the matter, rejected the opportunity as a matter of sound business judgment.

In addition to complying with 12 CFR 163.201, FSA directors and officers also owe a common law fiduciary duty of loyalty to the FSA. See the national bank section of the "Conflicts of Interest" discussion for an explanation of common law fiduciary duty of loyalty. See also the "Insider Activities" booklet of the *Comptroller's Handbook* and *The Director's Book*.

Covered Savings Associations

A covered savings association is required to comply with rules applicable to FSAs, including the common law duty of loyalty to the institution.

Loan Procurement Fees

National Banks

National banks are not subject to a regulation regarding loan procurement fees. Depending on the circumstances, the payment of a procurement fee to a national bank director or officer could be an unsafe or unsound practice or a breach of fiduciary duty.

Federal Savings Associations (12 CFR 160.130)

Pursuant to 12 CFR 160.130, FSA directors, officers, or other persons having the power to direct the management or policies of an FSA must not receive, directly or indirectly, any commission, fee, or other compensation in connection with the procurement of any loan made by the FSA or a subsidiary of the FSA.

Covered Savings Associations

A covered savings association is required to comply with the rule applicable to FSAs.

III. Corporate Governance Issues

Indemnification

For administrative proceedings or civil actions initiated by a federal banking agency, national banks and FSAs are subject to the same rule; they may make or agree to make reasonable indemnification payments to an institution-affiliated party (IAP)¹⁶ only if such payments are consistent with the requirements of 12 CFR 359.5.¹⁷

As discussed below, however, there are differences in the rules for national banks and FSAs regarding indemnification payments for other types of actions.

National Banks (12 CFR 7.2014)

For administrative proceedings or civil actions not initiated by a federal banking agency, 12 CFR 7.2014 provides that a national bank may indemnify an IAP for damages and expenses in accordance with the law of the state in which the bank's main office is located, the law of the state where the bank's holding company is incorporated, or the relevant provisions of the Model Business Corporation Act or Delaware General Corporation Law, provided the payments are consistent with safe and sound banking practices. A national bank must designate in its bylaws the body of law selected for making the indemnification payments. A national bank is not required to obtain OCC non-objection for these indemnification payments.

Federal Savings Associations (12 CFR 145.121)

For actions not initiated by a federal banking agency, 12 CFR 145.121 provides that an FSA must indemnify any person against whom an action is brought or threatened because that person is or was a director, officer, or employee of the FSA¹⁸ for (1) any amount for which that person becomes liable under a judgment and (2) reasonable costs and expenses.

¹⁶ "IAP" is defined to include (1) a director, officer, employee, or controlling stockholder of, or agent for, a bank; (2) any other person who has filed or is required to file a change-in control notice; (3) any shareholder, joint venture partner, and any other person who participates in the conduct of the affairs of the bank; and (4) any independent contractor who knowingly or recklessly participates in certain actions. See 12 USC 1813(u) for additional details.

¹⁷ Generally, this regulation provides that an insured depository institution may make or agree to make reasonable indemnification payments to an officer, director, or employee if (1) the board of directors, in good faith, determines in writing that the person in question acted in good faith and in a manner he/she believed to be in the best interests of the institution; (2) the board of directors, in good faith, determines in writing that the payment of such expenses will not materially adversely affect the institution's safety and soundness; (3) the indemnification payments do not constitute "prohibited indemnification payments" under 12 CFR 359.1(l); and (4) the person agrees in writing to reimburse the institution, to the extent not covered by payments from insurance or bonds, for that portion of the advanced indemnification payments that subsequently become prohibited pursuant to 12 CFR 359.1(l). See 12 CFR 359.5 for additional details.

¹⁸ Note that 12 CFR 145.121 applies only to officers, directors, and employees, and not to all IAPs.

In all cases of indemnification other than a final judgment on the merits in his or her favor, a majority of the disinterested directors must determine that the individual was acting in good faith within the scope of his or her employment or authority as he or she could reasonably have perceived it under the circumstances and for a purpose he or she could reasonably have believed under the circumstances was in the best interests of the association or its members.

In all cases, however, the FSA must give its supervisory office at least 60 days' notice of its intention to make such indemnification. (See 12 CFR 145.121(c) for information that should be included in the notice.) The FSA may not pay the indemnification if the OCC objects to the payment, in writing, within the notice period.¹⁹

Covered Savings Associations

A covered savings association must comply with the rules applicable to FSAs.

Board Composition Requirements

National Banks

(12 USC 71a, 72, and 76; 12 CFR 7.2012)

Statutory requirements govern the number of directors of a national bank. The board must have at least five but not more than 25 members. The Comptroller may permit more than 25 members by order or regulation. (12 USC 71a)

In addition, the president (but not the chief executive officer) of the bank must be a member of the board. The board may elect a director other than the president to be chairman of the board. (12 USC 76 and 12 CFR 7.2012)

Each director, during his or her whole term of service, must be a U.S. citizen, and a majority of directors must have resided in the state, territory, or district in which the bank is located, or within 100 miles of that location, for at least one year immediately preceding their election and during their service. The Comptroller may waive the residency requirement and the citizenship requirement for a minority of directors. (12 USC 72)

Federal Savings Associations

(12 CFR 5.21(e) and (j)(2)(viii), 5.22(l)(2), and 163.33)

An FSA must have at least five but not more than 15 directors, unless the OCC approves a smaller or larger number of directors. The FSA's bylaws must state a specific number of directors, not a range. (12 CFR 5.21(e) [Federal Mutual Charter Section 7] and 5.21(j)(2)(viii)) for mutual FSAs and 12 CFR 5.22(l)(2) for stock FSAs)

¹⁹ The OCC notes that an FSA that had a bylaw in effect relating to indemnification of its personnel before the 1969 implementation date of the indemnification regulation is governed solely by that bylaw.

12 CFR 163.33 requires that the board of directors of an FSA be composed as follows:

- A majority of the directors must not be salaried officers or employees of the FSA or of any subsidiary.
- Not more than two directors may be members of the same immediate family.
- Not more than one director may be an attorney with a particular law firm.

An FSA's board of directors is not subject to citizenship and residence requirements.

Covered Savings Associations

A covered savings association must comply with the requirements applicable to FSAs.

Qualifying Shares or Membership

National Banks

(12 USC 72; 12 CFR 7.2005)

A national bank director must own a qualifying equity interest in a national bank or a company that has control of a national bank. The director must own the qualifying equity interest in his or her own right and meet a certain minimum threshold ownership. See 12 CFR 7.2005 for the types of ownership that satisfy these requirements.

Federal Savings Associations

(12 CFR 5.22(l)(1) [stock FSAs] and 5.21(j)(2)(viii) [mutual FSAs])

A director of a stock FSA need not be a stockholder of the FSA unless the bylaws so require. A director of a mutual FSA must be a member of the FSA.

Covered Savings Associations

A covered savings association must comply with the requirements applicable to FSAs.

Corporate Title

National Banks

(12 USC 21a and 22, and 18 USC 709; 12 CFR 5.20(f)(2)(i)(F) and 5.42)

A national bank may not have a title that misrepresents the nature of the institution or the services it offers and must comply with applicable laws, including 18 USC 709, regarding false advertising and the misuse of a name to indicate a federal agency. The title of a national bank must include the word "national." (12 USC 22, and 12 CFR 5.20(f)(2)(i)(F) and 5.42.)

A national bank shall promptly notify the appropriate OCC licensing office if it changes its corporate title. A national bank whose corporate title is specified in its articles of association must amend its articles in accordance with 12 USC 21a. (12 CFR 5.42(d))

Federal Savings Associations (18 USC 709; 12 CFR 5.42)

The title of an FSA must comply with applicable laws, including 18 USC 709, regarding false advertising and the misuse of name to indicate a federal agency. There is no requirement that the title of an FSA include the word “federal.” An FSA must promptly notify the appropriate OCC licensing office if it changes its corporate title. An FSA must change its title by amending its charter in accordance with 12 CFR 5.21 (mutual FSAs) or 12 CFR 5.22 (stock FSAs).
(12 CFR 5.42)

Covered Savings Associations

A covered savings association must comply with the requirements applicable to FSAs.

Mutual Charter

National Banks

National banks may not be organized in mutual form nor have a mutual charter.

Federal Savings Associations (12 USC 1464; 12 CFR 5.21 and 144)

FSAs may be organized in mutual form. A federal mutual savings association does not issue capital stock and, therefore, has no shareholders. Federal mutual savings associations build capital almost exclusively through retained earnings. Holders of the federal mutual savings association’s savings, demand, and other authorized accounts are “members” of the mutual savings association. The federal mutual charter grants certain rights to mutual members.
(12 CFR 5.21)

Traditionally, federal mutual savings associations have been small, community- and consumer-focused institutions. They are required to comply with all rules and regulations that are applicable to stock FSAs, including capital requirements, compliance requirements, and restrictions on lending and investments, but they are very limited in their ability to raise capital without converting to stock form.

Covered Savings Associations

A federal mutual savings association may elect to be a covered savings association.

IV. Subsidiaries and Non-Controlling Investments

National banks are authorized to invest in operating subsidiaries, bank service companies, financial subsidiaries, and non-controlling investments. FSAs are authorized to invest in operating subsidiaries, bank service companies, service corporations, and pass-through investments. Because there are differences in the activities that national banks and FSAs may engage in directly, the permissible activities of their subsidiaries may also differ.²⁰

Operating Subsidiaries

National Banks (12 CFR 5.34)

A national bank operating subsidiary may engage in activities that are permissible for a national bank to engage in directly either as part of, or incidental to, the business of banking, as determined by the OCC or otherwise under other statutory authority. An operating subsidiary in which a national bank may invest includes a corporation, limited liability company (LLC), limited partnership, or similar entity if

- the bank has the ability to control the management and operations of the subsidiary, and no other person or entity exercises effective operating control over the subsidiary or has the ability to influence the subsidiary's operations to an extent greater than that of the bank;
- the parent bank owns and controls more than 50 percent of the voting (or similar type of controlling) interest of the operating subsidiary, or the parent bank otherwise controls the operating subsidiary and no other party controls a percentage of the voting (or similar type of controlling) interest of the operating subsidiary greater than the bank's interest; and
- the operating subsidiary is consolidated with the bank under GAAP.

Federal Savings Associations (12 CFR 5.38)

An FSA operating subsidiary may engage in any activity that the FSA may conduct directly. An operating subsidiary in which an FSA may invest includes a corporation, LLC, limited partnership, or similar entity if

- the FSA has the ability to control the management and operations of the subsidiary, and no other person or entity exercises effective operating control over the subsidiary or has the ability to influence the subsidiary's operations to an extent greater than that of the FSA;
- the parent FSA owns and controls more than 50 percent of the voting (or similar type of controlling) interest of the operating subsidiary, or the parent FSA otherwise controls the operating subsidiary and no other party controls a percentage of the voting (or similar type of controlling) interest of the operating subsidiary greater than the FSA's interest; and
- the operating subsidiary is consolidated with the FSA under GAAP.

²⁰ It is possible that a national bank and an FSA investing in the same company may have different filing requirements with the OCC, depending on the authority used for the investment.

The FSA and its operating subsidiary are generally consolidated and treated as a unit for statutory and regulatory purposes.

Covered Savings Associations

A covered savings association must comply with the rules and requirements applicable to national banks.

Bank Service Companies

National Banks and Federal Savings Associations (12 USC 1464(c)(4)(B) and 1861 et seq.; 12 CFR 5.35)

National banks and FSAs are both authorized to invest in bank service companies under the Bank Service Company Act, 12 USC 1861 et seq.

- A bank service company is any corporation or LLC organized to provide services authorized by the Bank Service Company Act.
 - If the bank service company is a corporation, all of the capital stock must be owned by one or more insured depository institutions.
 - If the bank service company is an LLC, all of the members of the LLC must be one or more insured depository institutions.
- A national bank or FSA may invest in a bank service company that conducts activities described in 12 CFR 5.35(f)(3) and (f)(4) and activities (other than taking deposits) permissible for the national bank or FSA and other insured depository institution shareholders or members of the bank service company.²¹
- Notwithstanding any other limitation, other than the limitation on the amount of investment by an FSA in 12 USC 1464(c)(4)(B), a national bank or FSA may not invest more than 10 percent of its capital and surplus in a bank service company. In addition, a national bank's or FSA's total investments in all bank service companies may not exceed 5 percent of the bank's or FSA's total assets. (12 USC 1862)

A national bank or FSA that wants to invest in a bank service company must comply with the filing requirements of 12 CFR 5.35. A notice that is eligible for expedited review is deemed approved by the OCC as of the 30th day after the OCC receives the notice, unless the OCC

²¹ Authorized activities under 12 CFR 5.35(f)(3) include providing the following services only for depository institutions: check and deposit posting and sorting; computation and posting of interest and other credits and charges; preparation and mailing of checks, statements, notices, and similar items; or any other clerical, bookkeeping, accounting, statistical, or similar functions. Authorized activities under 12 CFR 5.35 (f)(4) include services (except deposit taking) that the Federal Reserve Board has determined, by regulation, to be permissible for a bank holding company under 12 USC 1843(c)(8). A national bank or FSA must obtain the approval of the Federal Reserve Board before investing in the equity of a bank service company that provides services authorized under 12 CFR 5.35(f)(4).

notifies the bank or FSA before that date that the filing is not eligible for expedited review or the expedited review process is extended.²²

Covered Savings Associations

A covered savings association is authorized to invest in bank service companies and must comply with the rules applicable to national banks.

Service Corporations

National Banks

National banks are not authorized to invest in service corporations.

Federal Savings Associations

(12 USC 1464(c)(4)(B); 12 CFR 5.59)

FSAs are authorized to invest in service corporations. FSA service corporations are authorized to engage in any activity that FSAs may conduct directly, except taking deposits (12 USC 1464(c)(4)(B) and 12 CFR 5.59). FSA service corporations also are authorized to perform a wide range of business and professional services; credit-related activities; consumer services; real estate-related services; securities activities, liquidity management, and coins; investments; community development and charitable activities; and activities conducted on behalf of a customer on an other than “as principal” basis (12 CFR 5.59(f)). FSA service corporations also are authorized to engage in any activities “reasonably incident to” activities specifically listed in 5.59(f)(1)–(f)(10). (12 CFR 5.59(f)(11))

A service corporation is any entity that satisfies all the requirements in 12 USC 1464(c)(4)(B) and 12 CFR 5.59, and that the investing FSA designates as a service corporation pursuant to 12 CFR 5.59. A service corporation may engage in any of the designated permissible service corporation activities listed in 12 CFR 5.59(f), subject to any applicable filing requirement under 12 CFR 5.59(h). In addition, an FSA may request OCC approval for a service corporation to engage in any other activity reasonably related to the activities of financial institutions. (12 CFR 5.59(e)(3))

- An FSA is not required to have any particular percentage ownership interest in a service corporation and does not need to have control of the service corporation.
- A first-tier service corporation must be organized in the state where the FSA’s home office is located and may only be owned by savings associations²³ with home offices in that state (these requirements do not apply to lower-tier entities of the service corporation).

²² A notice is eligible for expedited review if both of the following requirements are met: (1) The national bank or FSA is well capitalized and well managed as defined in 12 CFR 5.34(d) or 5.38(d), as applicable; and (2) The bank service company engages only in activities that are permissible for the bank service company under 12 USC 1864 and that are listed in 12 CFR 5.34(e)(5)(v) or 5.38(e)(5)(v), as applicable.

²³ This includes FSAs and state-chartered savings associations.

- Generally, an FSA may invest up to 3 percent of its assets in the capital stock, obligations, and other securities of service corporations. In general, any investment that would cause the FSA's investment, in the aggregate, to exceed 2 percent of the association's assets must serve primarily community, inner city, or community development purposes. See 12 CFR 5.59(g) for additional details on investment authority and the application of lending limit rules to service corporation investments.
- A service corporation application is eligible for expedited treatment if the FSA is well capitalized and well managed, and the service corporation engages only in one or more of the authorized activities listed in 12 CFR 5.59(f). A service corporation application that meets the criteria for expedited review is deemed approved by the OCC as of the 30th day after the filing is received by the OCC, unless the OCC notifies the applicant before that date that the filing is not eligible for expedited review under 12 CFR 5.13(a)(2).
- The capital treatment of a service corporation depends on whether it is an includable subsidiary. See 12 CFR 3 for additional details.
- FSAs and their service corporations are subject to a regulation governing their separate corporate identities (12 CFR 5.59(e)(8)). Each FSA and service corporation thereof must be operated in a manner that demonstrates to the public that each maintains a separate corporate existence. Each must operate so that
 - their respective business transactions, accounts, and records are not intermingled;
 - each observes the formalities of their separate corporate procedures;
 - each is held out to the public as a separate enterprise; and
 - unless the parent FSA has guaranteed a loan to the service corporation, all borrowings by the service corporation indicate that the FSA is not liable.

Covered Savings Associations

A covered savings association is not permitted to invest in service corporations.

Financial Subsidiaries

National Banks

(12 USC 24a; 12 CFR 5.39)

National banks are authorized to invest in financial subsidiaries. A financial subsidiary is any company that is controlled by one or more insured depository institutions, other than a subsidiary that

- engages solely in activities that national banks may engage in directly and that are conducted subject to the same terms and conditions that govern the conduct of the activities by national banks, or
- a national bank is specifically authorized to control by the express terms of a federal statute (other than section 5136A of the Revised Statutes) and not by implication or interpretation such as by section 25 of the Federal Reserve Act, section 25A of the Federal Reserve Act, or the Bank Service Company Act.

In general, a financial subsidiary may engage only in activities

- that are financial in nature or incidental to a financial activity, authorized pursuant to 12 USC 24a; and
- that may be conducted by an operating subsidiary pursuant to 12 CFR 5.34. (See 12 CFR 5.39(e) for additional details.)

A national bank may hold an interest in a financial subsidiary only if

- the national bank and all depository institution affiliates are well capitalized and well managed;
- the aggregate consolidated assets of all of a bank's financial subsidiaries do not exceed 45 percent of the parent bank's consolidated total assets, or \$50 billion, whichever is less;
- if the national bank is one of the 100 largest insured banks, the bank has at least one issue of outstanding long-term, unsecured debt that meets such standards of creditworthiness or other criteria as the Secretary of the Treasury and the Federal Reserve Board may jointly establish pursuant to 12 USC 24a; and
- the parent national bank and any insured depository institution affiliate have at least a "satisfactory" Community Reinvestment Act rating.

For purposes of determining regulatory capital, the national bank must deduct the aggregate amount of its outstanding equity investment, including retained earnings, in its financial subsidiaries from regulatory capital as provided in 12 CFR 3.22(a)(7). The national bank may not consolidate the assets and liabilities of a financial subsidiary with those of the bank.

There are consequences to national banks that fail to continue to meet the qualification requirements. (12 CFR 5.39(j))

Federal Savings Associations

FSAs are not authorized to invest in financial subsidiaries.

Covered Savings Associations

A covered savings association is authorized to invest in financial subsidiaries and must comply with rules applicable to national banks.

Non-Controlling Investments/Pass-Through Investments

National Banks (12 CFR 5.36)

A national bank may make a non-controlling investment, directly or through its operating subsidiary, in an enterprise²⁴ that engages in

- activities described at 12 CFR 5.34(e)(5)(v)²⁵ or
- activities that are substantially the same as that contained in published OCC precedent approving a non-controlling investment by a national bank or operating subsidiary.²⁶

Before making a non-controlling investment, a national bank must satisfy the following requirements:

- The national bank must be able to prevent the enterprise from engaging in activities that are not set forth in 12 CFR 5.34(e)(5)(v) or not contained in published OCC precedent; otherwise, the national bank must have the ability to withdraw its investment from the enterprise.
- The investment must be convenient and useful to the bank in carrying out its business and not merely a passive investment.
- The bank's loss exposure must be limited as a legal matter.
- The enterprise in which the bank is investing must agree to be subject to OCC supervision and examination, subject to functional regulation limitations.

See 12 CFR 5.36 for additional details on non-controlling investments and for information on notice and application filing requirements.

²⁴ An "enterprise" means any corporation, LLC, partnership, trust, or similar business entity. See 12 CFR 5.36(c)(1).

²⁵ This regulation describes the authorized activities for an operating subsidiary and includes activities such as making loans or other extensions of credit; selling money orders, savings bonds, and travelers checks; purchasing, selling, servicing, or warehousing loans; providing courier services between financial institutions; providing check guaranty, verification, and payment services; providing data processing for the bank or its affiliates; providing tax planning and preparation services; providing financial and transaction advice and assistance; etc. See 12 CFR 5.34(e)(5)(v) for a complete list of activities.

²⁶ The national bank must conduct the activities according to the same terms and conditions applicable to the activities covered by the precedent and the national bank must provide the citation to the applicable precedent.

Federal Savings Associations (12 CFR 5.58 and 160.32)

An FSA may make a pass-through investment, directly or through its operating subsidiary, in an enterprise²⁷ that engages in

- activities described at 12 CFR 5.38(e)(5)(v)²⁸ or
- activities that are substantially the same as that contained in published OCC or OTS precedent approving a pass-through investment by an FSA or operating subsidiary.²⁹

Before making a pass-through investment, an FSA must satisfy the following requirements:

- The FSA must be able to prevent the enterprise from engaging in activities that are not set forth in 12 CFR 5.38(e)(5)(v) or not contained in published OCC or OTS precedent. Otherwise, the FSA must have the ability to withdraw its investment from the enterprise.
- The investment must be convenient and useful to the FSA in carrying out its business and not merely a passive investment.
- The FSA's loss exposure must be limited as a legal matter.
- The enterprise in which the FSA is investing must agree to be subject to OCC supervision and examination, subject to functional regulation limitations.

See 12 CFR 5.58 for additional details on pass-through investments and for information on notice and application filing requirements.

Covered Savings Associations

A covered savings association may make non-controlling investments and must comply with applicable requirements applicable to national banks.

Branches and Agency Offices

National Banks

(12 USC 36(j), 1823(k), and 1831u(b)(1), (3), and (4); 12 CFR 5.30)

For national banks, the term “branch” includes “any branch bank, branch office, branch agency, additional office, or any branch place of business established by a national bank ... at which deposits are received, checks paid, or money lent” (12 CFR 5.30(d) and 12 USC 36(j)). The term

²⁷ An “enterprise” means any corporation, LLC, partnership, trust, or similar business entity. See 12 CFR 5.58(d)(1).

²⁸ This regulation describes the preapproved activities for an operating subsidiary and includes activities such as making loans or other extensions of credit; selling money orders and travelers checks; purchasing, selling, servicing, or warehousing loans; providing management consulting, operational advice, and services for other financial institutions; providing check payment services; and providing financial and transaction advice and assistance. See 12 CFR 5.38(e)(5)(v) for a complete list of activities.

²⁹ The FSA must conduct the activities according to the same terms and conditions applicable to the activities covered by the precedent, and the FSA must provide the citation to the applicable precedent.

branch includes staffed mobile facilities, messenger services, temporary facilities, and drop boxes. The term branch does not include ATMs, remote service units, loan production offices, trust offices, administrative offices, data processing offices, or any other offices that do not engage in branching activities (i.e., deposits received, checks paid, or money lent).

National banks are required to file an application and obtain OCC approval to establish branches. National banks may establish or acquire branches in their main office states (intrastate branches) to the same extent as state banks chartered by such states (12 CFR 5.30). National banks may establish interstate de novo branches in any state that permits the establishment of a branch by a bank chartered by such state, subject to applicable state law limitations. (12 USC 36(j), 1823(k), 1831u(b)(1), (3), and (4), and 12 CFR 5.30)

National banks generally may establish non-branch facilities without geographic limitation and without OCC approval. National banks generally may not conduct branching activities (receive deposits, pay checks, or lend money) at non-branch facilities. For example, a national bank may establish a loan production office but would not be authorized to disburse loan funds from that office.

Federal Savings Associations (12 USC 1464(r); 12 CFR 5.31 and 145.92)

For FSAs, HOLA does not provide a general definition of the term “branch.”³⁰ OCC regulations, however, define a “branch office” of an FSA as “any office other than [the] home office, agency office, administrative office, data processing office, or an electronic means or facility.” (12 CFR 145.92)

FSAs are authorized to establish “agency offices” to engage in one or more of the following activities: (1) servicing, originating, or approving loans or contracts; (2) managing or selling real estate owned by the FSA; and (3) conducting fiduciary activities or activities ancillary to the FSA’s fiduciary business. Subject to OCC approval, an FSA may request to engage in other services in an agency office, except for payment on savings accounts. (12 CFR 5.31(k))

FSAs are authorized to establish branches in any state unless the location would violate 12 USC 1464(r), 1467a(e)(3), or 1823(k)(4). See also 12 CFR 5.31 and 145.92.

Covered Savings Associations

A covered savings association may continue to operate any branch or agency that the covered savings association operated on the effective date of the election (12 CFR 101.4(b)). If an agency office engages in a national bank branching activity (receive deposits, pay checks, or lend money), however, these activities will be considered nonconforming activities. Covered savings association must divest, conform, or discontinue nonconforming activities. (12 CFR 101.5)

³⁰ HOLA does provide a definition of “branch” in section 5(m), which specifically pertains to the establishment of branches in Washington, D.C. (12 USC 1464(m)(2)). Prior approval is required for FSA branches established in Washington, D.C.

For all newly established branches and non-branch office locations, covered savings associations must comply with the rules applicable to establishment of national bank branches and non-branch offices, including applicable licensing requirements.