



BANKING ISSUANCE

Comptroller of the Currency
Administrator of National Banks

Type: Banking Circular

Subject: Purchases Of Loans
In Whole Or In Part-Participations

TO: Chief Executive Officers of all National Banks, Senior Officers of all Federal Branches and Agencies, Deputy Comptrollers, District Administrators and all Examining Personnel

SUMMARY

The purchase of loans and participations in loans may constitute an unsafe or unsound banking practice in the absence of satisfactory documentation, credit analysis, and other controls over risk.

REVISION OF CIRCULAR

The present Circular supersedes Banking Circular 181; issued on December 8, 1983.

SCOPE

This Circular describes prudent purchases of loans and loan participations. A participation, as distinguished from a multibank loan transaction (syndicated loan),¹ is an arrangement in which a bank makes a loan to a borrower and then sells all or a portion of that loan to a purchasing bank.² All documentation of the loan is drafted in the name of the selling bank. Generally, the purchasing bank's share of the participated loan is evidenced by a certificate which assigns an interest in the loan and any related collateral.

¹ This Circular was drafted to address safety and soundness concerns arising from the purchase of loans and participations in loans. Nevertheless, the practices outlined in this Circular are illustrative of those principles of prudent banking which generally apply to any multibank lending transaction. For example, a prudent member of a loan syndication would obtain full and timely credit information to conduct an informed and independent analysis of the credit in a manner consistent with its formal lending policies and procedures.

² For the purposes of this Circular, a "loan" includes any binding agreement to advance funds on the basis of an obligation to repay the funds.



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BACKGROUND

The purchase and sale of loans and participations in loans are established banking practices. These transactions serve legitimate needs of the buying and selling banks and the public interest. However, recent abuses have highlighted the need for the Office to remind banks of prudent banking practices for these transactions.

POLICY

The absence of satisfactory controls over risk may constitute an unsafe or unsound banking practice and thus cause for the OCC to seek appropriate corrective action through its administrative remedies. Satisfactory controls over the purchase of loans and participations in loans ordinarily include, but are not limited to, the following:

- written lending policies and procedures governing these transactions;
- an independent analysis of credit quality by the purchasing bank;
- agreement by the obligor to make full credit information available to the selling bank;
- agreement by the selling bank to provide available information on the obligor to the purchaser; and
- written documentation of recourse arrangements outlining the rights and obligations of each party.

Lending Policy and Procedures

Prudent purchases of loans, loan participations, and loan portfolios are governed by the credit principles and procedures embodied in the purchasing bank's formal lending policy. The policy ordinarily entails:

- complete analysis and documentation of the credit quality of obligations to be purchased;
- an analysis of the value and lien status of the collateral; and
- the maintenance of full credit information on the obligor during the term of the loan.

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Independent Credit Analysis

To make a prudent credit decision, a purchaser conducts an independent credit analysis to satisfy itself that a loan, loan participation, or loan portfolio is a credit which it would make directly. The nature and extent of the independent analysis is a function of the type of transaction at issue and the purchaser's lending policies and procedures. Where loans are purchased in bulk, for example, a prudent purchaser might assess the credit of the class of obligors rather than each obligor. **See generally Comptroller's Handbook for National Bank Examiners** at § 205 (guidelines on loan portfolio management).

The acceptance by a purchaser of a favorable analysis of a loan issued by the seller, a credit rating institution, or another entity does not satisfy the need to conduct an independent credit analysis. A prudent purchaser may, however, consider such analyses obtained from the seller and other sources as factors when independently assessing a loan.

A prudent purchaser needs full credit information on an obligor before a loan or participation is purchased to make an informed and independent evaluation of the credit. After the purchase is made, the purchaser also needs timely credit information to monitor the status of the credit. Such information can often be obtained from the seller. In some situations, however, the purchaser may be unable to conduct an informed and independent analysis with information furnished by the selling or servicing bank. In such cases, other sources of information are needed to conduct an independent credit analysis.

Transfers of Credit Information

(a) Prudent Transfer Agreements. The indirect relationship between the obligor and the purchaser makes it difficult for the purchaser to assess the quality of the loan without the cooperation of the selling or servicing bank. The purchaser ordinarily needs to obtain full credit information on the obligor from the selling or servicing bank at the outset and during the life of the participation to perform a continuing independent assessment of the credit. Thus, a prudent purchase or participation document would generally include an agreement by the selling or servicing bank to provide available credit information on the obligor to the purchasing bank on a continuing basis. To ensure that full credit information will be available to the seller, a loan document would ordinarily include an agreement by the obligor to furnish such information to the seller on a continuing basis.³

³ The Office does not intend to suggest that existing loan and participation agreements be



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The absence of prudent transfer agreements may affect a purchaser's ability to obtain, assess, and maintain sufficient credit information. Accordingly, the purchase of a loan or participation absent such transfer obligations may be viewed as an unsafe or unsound banking practice.

(b)Scope of prudent transfers. Prudent transfers of credit information are sufficient in scope so as to enable a purchaser to make an informed and independent credit decision. Thus, prudent transfers encompass full and timely⁴ financial and nonfinancial information bearing on the quality of a loan. Financial information ordinarily includes:

- accrual status;
- status of principal and interest payments;
- financial statements, collateral values, and lien status; and
- any factual information bearing on the continuing credit worthiness of the obligor.

Prudent transfers also include nonfinancial information bearing on creditworthiness. For example, any known changes in the obligor's corporate structure or management affecting the quality of a loan would generally be disclosed.

renegotiated where full credit information is being furnished. Nonetheless, the Office may take appropriate action in any case where less than full credit information is obtained.

⁴References to "full" and "timely" transfers of credit information are made herein to provide supervisory guidelines on safe and sound transfers of credit information. The guidelines describe the scope of transfers required for a purchaser to make an informed and independent credit decision. Apart from such supervisory considerations, use of the terms "full" and "timely" is not intended to suggest that the terms have particular legal significance; thus, other terms may be used. The drafting and negotiation of standards governing transfers of credit information is the responsibility of bank management and counsel.



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Ordinarily, full credit information is obtained on each obligor. Where loans are purchased in bulk, however, a prudent purchaser might obtain credit information on the class of obligors rather than each obligor.

Prudent transfers of full credit information do not encompass the release of information in violation of law. In particular, loan classification information and other examiner opinions are set forth in confidential reports of examination and documents relating thereto. Such materials and information derived from them may not be disclosed absent express written approval by the Comptroller of the Currency pursuant to 12 C.F.R. § 4.18(c). Unauthorized disclosures may also incur criminal penalties under 18 U.S.C. § 641. In contrast, the facts underlying examiners' loan criticisms would generally be furnished; a knowing misrepresentation of credit quality may constitute a violation of 18 U.S.C. § 1014.

Recourse Arrangements

Repurchase agreements are subject to the limitations of 12 U.S.C. § 84. Other direct or indirect recourse arrangements, written or oral, provided by the selling bank will be considered as extensions of credit to the selling bank subject to 12 U.S.C. § 84. See 12 C.F.R. §§ 32.104 and 32.107.

Prudent recourse arrangements are documented in writing and reflected on the books and records of both the buying and selling bank. The failure to properly record or document these arrangements may constitute a false entry, statement, report or representation in violation of 18 U.S.C. § 1005.

ORIGINATING OFFICE

Questions regarding this Circular may be directed to the Chief National Bank Examiner's Office, Commercial Examinations Division (202) 447-1165, and to the Legal Advisory Services Division (202) 874-5170.

H. Joe Selby
Senior Duty Comptroller
Bank Supervision

* References in this guidance to national banks or banks generally should be read to include federal savings associations (FSA). If statutes, regulations, or other OCC guidance is referenced herein, please consult those sources to determine applicability to FSAs. If you have questions about how to apply this guidance, please contact your OCC supervisory office.