

experience in implementing part 24 suggests that investments that otherwise meet the requirements of part 24 will receive the support of the communities benefited.

The OCC received several comments from banks in support of the proposed deletion of this requirement. These commenters echoed our statement in the preamble to the NPRM that most investments that otherwise meet the requirements of part 24 will receive the support of the communities benefited. In addition, the supporting commenters said that mandating community involvement may limit management's ability to realize its own business strategy.

The OCC received no comments voicing opposition to the proposed deletion of the community support requirement either banks or community groups. The final rule therefore deletes the community support requirement.

#### *Investment Limits (§ 24.4)*

Section 24.4 of the rule implements the investment limits imposed by 12 U.S.C. 24 (Eleventh). Under both the regulation and the statute, a national bank's aggregate public welfare investments may not exceed 5 percent of its capital and surplus, unless the bank is at least adequately capitalized and the OCC determines that a higher amount will pose no significant risk to the deposit insurance fund. In no case, however, may a bank's aggregate outstanding part 24 investments exceed 10 percent of its capital and surplus.<sup>9</sup>

The OCC proposed amending § 24.4 to clarify that a bank should follow generally accepted accounting principles (GAAP) when calculating the aggregate amount of its part 24 investments, unless otherwise directed or permitted in writing by the OCC for prudential or safety and soundness reasons. We received two comments on this proposal seeking a further explanation of this clarification.

National banks prepare statements and reports required to be filed with the OCC using accounting standards that are consistent with GAAP. Under GAAP, the valuation method applied to an investment in an entity depends on the nature of the investment<sup>10</sup> and the

degree of the investor's control reflected by the percentage that the investment represents in the entity. Generally, investments over 50 percent are fully consolidated; investments between 20 and 50 percent are valued according to the equity method; and investments under 20 percent may be valued at cost, unless the asset becomes permanently impaired. There are certain circumstances, however, when the application of a particular GAAP valuation method to a part 24 investment may lead to unintended results.

For example, if the equity method of GAAP is applied to a part 24 investment, the value of a bank's part 24 investment carried on the bank's books would be originally recorded at cost but subsequently adjusted periodically to reflect the bank's proportionate share of the investment's earnings or losses, and decreased by any cash dividends or similar distributions from the investment. The use of the equity method would mean that the valuation of the bank's part 24 investment would fluctuate with the profits and losses of the investment. As the investment's profits increase under the equity method, the carrying value of the bank's investment would also increase. Consequently, even if the bank's investment was within the part 24 investment limits when made, this increase in the carrying value under the equity method could cause the investment to later exceed the investment limits.

Conversely, if the part 24 investment incurred losses, the value of the bank's investment would decrease, which would permit the bank to make additional investments without exceeding the investment limit. Thus, although the equity method may better reflect the current value of the bank's investment, its application could limit the investment capacity of banks with the most profitable part 24 investment programs while, contrary to safety and soundness, increasing the investment capacity of banks that make unprofitable part 24 investments.

In such circumstances, it may be appropriate for a bank to use a different method to calculate the aggregate amount of its part 24 investments. For example, under the cost method, the actual cost of a bank's part 24 investment would be used in determining compliance with the

statutory investment limit. No further adjustments would be required. As a result, as long as the part 24 investment was within the investment limits when made (and assuming there has been no change in the bank's capital and surplus), a bank's compliance with these limits would be unaffected by profits or losses on the investment.

In order to provide flexibility where the application of a specific GAAP valuation method would be inappropriate, the final rule follows the proposal and amends § 24.4 to provide that a bank should follow GAAP when calculating the aggregate amount of its part 24 investments, unless otherwise directed or permitted in writing by the OCC for prudential or safety and soundness reasons.

#### *Public Welfare Self-Certification and Prior Approval Procedures (§ 24.5)*

An eligible national bank may make qualifying public welfare investments without prior notification to, or approval by, the OCC by submitting a self-certification letter to the OCC within 10 working days after it makes the investment. For all other investments under part 24, a national bank must submit an investment proposal application to the OCC for prior approval. Unless otherwise notified in writing by the OCC, the proposed investment is deemed approved 30 calendar days from the date on which the OCC receives the proposal application.<sup>11</sup>

To emphasize that eligible national banks are not required to seek prior approval of eligible public welfare investments, the NPRM proposed changing the title of § 24.5 to "Public welfare investment after-the-fact notice and prior approval procedures," and changed references in the section from "self-certification" to "after-the-fact notice." The OCC further proposed to simplify the part 24 investment notification processes and make them more consistent with the notification processes established under 12 CFR part 5 for certain equity investments. Under those provisions of part 5, a national bank's written after-the-fact notice of certain equity investments must set forth simply "a description, and the amount, of the bank's investment."<sup>12</sup>

The NPRM proposed revising § 24.5 to make it more consistent with the part 5 equity investment notification procedures and to remove unnecessary administrative impediments to national bank public welfare investments. Thus, the proposal provided that a national

is identical in all material respects to 24 (Eleventh) and does not require the demonstration of community support for an investment.

<sup>9</sup> As explained in § 24.1(d), national banks that make loans or investments that are designed primarily to promote the public welfare and that are authorized under provisions other than section 24 (Eleventh) may do so without regard to the provisions—including the capital limitations—of 24 (Eleventh) or part 24.

<sup>10</sup> For example, Statement of Financial Accounting Standards Board No. 115, *Accounting*

*for Certain Investments in Debt and Equity Securities*, identifies the categories among which national banks must divide their securities holdings as held-to-maturity, trading, and available-for-sale, and provides a different accounting treatment for each category.

<sup>11</sup> See 12 CFR 24.5 and 24.6.

<sup>12</sup> See 12 CFR 5.36(d)(2).