

result, certain entities could have been affiliates under Regulation W, but not affiliates under the OTS interim final rules. By adopting the FRB's definition of control, the OTS will conform its rules regarding the treatment of these securities.

Several regulations cross-reference the definition of "affiliate" at § 563.41. These rules include: 12 CFR 560.93(a) (loans to one borrower restrictions); 562.4 (regulatory reporting standards); and 563.142 (capital distributions). As a result of changes in this final rule, the coverage of these other rules also will change.¹⁴

2. Financial Subsidiaries

Regulation W defines affiliate to include a financial subsidiary of a member bank. 12 CFR 223.2(a)(8). A financial subsidiary generally is any subsidiary of a member bank that "engages, directly or indirectly, in any activity that national banks are not permitted to engage in directly or that is conducted on terms and conditions that differ from those that govern the conduct of such activity by national banks."¹⁵

In the preamble to the interim rule, OTS addressed whether a savings association subsidiary would be considered to be financial subsidiary and, thus, an affiliate under section 23A of the FRA. OTS concluded that there is no statutory or supervisory basis for applying affiliate restrictions to savings association subsidiaries by classifying them as financial subsidiaries. The one commenter who addressed this issue agreed with OTS's conclusion regarding financial subsidiaries.

For the reasons stated in the preamble to the interim rule, the final rule at § 563.41(b) continues to state that savings association subsidiaries do not meet the statutory definition of financial subsidiary. As a result, Regulation W references to financial subsidiaries do not apply.

of the company and, thus, address only direct purchases from an issuer rather than secondary market purchases (12 CFR 574.4(a)(2)(vi)); or (2) require the controlling person to also hold at least 10 percent of any class of voting stock or 25 percent any class of stock (12 CFR 574.4(b)(1)(i) and (ii), and 574.4(c)(2)).

¹⁴ The definition of "subsidiary" in OTS's loans to insider rule at 12 CFR 563.43(d) includes cross-references to the definitions of "control" and "subsidiary" in 12 CFR 563.41. OTS is examining whether it should revise § 563.43(d) to more closely follow the FRB's loan's to insiders rule at 12 CFR part 215, and may undertake a separate rulemaking proposing changes. To avoid confusion to the industry in the interim, OTS has not revised the substance of this definition.

¹⁵ 12 CFR 223.3(p). FRB has provided several exceptions to this definition.

B. Prohibition of Loans and Extensions of Credit to Affiliates Engaged in Non-Bank Holding Company Activities

As noted above, section 11 of the HOLA applies two prohibitions to a savings association's transactions with its affiliates in addition to the section 23A and 23B limitations. Commenters raised several issues regarding OTS's implementation of section 11(a)(1)(A) of the HOLA, which prohibits a savings association from making a loan or other extension of credit to an affiliate unless the affiliate is engaged only in activities that a bank holding company may conduct.

1. Reverse Repurchase Agreements

The interim rule retained a provision on repurchase agreements that was adopted in a final rule published August 13, 1998 (63 FR 43292). Specifically, the interim rule states that a purchase of assets that is subject to the affiliate's agreement to repurchase (reverse repurchase agreement)¹⁶ is a loan or extension of credit for the purposes of the section 11 loan prohibition. As a result, a savings association may not generally enter into reverse repurchase agreements with an affiliate that engages in non-bank holding company activities. The interim rule exempted certain agreements that involve United States Treasury securities and that meet other specified requirements. OTS specifically requested comment whether it should retain the repurchase agreement provisions.

Both commenters responded to this request. One urged OTS to delete the repurchase agreement prohibition. The commenter asserted that "loan or extension of credit," as used in section 11 of the HOLA, does not encompass reverse repurchase agreements. At a minimum, both commenters urged OTS to retain the current exemption for transactions in United States Treasury securities.

Upon further review, OTS has decided to delete the repurchase agreement prohibition. In the preamble to the 1998 rule, OTS noted that section 11 of the HOLA does not define "loan or other extension of credit," and does not compel a legal conclusion that purchases of assets that are subject to an affiliate's agreement to repurchase are, or are not, prohibited by statute.

While the text of section 11 does not "compel" either legal conclusion, upon further review, OTS now believes that

¹⁶ A sale of assets subject to an agreement to repurchase is known as a "reverse repurchase agreement" when a bank or thrift is the purchaser of the assets. See M. Stigum, *The Repo and Reverse Markets* 4 (1989).

other factors strongly suggest that Congress did not intend for such transactions to be included as loans or extensions of credit under this section. OTS has two bases for this conclusion.

First, the definition of "covered transaction" in section 23A of the FRA treats repurchase agreements as asset purchases, rather than as loans or extensions of credit. Specifically, section 23A(b)(7)(C) of the FRA defines purchases of assets to include "assets subject to an agreement to repurchase" rather than a loan or extension of credit under section 23A(b)(7)(A). Based upon the language of the statute, FRB staff has informally indicated that it considers reverse repurchase agreements to be purchases of assets and not extensions of credit.¹⁷

Second, the legislative history of the statutes governing thrift transactions with affiliates reinforces the conclusion that reverse repurchase agreements should not be treated as loans or extensions of credit under section 11(a)(1)(A). Before the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Public Law 101-73 (FIRREA), a savings association's transactions with affiliates were governed by section 408 of the National Housing Act (NHA). 12 U.S.C. 1730a. Under section 408(p) of the NHA, thrift transactions with affiliates engaged only in bank holding company activities were subject to sections 23A and 23B of the FRA. Section 408(d) of the NHA addressed transactions with affiliates engaged in non-bank holding company activities. This section specifically prohibited six types of transactions and, like current section 23A, listed loans and extensions of credit separately from the "purchase [of] securities or other assets or obligations under repurchase agreement from any affiliate." Compare section 408(d)(3) with (d)(4). The successor statute addressing transactions with affiliates engaged in non-bank holding company activities at section 11(a)(1)(A) of the HOLA, however, specifically prohibits only transactions within one of the original six categories—loans and extensions of credit. This suggests that Congress did not intend to prohibit transactions with affiliates that engage in non-bank holding companies activities to the extent that the transactions fell within one of the other five categories.

The 1998 rule on repurchase agreements treated reverse repurchase

¹⁷ As a general rule, the interim rule applies all Regulation W definitions to the additional section 11 prohibitions. The treatment of repurchase agreements was an exception to this general rule.