

agreements as loans because these transactions bear some of the economic characteristics of a loan.¹⁸ However, the typical reverse repurchase agreement structured in conformity with general market practices has economic attributes that distinguish it from other loans and extensions of credit. For example, such agreements typically involve an institution's purchase of a security, subject to an agreement by the counterparty to repurchase the same or a similar security at a fixed price at a later date. In these transactions, the "purchaser" of the securities takes title to the securities and can trade, sell or pledge the security during the term of the contract. The reverse repurchase agreement merely imposes a contractual obligation to deliver identical securities on the settlement date set by the contract. This unique feature makes it far more flexible than a standard collateralized loan, where the lender cannot obtain access to the collateral in the absence of a default.¹⁹

OTS may, of course, impose additional restrictions on transactions with affiliates under section 11(a)(4) of the HOLA if it determines that the restriction is necessary to protect the safety and soundness of savings associations. OTS believes that the quantitative limits, safety and soundness requirements, and low-quality asset prohibitions contained in section 23A, and the arms-length requirements in section 23B sufficiently address the safety and soundness concerns raised by repurchase agreements. To the extent that a particular savings association may attempt to evade the lending prohibition through artful restructuring of a prohibited loan as a reverse repurchase agreement, § 563.41(c)(1) (discussed below) provides OTS with sufficient authority to address the circumvention. Accordingly, the final rule treats reverse

repurchase agreements as purchases of assets, and not as extensions of credit.

2. Attribution of Transactions and Activities

a. Third-party Attribution Rule

Sections 23A(a)(2) and 23B(a)(3) of the FRA require a member bank (and, thus, a savings association) to treat a transaction with any person as a transaction with an affiliate to the extent that the proceeds are used for the benefit of, or transferred to, an affiliate.²⁰ The text of section 11(a)(1)(A) of the HOLA does not specify a similar third party attribution requirement for the loan prohibition, and OTS has declined to infer such a requirement. To clarify this matter, the interim rule specifically stated that a loan or extension of credit to a third party is not prohibited under section 11(a)(1)(A) of the HOLA "merely because proceeds of the transaction are used for the benefit of, or transferred to, an affiliate." Interim rule at § 563.41(c)(1).

The preamble to the interim rule noted that OTS may, nonetheless, attribute a loan to a third party to an affiliate, for example, where a savings association attempts to circumvent the loan prohibition through sham transactions.²¹ OTS requested comment whether it should include this additional guidance in the final rule. One commenter responded asserting that further guidance was not needed.

The final regulation continues to state that a loan or extension of credit to a third party is not prohibited under section 11(a)(1)(A) merely because proceeds of the transaction are used for the benefit of, or transferred to, an affiliate. However, OTS is concerned that savings associations and their affiliates may misinterpret this provision and incorrectly conclude that the third party attribution rule will not apply to the loan prohibition under any circumstances. Accordingly, OTS clarified the final rule to state that OTS may inform the savings association that a particular transaction is prohibited if OTS determines that the transaction is, in substance, a loan or extension of credit to an affiliate that is engaged in non-bank holding company activities, or OTS has other supervisory concerns concerning the transaction. OTS will make such a determination, for example, if a loan is a prearranged step in a series of transactions designed to channel funds to an affiliate engaged in

non-bank holding company activities, or is otherwise designed to circumvent the loan prohibition. If OTS determines that a particular transaction is prohibited it may direct the savings association to divest the loan, unwind the transaction, or take other appropriate action.

b. Attribution of Activities Among Affiliates

When OTS originally issued its transactions with affiliates rule in 1991, it considered whether a savings association would be barred from extending credit to an affiliate that directly engaged only in activities permissible for a bank holding company, but the affiliate owned or controlled subsidiaries engaged in impermissible activities. OTS determined that activities must be attributed from a subsidiary to a parent affiliate in a vertical ownership chain up to, but not including, a controlling holding company in the corporate structure.²² The preamble to the 1991 rule suggests that this attribution determination was intended to prevent savings associations from evading the section 11 loan prohibition by structuring transactions through "strawmen" affiliates.²³

OTS specifically requested comment whether this interpretation should be included in the final rule. One commenter urged OTS to withdraw the guidance.

Upon reconsideration, OTS has decided to withdraw its 1991 guidance. Section 11 does not specifically require the attribution of activities from affiliated subsidiaries to their parent companies and, in the absence of information suggesting that this interpretation is necessary to protect the safety and soundness of savings associations, OTS is disinclined to interpret section 11 in a way that imposes additional burdens on savings associations. Rather than unduly restrict all savings associations, OTS believes that it can best address attempts at circumvention on a case-by-case basis. As noted above, the final rule states that OTS may prohibit a transaction if it determines that the transaction is, in substance, a loan or extension of credit to an affiliate that is engaged in non-bank holding company activities or OTS has other supervisory concerns concerning the transaction. Under this provision, OTS will prohibit a loan, for example, if it is a prearranged step in a

¹⁸ The savings association transfers funds to the affiliate, expecting to be repaid when the company repurchases the assets. The purchased assets essentially amount to collateral because the savings association is required to return the assets at the time of repurchase. The savings association earns a pre-determined amount under the agreement. The principal risk to the savings association and the deposit insurance fund is credit risk—the possibility that the affiliate will default on its obligation to make the repurchase. These types of agreements are generally considered to be the functional equivalent of a loan. See amendments to Federal Financial Institution Examination Counsel Policy Statement on Repurchase Agreements of Depository Institutions with Securities Dealers and Others (FFIEC Policy Statement), 63 FR 6935 (Feb. 11, 1998).

¹⁹ In addition, the bankruptcy code permits the purchaser under the agreement to liquidate securities without being subject to an automatic stay or similar delay. 11 U.S.C. 362(b)(7).

²⁰ Regulation W addresses the "third party attribution rule" at 12 CFR 223.16 and 223.52(b).

²¹ 67 FR 77909, at 77914. Op. OTS Chief Counsel (Dec. 22, 1991) and Op. OTS Chief Counsel (Mar. 13, 1992).

²² 56 FR 34005, at 34009. See also, Op. OTS Chief Counsel (Nov. 13, 1990). Activities of a parent were not, however, attributed downward to its subsidiaries.

²³ See 56 FR 34005, at 34008. (Discussion of attribution of transactions).