Regulation O – Loans to Insiders

Community Bankers for Compliance School

LENDING

2016

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Regulation O

Section 1: Background

Purpose

Regulation O [12 C.F.R. § 215] was enacted as a deterrent to abusive insider lending behavior. Because executive officers, directors, and principal shareholders have the opportunity or potential to take advantage of their positions, strict lending restrictions were incorporated into bank regulations to prevent such occurrences.

The most recent change to this regulation was the issuance of an interim final rule establishing regulations for savings and loan holding companies (SLHCs). The rule was released August 12, 2011 and was in effect soon after when published in the *Federal Register*. Under Dodd-Frank, supervisory and rulemaking authority for SLHCs and their nondepository subsidiaries transferred from the Office of Thrift Supervision (OTS) to the Board on July 21, 2011.

Prior to the 2011 changes to this regulation, the most extensive change took place on December 11, 2006. At that time, the Federal Reserve Board (the regulator responsible for this regulation) published an "interim final rule" which was effective immediately. This change was prompted by section 601 of the Financial Services Regulatory Relief Act of 2006. The interim final rule became a final rule during 2007. The final rule and the interim final rule are identical.

Section 2: Definitions [12 C.F.R. § 215.2]

Affiliate. An affiliate is any company of which a bank is a subsidiary or any other subsidiary of that company.

Company. A company is any corporation, partnership, trust (business or otherwise), association, joint venture, pool syndicate, sole proprietorship, unincorporated organization, or any other form of business entity not specifically listed above. However, the term does not include:

- An insured depository institution (as defined in 12 U.S.C. § 1813); or
- A corporation of which the majority of the shares are owned by the United States or by any state.

Control of a company or bank. Control of a company or bank means that a person directly or indirectly, or acting through or in concert with one or more persons:

- Owns, controls, or has the power to vote 25 percent or more of any class of voting securities of the company or bank;
- Controls (in any manner) the election of a majority of the directors of the company or bank; or
- Has the power to exert a controlling influence over the management or policies of the bank.

In addition, a person is presumed to have control, including the power to exert a controlling influence over the management or policies of the bank, if:

- The person is
  - an executive officer or director of the bank; and
  - Directly or indirectly owns, controls, or has the power to vote more than 10 percent of any class of voting securities of the bank; or
- The person directly or indirectly
  - Owns, controls, or has the power to vote more than 10 percent of any class of voting stock of the bank; and
  - No other person owns, controls, or has the power to vote a greater percentage of the class of voting securities.

An individual is not considered to have control, including the power to exercise a controlling influence over the management or policies of a company or bank, solely by virtue of the individual's position as an officer or director of the company or bank.

The presumption of control discussed above can be rebutted by submitting to the appropriate federal banking agency written materials that, in the agency's judgment, demonstrate an absence of control.

Director. A director of a bank includes any director of a bank, whether or not he or she is receiving compensation.

An *advisory director* is not considered a director if the advisory director:

- Is not elected by the shareholders;
- Is not authorized to vote on board matters; and
- Provides only general advice to the board of directors (e.g., director emeritus).

Extensions of credit to a *director of an affiliate* of a bank are not subject to the general prohibitions, the prohibition on knowingly receiving unauthorized extensions of credit, and the recordkeeping requirements of this rule if the following criteria are met:

- The director of the affiliate is excluded, by resolution of the board of directors or by the bylaws of the bank, from participation in major policymaking functions of the bank and the director does not actually participate in such functions.
- The affiliate does not control the bank.
- As determined annually, the assets of the affiliate do not constitute more than 10 percent of the consolidated assets of the company that:
  - Controls the bank; and
  - Is not controlled by any other company.
- The director of the affiliate is not otherwise subject to the above-mentioned sections of the regulation.

To exclude a director of an affiliate from participation in major policymaking functions of the bank by the resolution of the board of directors or the bylaws of the bank, the bank may either:

- Include the director (by name or by title) in a list of persons excluded from participation in such functions; or
- Not include the director in a list of persons authorized (by name or by title) to participate in such functions.

Executive officer. An executive officer of a bank is any person who participates, or has the authority to participate (other than in the capacity of a director), in major policymaking functions of the bank, whether or not:

- The officer has an official title;
- The title designates the officer as an assistant; or
- The officer is serving without salary or other compensation.

Generally, the following are considered executive officers:

- Chairman of the board
- The president

- All vice presidents
- The cashier
- The secretary
- The treasurer of the bank

The only way to remove any of these individuals from "Executive Officer" status under the regulation is by:

- Excluding the officer (or person) by board resolution or bank bylaws from participating in major policymaking functions of the bank; and
- Assuring that the officer (person) does not actually participate in major policymaking functions of the bank.

The term is not intended to include persons who may have official titles and may exercise a certain measure of discretion in the performance of their duties, including discretion in the making of loans, but who do not participate in the determination of major policies of the bank or company and whose decisions are limited by policy standards fixed by the senior management of the bank or company.

For example, the term does not include a manager or assistant manager of a branch of a bank unless that individual participates, or is authorized to participate, in major policymaking functions of the bank or company.

Extensions of credit to an executive officer of an affiliate of a bank are not subject to the general prohibitions, the prohibition on knowingly receiving unauthorized extensions of credit, and the recordkeeping requirements of this rule if the following criteria are met:

- The executive officer of the affiliate is excluded, by resolution of the board of directors or by the bylaws of the bank, from participation in major policymaking functions of the bank and the executive officer does not actually participate in such functions.
- The affiliate does not control the bank.
- As determined annually, the assets of the affiliate do not constitute more than 10 percent of the consolidated assets of the company that:
    - Controls the bank; and
    - Is not controlled by any other company.

In these circumstances, the executive officer of the affiliate is not otherwise subject to the above-mentioned sections of the regulation.

To exclude an executive officer of an affiliate from participation in major policymaking functions of the bank by the resolution of the board of directors or the bylaws of the bank, the bank may either:

- Include the executive officer (by name or by title) in a list of persons excluded from participation in such functions; or

- Not include the executive officer in a list of persons authorized (by name or by title) to participate in such functions.

Immediate family. The immediate family is the spouse of an individual, the individual's minor children, and any of the individual's children, (including adults), residing within the individual's home. This definition has been included in Regulation O and has a bearing on the insider when an extension of credit has economic benefit to the director, executive officer, and/or principal shareholder.

Insider. An insider is any executive officer, director, principal shareholder, or their related interests.

Lending limit. The lending limit is equal to the legal lending limits of the bank.

- This amount is established by statute, and is currently 15 percent of the bank's unimpaired capital and unimpaired surplus in the case of loans not fully secured.
- An additional 10 percent of unimpaired capital and unimpaired surplus may be allowed when the loan is secured by readily marketable securities and other cited forms of collateral having a market value, as determined by reliable and continuously available price quotations, at least equal to the amount of the loan.
- State-chartered banks should review their state banking codes. Where state law establishes a lending limit for a state bank that is lower than the amount permitted in federal statutes, the lending limit established by applicable state laws is the lending limit for the state bank.

A bank's *unimpaired capital and unimpaired surplus* equals the sum of:

- Its Tier 1 and Tier 2 capital included in the bank's risk-based capital under the capital guidelines of the appropriate federal banking agency, based on the bank's most recent consolidated report of condition; and
- The balance of the bank's allowance for loan and lease losses not included in the bank's Tier 2 capital.

Pay an overdraft on an account. This means to pay an amount upon the order of an account holder in excess of funds on deposit in the account.

Person. This means an individual or a company.

Principal shareholder. A principal shareholder is a person (individual or company, other than an insured bank) that directly or indirectly; or acting through or in concert with one or more persons; owns, controls, or has the power to vote more than 10 percent of the voting stock of the bank. A principal shareholder of a bank does not include a company of which a bank is a subsidiary.

Shares owned or controlled by a member of an individual's immediate family are considered to be held by the individual.

Related interest. A related interest of a person is a company that is controlled by that person, a political or campaign committee that is controlled by that person, or the funds or services to be provided that will benefit that person.

Section 3: Extensions of Credit [12 C.F.R. § 215.3]

Regulation O defines an "extension of credit" in the broadest of terms to prevent circumvention of the intent of the law, as well as of the technical requirements of the regulation.

General Definition

An "extension of credit" is a making or renewal of any loan, a granting of a line of credit, or an extending of credit in any manner whatsoever. It includes the following:

1. A purchase under repurchase agreement of securities, other assets, or obligations
2. An advance by means of an overdraft, cash item, or otherwise
3. Issuance of a standby letter of credit (or other similar arrangement regardless of name or description) or an ineligible acceptance
4. An acquisition by discount, purchase, exchange, or otherwise of any note, draft, bill of exchange, or other evidence of indebtedness upon which an insider may be liable as maker, drawer, endorser, guarantor, or surety
5. An increase of an existing indebtedness, but not if the additional funds are advanced by the bank for its own protection for accrued interest or taxes, insurance, or other expenses incidental to the existing indebtedness
6. An advance of unearned salary or other unearned compensation for a period in excess of 30 days
7. Any other similar transaction as a result of which a person becomes obligated to pay money (or its equivalent) to a bank, whether the obligation arises directly or indirectly, or because of an endorsement on an obligation or otherwise, or by any means whatsoever

Exceptions

An "extension of credit" does not include the following:

1. An advance against accrued salary or other accrued compensation, or an advance for the payment of authorized travel or other expenses incurred or to be incurred on behalf of the bank
2. A receipt by a bank of a check deposited in or delivered to the bank in the usual course of business unless it results in the carrying of a cash item for or the granting of an overdraft (other than an inadvertent overdraft in a limited amount that is promptly repaid)
3. An acquisition of a note, draft, bill of exchange, or other evidence of indebtedness through:
    a. A merger or consolidation of banks or a similar transaction by which a bank acquires assets and assumes liabilities of another bank or similar organization

b. Foreclosure on collateral or similar proceeding for the protection of the bank, provided that such indebtedness is not held for a period of more than three years from the date of the acquisition, subject to extension by the appropriate federal banking agency for good cause

4. An endorsement or guarantee for the protection of a bank of any loan or other asset previously acquired by the bank in good faith or any indebtedness to a bank for the purpose of protecting the bank against loss or of giving financial assistance to it
5. Indebtedness of $15,000 or less arising from a bank credit card plan, check credit plan, or similar open-end credit plan, provided:
   a. The indebtedness does not involve prior individual clearance or approval by the bank other than for the purposes of determining authority to participate in the arrangement and compliance with any dollar limit under the arrangement; and
   b. The indebtedness is incurred under terms that are not more favorable than those offered to the general public
6. Indebtedness of $5,000 or less arising by reason of an interest-bearing overdraft credit plan
7. A discount of promissory notes, bills of exchange, conditional sales contracts, or similar paper without recourse (such as financing purchases of goods from a business owned by a bank director)

Non interest-bearing deposits to the credit of a bank are not considered loans, advances, or extensions of credit to the bank of deposit, nor is the giving of immediate credit to a bank upon uncollected items received in the ordinary course of business considered to be a loan, advance, or extension of credit to the depositing bank.

Timing

An extension of credit by a bank is considered to be made at the time the bank enters into a binding commitment to make the extension of credit.

Participations

A participation without recourse is considered to be an extension of credit by the participating bank, not by the originating bank.

Tangible Economic Benefit Rule

An extension of credit is considered made to an insider to the extent that the proceeds are transferred to the insider or are used for the tangible economic benefit of the insider.

An extension of credit is not considered made to an insider if both of the following conditions are met:

1. The credit is extended on terms that would satisfy the general standards set forth for extensions of credit to insiders.
2. The proceeds of the extension of credit are used in a bona fide transaction to acquire property, goods, or services from the insider.

Section 4: General Prohibitions [12 C.F.R. § 215.4]

Regulation O contains the following restrictions and prohibited practices regarding loans to insiders.

Terms and Creditworthiness

The terms of the extension of credit and the creditworthiness of all executive officers, directors, principal shareholders, or any related interest of the person must meet all of the following criteria:

- Follow credit underwriting procedures that are not less stringent than those prevailing at the time for comparable transactions with persons who are not employed by the bank
- Be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with persons who are not insiders of the bank
- Not involve more than the normal risk of repayment or present any other unfavorable risks or features

Exception

The above limits on terms for extensions of credit to insiders do not prohibit any extension of credit made under a benefit or compensation program that meets both of the following standards:

- Widely available to employees of the bank and, in the case of extensions of credit to an insider of its affiliates, is widely available to employees of the affiliates at which that person is an insider
- Does not give preference to any insider of the bank over other employees of the bank and, in the case of extensions of credit to an insider of its affiliates, does not give preference to any insider of its affiliates over other employees of the affiliates at which that person is an insider

Prior Approval Required

To assure that the institution monitors itself concerning preferential terms and comparable risk of repayment without imposing undue constraints on the insider borrowers, a scale or range of extensions of credit was developed to allow less substantial borrowers to be approved within the institution's day-to-day credit authority and all other credit to be approved by the board of directors.

Before extending credit to an insider of the institution or to any director of its holding company or another subsidiary of that holding company (or to their related interests) in an amount exceeding the higher of $25,000 or 5 percent of the institution's unimpaired capital and unimpaired surplus (but in no event more than $500,000), the following criteria must be met:

- The board of directors of the institution must approve such extension in advance by a majority vote.
- The insider must refrain from participating in the voting process either directly or indirectly. Participation in the discussion, or any attempt to influence the voting, by the board of directors regarding an extension of credit constitutes indirect participation in the voting by the board of directors on an extension of credit.

Lines of Credit

To establish some practicality for this requirement, the regulation allows the institution to establish credit limits annually for each executive officer, director, and principal shareholder. If a line of credit has been approved (or re-approved) as outlined above within the last 14 months, an extension may be made under this line without prior board approval.

Individual Lending Limit

A single insider and his related interests are limited to the total amount of loans that may be extended to any single non-insider borrower and its related interests. In other words, insider loans are subject to the general individual lending limits that apply to all other loans.

This prohibition does not apply to an extension of credit by a bank to a company of which the bank is a subsidiary or to any other subsidiary of that company.

Aggregate Lending Limit

In general, the aggregate amount of extensions of credit to all of an institution's insiders may not exceed the bank's unimpaired capital and unimpaired surplus.

A bank with deposits of less than $100,000,000 may increase the general aggregate lending limit to a level not to exceed two times the bank's unimpaired capital and unimpaired surplus by an annual resolution of its board of directors, if it meets all of the following:

1. The board of directors determines that such higher limit is consistent with prudent, safe and sound banking practices in light of the bank's experience in lending to its insiders, and is necessary to attract or retain directors or to prevent restricting the availability of credit in small communities.
2. The resolution sets forth the facts and reasoning on which the board of directors bases the finding, including the amount of the bank's lending to its insiders as a percentage of the

bank's unimpaired capital and unimpaired surplus as of the date of the resolution. (Raising the limit to 200 percent is not automatic. A lower limit may be sufficient.)

3. The bank meets or exceeds, on a fully phased-in basis, all applicable capital requirements established by the appropriate federal banking agency.
4. The bank received a satisfactory composite rating in its most recent report of examination.

A bank which has adopted a resolution authorizing a higher limit that later fails to meet the above requirements must not extend any additional credit (including a renewal of any existing extension of credit) to any insider of the bank or its affiliates unless the extension or renewal is consistent with the general limit of only the bank's unimpaired capital and unimpaired surplus.

If a state law establishes a lower limit for loans to one borrower than Regulation O, then the state law applies with regard to loans to a single insider as well.

Exceptions

The aggregate insider limit does not apply to the following:

1. Extensions of credit secured by a perfected security interest in bonds, notes, certificates of indebtedness, or Treasury bills of the United States or in other such obligations fully guaranteed as to principal and interest by the United States
2. Extensions of credit to or secured by unconditional takeout commitments or guarantees of any department, agency, bureau, board, commission, or establishment of the United States or any corporation wholly-owned directly or indirectly by the United States
3. Extensions of credit secured by a perfected security interest in a segregated deposit account in the lending bank
4. Extensions of credit arising from the discount of negotiable or non-negotiable installment consumer paper that is acquired from an insider and carries a full or partial recourse endorsement or guarantee by the insider, provided that all the following conditions are met:
    a. The financial condition of each maker of such consumer paper is reasonably documented in the bank's files or known to its officers.
    b. An officer of the bank designated for that purpose by the board of directors of the bank certifies in writing that the bank is relying primarily on the responsibility of each maker for payment of the obligation and not on any endorsement or guarantee by the insider.
    c. The maker of the instrument is not an insider.

The first three exceptions apply only to the amounts of such extensions of credit that are secured in the manner described above.

While these loans do not have to be counted against the aggregate insider debt limit, they remain subject to other Regulation O requirements (such as being made on generally available terms, not involving more than normal risk, and being pre-approved by the board).

Overdrafts

A financial institution may not pay an overdraft of an account of an executive officer or director of the institution or its affiliates, except in accordance with one of the following:

- A written, pre-authorized, interest-bearing credit plan with a specified method of repayment
- A written, pre-authorized transfer of funds from another account of the accountholder at the institution

This overdraft prohibition does not apply to the payment by a bank of:

- An overdraft by a principal shareholder of the bank, unless the principal shareholder is also an executive officer or director
- An overdraft of a related interest of an executive officer, director, or principal shareholder of the bank or one of its affiliates
- An overdraft that is inadvertent, less than $l,000 in aggregate, paid within five business days or less, and is charged the same fees as for any other customer in similar circumstances

A negative balance on a zero-balance account is an overdraft and, therefore, an extension of credit, unless the negative balance qualifies as an inadvertent overdraft. This is not affected by the existence of funds in a second account of the accountholder, unless the bank has written authorization from the accountholder to charge the second account and that account is actually charged in the amount of the overdraft. However, a negative balance outstanding for 24 hours or less would not be considered an overdraft where funds are being automatically or electronically deposited or transferred.

A check drawn and paid against uncollected funds is neither an overdraft nor an extension of credit. However, it does become an extension of credit if it is returned to the bank uncollected and does not qualify as an inadvertent overdraft.

Section 5: Executive Officers [12 C.F.R. § 215.5]

Additional Restrictions on Loans to Executive Officers

Regulation O imposes a number of special limitations on extensions of credit by a bank to any of its executive officers, in addition to the general restrictions on extensions of credit to its insiders (and those of its affiliates). The restrictions of this section apply only to executive officers of the bank and not to executive officers of its affiliates.

Due to the influence and potential for abuse as an insider, even stricter control requirements have been developed for executive officers, while trying to allow as much flexibility as possible for typical credit needs. Generally, the determining factor is the purpose of the extension of credit.

No Limitations on Amount

A bank may extend credit to any executive officer of the bank in any amount if it is:

- To finance the education of the executive officer's children
- To finance or refinance the purchase, construction, maintenance, or improvement of a residence of the executive officer, provided all of the following criteria are met:
  - The extension of credit is secured by a first lien on the residence (therefore, an executive officer may only use this exemption for a first mortgage – home improvement loans or other subordinate liens are not covered by this portion of the regulation)
  - The residence is owned (or expected to be owned after the extension of credit) by the executive officer
  - In the case of a refinancing, only the amount used to repay the original extension of credit, (together with the closing costs of the refinancing), and any additional amount used for purchase, construction, maintenance, or improvement of a residence of the executive officer
- Secured by collateral that excludes it from the aggregate insider lending limit (see "Exceptions" in section 4 of this manual)

Limitations on Amount

Extensions of credit for any other purpose are allowable provided the total "other purpose" debt does not exceed the greater of 2.5 percent of the bank's unimpaired capital and unimpaired surplus or $25,000 but, in no event, more than $100,000.

Extensions of credit to partnerships made up of one or more executive officers (that individually or together hold a majority interest), are allowable provided that the total debt for any "other purpose" does not exceed the limit specified above. The total amount of credit extended to such a partnership is considered to be extended to each executive officer individually. This will have an impact on the aggregate lending limits of the bank and should be monitored to prevent inadvertent violations.

All extensions of credit to executive officers must be:

- Promptly reported to the board of directors (no later than the next board meeting)
- In compliance with the general prohibitions noted above
- Made only after submission of a detailed, current financial statement from the executive officer
- Made subject to the written condition that the institution has the right to call the loan at any time the officer's indebtedness to any other financial institution is greater than the loan limit for an executive officer at his or her own institution

Prohibition against Knowingly Receiving Unauthorized Extension of Credit [12 C.F.R. § 215.6]

Investigations into numerous bank and thrift failures revealed that a major contributor to weaknesses was often inappropriate and illegal insider activities. Therefore, Regulation O has a specific prohibition against any executive officer, director, and principal shareholder knowingly receiving or knowingly permitting any of that person's related interests to receive an extension of credit in violation of the regulation.

Extensions of Credit Outstanding on March 10, 1979 [12 C.F.R. § 215.7]

This section is being omitted from this presentation due to its limited relevance.

Section 6: Recordkeeping Requirements [12 C.F.R. § 215.8]

The bank must maintain certain records to document and support its compliance with the various requirements of Regulation O.

Bank Insiders

Each bank must maintain records that:

- Identify all of its executive officers, directors, principal shareholders, and their related interests through an annual survey. (Many banks not only take this step, but prepare and approve a board resolution detailing those in each of the categories.)
- Specify the amount and terms of each extension of credit to these persons and to their related interests.

These records must be updated at least annually by requesting current information from bank insiders.

Insiders of Affiliates

Each bank must obtain and maintain records of extensions of credit to insiders of its affiliates through one of the following three methods:

1. **Survey method**. This method identifies, through an annual survey, each insider of the bank's affiliates and maintains records of the amount and terms of each extension of credit by the bank to such insiders.
2. **Borrower inquiry method**. This method requires, as part of each extension of credit, that the borrower indicates whether he/she is an insider of an affiliate of the bank and maintains records that identify the amount and terms of each extension of credit by the bank to borrowers so identifying themselves.
3. **Alternative methods**. A bank may employ a recordkeeping method other than the survey or borrower inquiry method if the appropriate federal banking agency determines that the bank's method is at least as effective as the identified methods.

A bank that is prohibited by law or by an express resolution of its board of directors from making an extension of credit to any company or other entity that is covered by Regulation O, as a company, is not required to maintain any records of the related interests of the insiders of the bank or its affiliates or to inquire of borrowers whether they are related interests of the insiders of the bank or its affiliates. Such lenders include non-bank credit card institutions.

Other Records

No other records are required by the regulation (other than related to any public disclosures of insider loan information, discussed later), but the following may be necessary to retain in order to assure compliance with the requirements of the regulation:

- Lists of correspondent financial institutions
- Lists of the executive officer, directors, and principal shareholders of correspondent institutions, and their related interests
- Copies of board resolutions approving a list of executive officers

Disclosure of Credit from Banks to Executive Officers and Principal Shareholders [12 C.F.R. § 215.9]

This section has specific definitions, as follows:

- **Principal shareholder of a bank**. This means any person (other than an insured bank, or a foreign bank, as defined in 12 U.S.C. 3101(7)), that, directly or indirectly owns, controls, or has power to vote more than 10 percent of any class of voting securities of the member bank. The term includes a person that controls a principal shareholder (e.g., a person that controls a bank holding company). Shares of a bank (including a foreign bank), bank holding company, or other company owned or controlled by a member of an individual's immediate family are presumed to be owned or controlled by the individual for the purposes of determining principal shareholder status.
- **Related interest**. This means:
  - Any company controlled by a person; or
  - Any political or campaign committee where the funds or services of which will benefit a person or that is controlled by a person. For the purpose of this section, a related interest does not include a bank or a foreign bank (as defined in 12 U.S.C. 3101(7)).

Public Disclosure

Upon receipt of a written request from the public, a member bank shall make available the names of each of its executive officers and each of its principal shareholders to whom, or to whose related interests, the member bank had an outstanding (as of the end of the latest, previous quarter of the year) extension of credit that, when aggregated with all other outstanding extensions of credit at such time from the member bank to such person and to all related interests of such person, equaled or exceeded 5 percent of the member bank's capital and unimpaired surplus or $500,000, whichever amount is less. No disclosure under this paragraph is required if the aggregate amount of all extensions of credit outstanding at such time from the member bank to the executive officer or principal shareholder of the member bank, and to all related interests of such a person, does not exceed $25,000.

This disclosure does not require the member bank to disclose the specific amounts of individual extensions of credit.

Each member bank shall maintain records of all public requests for the information described above and the disposition of such requests. These records may be disposed of after two years from the date of the request.

Loans Secured by Institution Stock [12 C.F.R. § 215.10]

Executive officers and directors of financial institutions (whose stock is not publicly traded) must make an annual report to the board of directors of their institution. The report merely needs to state the amount of their outstanding credit that is secured by shares of the institution's stock.

Civil Penalties [12 C.F.R. § 215.11]

Any member bank, (or any officer, director, employee, agent, or other person participating in the conduct of the affairs of the bank), that violates any provision of this part (other than §215.9) is subject to civil penalties as specified in section 29 of the Federal Reserve Act (12 U.S.C. 504).

The regulation contains an appendix for National Banks only. The entire text of this appendix is included, as follows.

Appendix to Part 215–Section 5200 of the Revised Statutes Total Loans and Extensions of Credit

(a)

(1) The total loans and extensions of credit by a national banking association to a person outstanding at one time and not fully secured, as determined in a manner consistent with paragraph (2) of this subsection, by collateral having a market value at least equal to the amount of the loan or extension of credit) shall not exceed 15 per centum of the unimpaired capital and unimpaired surplus of the association.

(2) The total loans and extensions of credit by a national banking association to a person outstanding at one time and fully secured by readily marketable collateral having a market value, as determined by reliable and continuously available price quotations, at least equal to the amount of the funds outstanding shall not exceed 10 per centum of the unimpaired capital and unimpaired surplus of the association. This limitation shall be separate from, and in addition to, the limitations contained in paragraph (1) of this subsection.

Definitions

(b) For the purposes of this section

(1) the term "loans and extensions of credit" shall include all direct or indirect advances of funds to a person made on the basis of any obligation of that person to repay the funds or repayable from specific property pledged by or on behalf of the person, and to the extent specified by the Comptroller of the Currency, such term shall also include any liability of a national banking association to advance funds to or on behalf of a person pursuant to a contractual commitment; and

(2) the term "person" shall include an individual, sole proprietorship, partnership, joint venture, association, trust, estate, business trust, corporation, sovereign government or agency, instrumentality, or political subdivision thereof, or any similar entity or organization.

Exceptions

(c) The limitations contained in subsection (a) of this section shall be subject to the following exceptions:

(1) Loans (or extensions of credit) arising from the discount of commercial or business paper evidencing an obligation to the person negotiating it with recourse shall not be subject to any limitation based on capital and surplus.

(2) The purchase of bankers' acceptances of the kind described in section 372 of this title, and issued by other banks, shall not be subject to any limitation based on capital and surplus.

(3) Loans and extensions of credit secured by bills of lading, warehouse receipts, or similar documents transferring or securing title to readily marketable staples shall be subject to a limitation of 35 per centum of capital and surplus, in addition to the general limitations if the market value of the staples securing each additional loan or extension of credit at all times equals or exceeds 115 per centum of the outstanding amount of such loan or extension of credit. The staples shall be fully covered by insurance whenever it is customary to insure such staples.

(4) Loans or extensions of credit secured by bonds, notes, certificates of indebtedness, or Treasury bills of the United States, or by other such obligations fully guaranteed as to principal and interest by the United States, shall not be subject to any limitation based on capital and surplus.

(5) Loans or extensions of credit to (or secured by) unconditional takeout commitments or guarantees of any department, agency, bureau, board, commission, or establishment of the United States or any corporation wholly-owned directly or indirectly by the United States shall not be subject to any limitation based on capital and surplus.

(6) Loans or extensions of credit secured by a segregated deposit account in the lending bank shall not be subject to any limitation based on capital and surplus.

(7) Loans or extensions of credit to any financial institution or to any receiver, conservator, superintendent of banks, or other agent in charge of the business and property of such financial institution, when such loans or extensions of credit are approved by the Comptroller of the Currency, shall not be subject to any limitation based on capital and surplus.

(8)

(A) Loans and extensions of credit arising from the discount of negotiable or nonnegotiable installment consumer paper which carries a full recourse endorsement or unconditional guarantee by the person transferring the paper shall be subject under this section to a maximum limitation equal to 25 per centum of such capital and surplus, notwithstanding the collateral requirements set forth in subsection (a)(2) of this section.

(B) If the bank's files or the knowledge of its officers of the financial condition of each maker of such consumer paper is reasonably adequate, and an officer of the bank designated for that purpose by the board of directors of the bank certifies in writing that the bank is relying primarily upon the responsibility of each maker for payment of such loans or extensions of credit and not upon any full or partial recourse endorsement or guarantee by the transferor, the limitations of this section as to the loans or extensions of credit of each such maker shall be the sole applicable loan limitations.

(9)

(A) Loans and extensions of credit secured by shipping documents or instruments transferring or securing title covering livestock or giving a lien on livestock, when the market value of the livestock securing the obligation is not at any time less than 115 per centum of the face amount of the note covered, shall be subject under this section notwithstanding the collateral requirements set forth in subsection (a)(2) of this section, to a maximum limitation equal to 25 per centum of such capital and surplus.

(B) Loans and extensions of credit which arise from the discount by dealers in dairy cattle of paper given in payment for dairy cattle, which paper carries a full recourse endorsement or unconditional guarantee of the seller and which are secured by the cattle being sold, shall be subject under this section, notwithstanding the collateral requirements set forth in paragraph (a)(2) of this section, to a limitation of 25 per centum of such capital and surplus.

(10) Loans or extensions of credit to the Student Loan Marketing Association shall not be subject to any limitation based on capital and surplus.

Authority of Comptroller of the Currency

(d)

(1) The Comptroller of the Currency may prescribe rules and regulations to administer and carry out the purposes of this section, including rules or regulations to define or further define terms used in this section and to establish limits or requirements other than those specified in this section for particular classes or categories of loans or extensions of credit.

(2) The Comptroller of the Currency also shall have authority to determine when a loan putatively made to a person shall for purposes of this section be attributed to another person.

§215.12 Application to savings associations.

The requirements of this part apply to savings associations, as defined in 12 CFR 238.2(l) (including any subsidiary of a savings association), in the same manner and to the same extent as if the savings association were a member bank; provided that a savings association's unimpaired capital and unimpaired surplus will be determined under regulatory capital rules applicable to that savings association.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

SCOTT G. ALVAREZ
GENERAL COUNSEL

May 22, 2006

Douglas H. Jones, Esq.
Acting General Counsel
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, DC 20429

Dear Mr. Jones:

This is in response to your letter dated February 13, 2006, requesting clarification of the application of the Board's Regulation O (12 CFR part 215) to credit cards issued to bank insiders for the bank's business purposes. Specifically, you have asked whether and under what circumstances an insider's use of a bank-owned credit card would be deemed an extension of credit by the bank to the insider for purposes of Regulation O.

You have indicated that insiders of a bank often use a bank-owned credit card to purchase goods and services for the bank's business purposes. A bank-owned credit card is a credit card issued by a third-party financial institution to a bank to enable the bank (through its employees) to finance the purchase of goods and services for the bank's business. I understand that a bank that provides a bank-owned credit card to its employees typically forbids or discourages use of the card by employees for their personal purposes and that an employee who uses the card for personal purposes is obligated to promptly reimburse the bank. I also understand that the bank is liable to the card-issuing institution for all extensions of credit made under the card (whether for the bank's business purposes or for an employee's personal purposes).[1]

Although section 215.3(a) of Regulation O defines an extension of credit broadly to include "a making or renewal of a loan, a granting of a line of credit, or an extending of credit in any manner whatsoever," the rule also provides several important exceptions to the definition that are relevant to your inquiry. Section 215.3(b)(1) of Regulation O excludes from the definition of extension of credit any advance by a bank to an insider for the payment of authorized or other expenses incurred or to be incurred

[1] I also understand that some banks directly issue credit cards to their employees to enable the employees to finance the purchase of goods and services for the bank's business ("bank-issued credit cards"). The principles set forth in this letter with regard to bank-owned credit cards also would apply to bank-issued credit cards.

on behalf of the bank. Section 215.3(b)(5) of Regulation O excludes from the definition of extension of credit indebtedness of up to $15,000 incurred by an insider with a bank under an ordinary credit card.

In light of these provisions of the regulation and the purposes of the insider lending restrictions in the Federal Reserve Act, it is my opinion that a bank does not make an extension of credit to an insider for purposes of Regulation O at the time of issuance of a bank-owned credit card to the insider (regardless of whether the line of credit associated with the card is greater than $15,000). In addition, a bank does not extend credit to an insider for the purposes of Regulation O when the insider uses the card to purchase goods or services for the bank's business purposes. When an insider uses the card to purchase goods or services for the insider's personal purposes, however, the bank may be making an extension of credit to the insider. An extension of credit would occur for the purposes of Regulation O if (and to the extent that) the amount of outstanding personal charges made to the card, when aggregated with all other indebtedness of the insider that qualifies for the credit card exception in section 215.3(b)(5) of Regulation O, exceeds $15,000.

You also ask whether incidental personal expenses charged by an insider to a bank-owned credit card are per se violations of the market terms requirement in section 215.4(a) of Regulation O because non-insiders do not have access to this form of credit from the bank. Section 215.4(a) requires extensions of credit by a bank to its insiders to (i) be on substantially the same terms (including interest rates and collateral) as, and subject to credit underwriting standards that are not less stringent than, those prevailing at the time for comparable transactions with non-insiders; and (ii) not involve more than the normal risk of repayment or other features unfavorable to the bank.

A bank may be able to satisfy the market terms requirement, however, if the bank approves an insider for use of a bank-owned credit card only if the insider meets the bank's normal credit underwriting standards and the card does not have preferential terms (or the card does not have preferential terms in connection with uses of the card for personal purposes). Nonetheless, use of a bank-owned credit card by an insider for personal purposes may violate the market terms requirement of Regulation O if the card carries a lower interest rate or permits a longer repayment period than comparable consumer credit offered by the bank.

This opinion applies only to the specific issues and circumstances described above and does not address any other issues or circumstances. Please do not hesitate to call me if you have any additional questions concerning this matter.

Sincerely,

Section 9: Section 615 of the Dodd Frank Act

Summary

Section 615 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) imposes limitations on assets purchased from or sold to insiders. Under this section, a bank may not purchase an asset from, or sell an asset to, an executive officer, director, or principal shareholder of the bank, or any related interest of such person unless the transaction is on market terms and if the transaction represents more than 10 percent of the capital stock and surplus of the bank, the transaction must have prior approval from the bank's board of directors who do not have an interest in the transaction.

Effective Date

The amendments made by this section of the Dodd Frank Act were effective July 21, 2011.

Regulatory Text

SEC. 615. LIMITATIONS ON PURCHASES OF ASSETS FROM INSIDERS.

(a) AMENDMENT TO THE FEDERAL DEPOSIT INSURANCE ACT.

Section 18 of the Federal Deposit Insurance Act (12 U.S.C. 1828) is amended by adding at the end the following:

"(z) GENERAL PROHIBITION ON SALE OF ASSETS.

"(1) IN GENERAL. An insured depository institution may not purchase an asset from, or sell an asset to, an executive officer, director, or principal shareholder of the insured depository institution, or any related interest of such person (as such terms are defined in section 22(h) of Federal Reserve Act), unless

"(A) the transaction is on market terms; and

"(B) if the transaction represents more than 10 percent of the capital stock and surplus of the insured depository institution, the transaction has been approved in advance by a majority of the members of the board of directors of the insured depository institution who do not have an interest in the transaction.

"(2) RULEMAKING. The Board of Governors of the Federal Reserve System may issue such rules as may be necessary to define terms and to carry out the purposes this subsection.

Before proposing or adopting a rule under this paragraph, the Board of Governors of the Federal Reserve System shall consult with the Comptroller of the Currency and the Corporation as to the terms of the rule."

(b) AMENDMENTS TO THE FEDERAL RESERVE ACT. Section 22(d) of the Federal Reserve Act (12 U.S.C. 375) is amended to read as follows:

(d) [Reserved].

(c) EFFECTIVE DATE. The amendments made by this section shall take effect on the transfer date.

Section 10: Section 614 of the Dodd Frank Act

Summary

Section 614 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) extends the current limitations on transactions to insiders to include derivative transactions, repurchase agreements, reverse repurchase agreements, securities lending transactions, and securities borrowing transactions.

Effective Date

The amendments made by this section of the Dodd Frank Act will be effective July 21, 2012.

Regulatory Text

SEC. 614. LENDING LIMITS TO INSIDERS.

(a) EXTENSIONS OF CREDIT. Section 22(h)(9)(D)(i) of the Federal Reserve Act (12 U.S.C. 375b(9)(D)(i)) is amended

(1) by striking the period at the end and inserting "; or";

(2) by striking "a person" and inserting "the person";

(3) by striking "extends credit by making" and inserting the following: "extends credit to a person by

"(I) making"; and (4) by adding at the end the following:

"(II) having credit exposure to the person arising from a derivative transaction (as defined in section 5200(b) of the Revised Statutes of the United States (12 U.S.C. 84(b))), repurchase agreement, reverse repurchase agreement, securities lending transaction, or securities borrowing transaction between the member bank and the person.".

(b) EFFECTIVE DATE. The amendments made by this section shall take effect 1 year after the transfer date.