

September 29, 2020

MEMORANDUM TO: Board of Directors

FROM: Doreen R. Eberley, Director
Division of Risk Management Supervision

SUBJECT: **Notice of Proposed Rulemaking.** Removal of Transferred OTS Regulations Regarding Subordinate Organizations (Part 390, Subpart O)

Summary: Staff requests that the FDIC Board of Directors (Board) approve and authorize for publication in the *Federal Register*, with a 30-day public comment period, a notice of proposed rulemaking (NPR) to rescind and remove 12 CFR Part 390, Subpart O, entitled *Subordinate Organizations* (Subpart O).

Subpart O sets forth procedures by which State savings associations may establish or acquire a subsidiary, engage in new activities through an existing subsidiary, and exercise salvage power, in addition to providing requirement for subsidiary issuance of securities.

By rescinding Subpart O, the FDIC will eliminate redundant or otherwise unnecessary regulations and streamline FDIC regulations.

Concur:

Nicholas J. Podsiadly
General Counsel

I. Background

A. The Dodd-Frank Act

Effective July 21, 2011, section 311 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) transferred to the FDIC the powers, duties and functions formerly performed by the Office of Thrift Supervision (OTS) with respect to State savings associations. Section 316(b) of the Dodd-Frank Act provided that OTS regulatory issuances in effect as of the transfer date would continue in effect and be enforceable by the appropriate Federal banking agency until modified, terminated, set aside, or superseded.

On June 14, 2011, the Board approved a “List of OTS Regulations to be Enforced by the OCC and the FDIC Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act.”¹ When the transferred OTS regulations were subsequently published as new FDIC regulations, the FDIC specifically noted that staff would evaluate the transferred OTS regulations, and later incorporate the regulations into other FDIC rules, or amend or rescind the regulations, as appropriate.

Although Section 312 of the Dodd-Frank Act² granted the OCC rulemaking authority relating to both State and Federal savings associations, nothing in the Dodd-Frank Act affected the FDIC’s existing authority to issue regulations under the Federal Deposit Insurance Act (FDI Act) and other laws as the “appropriate Federal banking agency.” Section 312(c) of the Dodd-Frank Act amended the definition of “appropriate Federal banking agency” contained in section 3(q) of the FDI Act to add State savings associations to the list of entities for which the FDIC is designated the “appropriate Federal banking agency.”³ As a result, when the FDIC acts as the

¹ Pub. L. 111-203, 124 Stat. 1376 (2010).

² See 312(b)(2)(B)(i)(II).

³ *Id.*

“appropriate Federal banking agency” for State savings associations, it has the authority to issue, modify, and rescind regulations involving such institution.

B. Part 390, Subpart O – Subordinate Organizations

Subpart O was among the rules transferred to the FDIC from the OTS, and governs investments in, and activities of, subordinate organizations of State savings associations. The OTS rules, formerly found at 12 CFR Part 559, were transferred to the FDIC with nominal changes and are currently found at Part 390, Subpart O, *Subordinate Organizations*.⁴

II. Proposal to Rescind Part 390, Subpart O

Staff carefully reviewed Subpart O and determined that the procedures with respect to investments in, and activities of, subordinate organizations are substantially similar to requirements that a State savings association must satisfy under federal banking laws and regulations, specifically Part 362 of the FDIC Rules and Regulations,⁵ as well as State statutes. Two sections of this recommendation should be highlighted.

First, section 390.254 sets forth requirements for issuing securities through a subsidiary of a state savings association. Because State savings association subsidiaries are permitted to issue securities pursuant to section 28 of the FDI Act because the operating subsidiaries and service corporations of Federal savings associations are permitted to issue securities, subject to regulatory limitations, staff proposes in the NPR to remind State savings associations and subsidiaries that subsidiary issuances, like other permissible activities, are subject to the same restrictions or conditions imposed on the Federal savings association and must be conducted in the same manner in which an operating subsidiary or service corporation is authorized to issue such securities.

⁴ 12 CFR part 390, subpart O.

⁵ Part 362, Subparts C and D are applicable to State savings associations and subsidiaries.

Accordingly, a State savings association subsidiary should not state or imply that the securities it issues are covered by Federal deposit insurance, or issue any security the payment, maturity, or redemption of which may be accelerated upon the condition that the controlling State savings association is insolvent or has been placed into receivership, and for as long as any securities are outstanding, the controlling State savings association must maintain all records generated through each securities issuance in the ordinary course of business, including but not limited to a copy of the prospectus, offering circular, or similar document concerning such issuance, and make such records available for examination by the FDIC.

Second, section 390.255 generally permits a State savings association to notify the FDIC at least 30 days before making a contribution or a loan to a lower-tier entity (salvage investment) that exceeds the maximum amount otherwise permitted under law or regulation to exercise its power to salvage the underlying asset (typically, an outstanding loan).⁶

The salvage power doctrine was a long-held position of the OTS and its predecessor, the Federal Home Loan Bank Board (FHLBB),⁷ that a Federal savings association has inherent or implied authority to take whatever steps may be necessary to salvage an investment.⁸ When integrating the OTS regulations for Federal savings associations, the OCC adopted the position that a Federal savings association has inherent or implied authority to use salvage power,⁹ as

⁶ Without the salvage power provision, the maximum amount a State savings association would be permitted would be related the loans to one borrower limit (LTOB Limit), which is equivalent to the applicable state's legal lending limit.

⁷ A July 1941 legal opinion provided that savings associations had "an inherent power and a positive duty" to salvage an investment to protect the FSLIC insurance fund. FHLBB Op. G.C. B-50, Salvage Operations, July 1, 1941.

⁸ Salvage powers permit Federal savings association to take whatever steps necessary to salvage an investment, provided the steps taken are integral parts of a reasonable and bona fide salvage plan and do not contravene a specific legal prohibition. Comptrollers Handbook, Other Real Estate Owned, Version 1.1, August 2018 p. 18.

⁹ See 12 CFR 5.59(i). (Federal savings association permitted to exercise its salvage powers to make a salvage investment to a service corporation investment); see also, Comptroller's Handbook, Other Real Estate Owned (Federal savings association's salvage powers are derived from 12 CFR 160.30, General Lending and Investment Powers, and permit the acquisition, holding, and operation of OREO and the expenditure of additional funds in regard to OREO), <https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-handbook/files/other-real-estate-owned/index-other-real-estate-owned.html>, last visited 7/9/2020.

well as the position that the LTOB Limit is not a specific legal prohibition with respect to the salvage powers doctrine.¹⁰

Because a State savings association derives its powers, including salvage power, from its respective State chartering banking agency, there may be lack of uniformity among State LTOB Limits (or legal lending limit).¹¹ For these reasons, staff proposes that State savings associations apply to the FDIC for prior approval pursuant to section 362.11 before making a contribution or a loan to a lower-tier entity (salvage investment) that exceeds the maximum amount otherwise permitted under law or regulation to exercise its power to salvage the underlying asset to be consistent with State law. The applicant would be required to provide evidence that the State approved any exception over the LTOB limit.¹²

III. Recommendation

Based on the foregoing, staff recommends that the Board approve the attached Resolution to adopt and authorize the publication in the Federal Register of the referenced NPR for public comment.

Staff Contacts:

RMS
Don Hamm (202) 898-3528
Shelli Coffey (312) 382-7539

Legal
Suzanne Dawley (202) 898-6509
Karlyn Hunter (703) 562-2310

¹⁰ National banks and savings associations are subject to 12 CFR part 32, Lending Limits, but *see also* Comptroller's Handbook OREO (“(Note: The lending limit is not considered to be a specific legal prohibition within the meaning of the salvage powers doctrine.”))

¹¹ *See* 2007 WL 7112410, OTS RB 37-21, *Examination Handbook, Asset Quality, Section 211, LOANS TO ONE BORROWER*, December 13, 2007. *Rescinded by OCC Bulletin 2012-19, dated June 29, 2012.* (“[s]tate-chartered savings associations have similar authority under state law.”) *See also*, 1975 WL 171273, Office of Thrift Supervision, August 7, 1975 (“[i]n the case of a state-chartered institution, the application must be accompanied by an opinion of counsel that the action proposed is within the institution’s power.”) and 1975 WL 171331, Office of Thrift Supervision, December 19, 1975 (“[w]hether a state chartered association possesses similar salvage powers, [to a Federal savings association is] ... governed by the laws of the chartering jurisdiction.”)

¹² LTOB Limits are established by state law of each chartering authority, and LTOB Limits are not consistent from state to state. Some states allow waivers or modifications, while others do not. Part 362 does not authorize any insured State savings association to make investments or conduct activities that are not authorized or that are prohibited by either Federal or State law. 12 CFR 362.9(c).