State and local officials. (*See* 7 CFR part 3015, subpart V.)

Executive Order 12988

This proposed rule has been reviewed under Executive Order 12988, Civil Justice Reform. It is not intended to have retroactive effect. This rule would not preempt any State or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule. There are no administrative procedures which must be exhausted prior to a judicial challenge to the provisions of this rule.

Paperwork Reduction Act

This document contains no information collection or recordkeeping requirements under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*).

Regulatory Reform

This action is part of the President's Regulatory Reform Initiative, which, among other things, directs agencies to remove obsolete and unnecessary regulations and to find less burdensome ways to achieve regulatory goals.

List of Subjects in 9 CFR Part 101

Animal biologics.

Accordingly, 9 CFR part 101 would be amended as follows:

PART 101—DEFINITIONS

1. The authority citation for part 101 would be revised to read as follows:

Authority: 21 U.S.C. 151–159; 7 CFR 2.22, 2.80, and 371.2(d).

2. Section 101.2 would be amended by revising the term ''biological products'' to read as follows:

§ 101.2 Administrative terminology.

* * * * *

Biological products. The term ''biological products,'' also referred to in this subchapter as biologics, biologicals, or products, shall mean all viruses, serums, toxins (excluding substances that are selectively toxic to microorganisms, *e.g.,* antibiotics), or analogous products at any stage of production, shipment, distribution, or sale, which are intended for use in the treatment of animals and which act primarily through the direct stimulation, supplementation, enhancement, or modulation of the immune system or immune response. The term ''biological products'' includes but is not limited to vaccines, bacterins, allergens, antibodies, antitoxins, toxoids, immunostimulants, certain cytokines, antigenic or immunizing components of live organisms, and diagnostic components, that are of natural or synthetic origin, or that are derived from synthesizing or altering various substances or components of substances such as microorganisms, genes or genetic sequences, carbohydrates, proteins, antigens, allergens, or antibodies.

(1) The term analogous products shall include:

(a) Substances, at any stage of production, shipment, distribution, or sale, which are intended for use in the treatment of animals and which are similar in function to biological products in that they act, or are intended to act, through the stimulation, supplemention, enhancement, or modulation of the immune system or immune response, or

(b) Substances, at any stage of production, shipment, distribution, or sale, which are intended for use in the treatment of animals through the detection or measurement of antigens, antibodies, nucleic acids, or immunity, or

(c) Substances, at any stage of production, shipment, distribution, or sale, which resemble or are represented as biological products through appearance, packaging, labeling, claims (either oral or written), representations, or through any other means.

(2) The term ''treatment'' shall mean the prevention, diagnosis, management, or cure of diseases of animals.

* * * * *

§ 101.2 [Amended]

3. In § 101.2, the term ''Guidelines'' would be added in alphabetical order to read as follows:

* * * * *

Guidelines. Guidelines establish principles or practices related to test procedures, manufacturing practices, product standards, scientific protocols, labeling, and other technical or policy considerations. Guidelines contain procedures or standards of general applicability that are usually not regulatory in nature, but that are related to matters that fall under the Virus-Serum-Toxin Act. Guidelines issued by the agency include Veterinary Biologics Licensing Considerations, Memoranda, Notices, and Supplemental Assay Methods.

* * * * *

Done in Washington, DC, this 20th day of August 1996.

A. Strating,

Acting Administrator, Animal and Plant Health Inspection Service.

[FR Doc. 96–21556 Filed 8–22–96; 8:45 am]

BILLING CODE 3410–34–P

FEDERAL DEPOSIT INSURANCE CORPORATION

12 CFR Part 362

RIN 3064–AA29

Activities and Investments of Insured State Banks

AGENCY: Federal Deposit Insurance Corporation (FDIC).

ACTION: Proposed rule.

SUMMARY: The FDIC is proposing to amend its regulations governing the activities and investments of insured state banks. In general, subject to certain exceptions, insured state banks are prohibited from making equity investments of a type and in an amount that are not permissible for national banks or engaging as principal in activities of a type not permissible for national banks. The regulation requires banks to file with the FDIC their plan for the divestiture of any prohibited equity investments, establishes procedures regarding notices to the FDIC pertaining to excepted equity investments, delegates authority to act on notices, applications and divestiture plans, requires that banks provide certain information to the FDIC regarding existing insurance underwriting activities that the law allowed banks to continue, provides for application procedures to obtain consent to engage in otherwise impermissible activities, and establishes a number of exceptions to required consent. The proposed amendment substitutes a notice for an application when banks meet specified requirements for particular real estate, life insurance and annuity investment activities. If the FDIC does not object to the notice during the notice period, the bank may proceed with the planned investment activities.

DATES: Comments must be received by October 22, 1996.

ADDRESSES: Send comments to Jerry L. Langley, Executive Secretary, Federal Deposit Insurance Corporation, 550 17th Street N.W., Washington, D.C. 20429. Comments may be hand delivered to room F–402, 1776 F Street N.W., Washington, D.C. on business days between 8:30 a.m. and 5 p.m. Comments may be sent through facsimile to: (202) 898–3838 or by the Internet to: comments@fdic.gov. Comments will be available for inspection at the FDIC Public Information Center, room 100, 801 17th Street, N.W., Washington, D.C. on business days between 9:00 a.m. and 4:30 p.m.

FOR FURTHER INFORMATION CONTACT: Shirley K. Basse, Review Examiner,

(202) 898–6815, Division of Supervision, FDIC, 550 17th Street, N.W., Washington, D.C. 20429; Pamela E.F. LeCren, Senior Counsel, (202) 898-3730, Patrick J. McCarty, Counsel, (202) 898–8708 or Linda L. Stamp, Counsel, (202) 898–7310, Legal Division, FDIC, 550 17th Street, N.W., Washington, D.C. 20429.

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in part 362 has been approved by the Office of Management and Budget under control number 3064–0111 pursuant to section 3504(h) of the Paperwork Reduction Act (44 U.S.C. 3501 *et seq.*). Comments on the collection of information should be directed to the Office of Information and Regulatory Affairs, Office of Management and Budget, Washington, D.C. 20503, Attention: Desk officer for the Federal Deposit Insurance Corporation, with copies of such comments to be sent to Steven F. Hanft, Office of the Executive Secretary, room F–453, Federal Deposit Insurance Corporation, 550 17th Street, NW, Washington, D.C. 20429. The collection of information in this amended regulation is found in § 362.4(c)(3)(vi) and § 362.4(c)(3)(vii) and takes the form of a 60 day advance notice to be filed by an insured state bank that meets certain requirements and intends to: (1) invest, indirectly through a majority-owned subsidiary, in real estate investment activities; and/or (2) directly, or indirectly through a majority-owned subsidiary, invest in insurance products or annuity contracts. The information will allow the FDIC to properly discharge its responsibilities under section 24 of the Federal Deposit Insurance Corporation Act (12 U.S.C. 1831a). The information in the notices will be used by the FDIC to ensure compliance with the law, as part of the process of determining risk to the deposit insurance funds.

Notice to Indirectly Engage as Principal in Real Estate Investment Activities

Number of Respondents: 250.
Number of Responses Per Respondent: 1
Total Annual Responses: 250
Hours Per Response: 6
Total Annual Burden Hours: 1,500

Notice to Directly or Indirectly Acquire or Retain Life Insurance Products or Annuity Contracts

Number of Respondents: 60.
Number of Responses Per Respondent: 1.
Total Annual Responses: 60.
Hours Per Response: 4.
Total Annual Burden Hours: 240.

Background

On December 19, 1991, the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) (Pub. L. 102–242, 105 Stat. 2236) was signed into law. Section 303 of FDICIA added section 24 to the Federal Deposit Insurance Act (FDI Act), ''Activities of Insured State Banks'' (12 U.S.C. 1831a). With certain exceptions, section 24 of the Federal Deposit Insurance Act (FDI Act) limits the direct equity investments of state chartered insured banks to equity investments of a type and in an amount that are permissible for national banks. In addition, the statute prohibits an insured state bank from directly, or indirectly through a subsidiary, engaging as principal in any activity that is not permissible for a national bank unless the bank meets its capital requirements and the FDIC determines that the activity will not pose a significant risk to the deposit insurance fund. Section 24 provides that the FDIC may make such determinations by regulation or order. The statute requires that equity investments that do not conform to the new requirements must be divested no later than December 19, 1996 and requires that banks file certain notices with the FDIC concerning grandfathered investments.

Part 362 of the FDIC's regulations (12 CFR part 362) implements the provisions of section 24 of the FDI Act. Among other things, part 362 sets out application procedures whereby insured state banks may seek the FDIC's consent to engage in otherwise impermissible activities. The FDIC may impose such conditions and restrictions on the approval of any application as it deems necessary to prevent the conduct of the activity from posing a significant risk to the deposit insurance fund. Part 362 also provides for certain exceptions which allow adequately-capitalized insured state banks to engage in named activities without prior consent as the FDIC has determined that engaging in the activities in question does not present a significant risk to the insurance fund.

Between 1992 and April 30, 1996, the FDIC acted on 1156 applications, notices and divestiture plans under section 24 either by action of the Board of Directors or by the Division of Supervision pursuant to delegated authority. The majority of the filings were notices and divestiture plans. The applications submitted for Board action have for the most part involved indirect equity interests in real estate (i.e. a majority-owned subsidiary holds or would hold the real estate investment) and direct investments in life insurance policies and annuities. The FDIC has evaluated these applications with a view toward developing a proper balance between minimizing risk to the deposit insurance funds and allowing state banks to engage in real estate, insurance and annuity investment activities where otherwise permitted under state law.

Of the applications, notices and divestiture plans filed under section 24 and part 362, the Board acted on 34 applications to directly or indirectly initiate or continue as principal an impermissible activity, approving 31 applications. The Division of Supervision acted on a total of 1122 applications and/or notices which consisted of the following: 388 requests to directly or indirectly initiate or continue as principal in an impermissible activity; 460 notices regarding grandfathered investments in common or preferred stock or shares of an investment company (which includes plans for divestitures of the excess investments in the products); 272 divestiture plans regarding impermissible equity investments and impermissible activities; and 2 requests to retain an equity investment in an insurance underwriting department. Of these filings, 5 applications were denied either in whole or in part.

Based on the agency's experience with the applications to date, the FDIC proposes to amend part 362 to substitute a notice procedure for prior approval by application in the case of real estate investment, life insurance and annuity investment activities provided the banks meet certain conditions and restrictions. Under the proposed amendment, if the FDIC does not object to the notice within a maximum period of 90 days (60 days initial period plus 30 day optional extension), the bank may proceed with its investment activity as planned. The agency's experience to date with real estate, insurance and annuity investment activities is discussed below along with a discussion of the risks associated with these types of investment activities. A detailed discussion of the proposed notice provisions follows.

Real Estate Investment Activities

The circumstances under which national banks may hold equity investments in real estate are limited. If a particular real estate investment is permissible for a national bank, a state bank only needs to document that determination. If a particular real estate investment is not permissible for a national bank and a state bank wants to

engage in real estate investment activities (or continue to hold the real estate investment in the case of investments acquired before enactment of section 24 of the FDI Act), the bank must file an application with FDIC for consent. The FDIC may approve such applications if the investment is made through a majority-owned subsidiary, the institution is well capitalized and the FDIC determines that the activity does not pose a significant risk to the deposit insurance fund.

The FDIC approved 63 of 66 applications from December 1992 through April 30, 1996 involving real estate investment activities. The FDIC denied one application, approved one in part, and one bank withdrew its application. The real estate investment applications generally have fallen into three categories: (1) Requests for consent to hold real estate at the subsidiary level while liquidating the property where the bank expects that liquidation will be completed later than December 19, 1996; (2) requests for consent to continue to engage in real estate investment activity in a subsidiary, where such activities were initiated prior to enactment of section 24 of the FDI Act; and (3) requests for consent to initiate for the first time real estate investment activities through a majority-owned subsidiary.

The approved applications have involved investments which have ranged from less than 1% to over 70% of the bank's Tier 1 capital. The majority of the investments, however, involved investments of less than 10% of Tier 1 capital with only four applications involving investments exceeding 25% of Tier 1 capital. The applications filed with the FDIC have involved a range of real estate investments including holding residential properties, commercial properties, raw land, the development of both residential and commercial properties, and leasing of previously improved property. The applications FDIC approved included 21 residential properties, 29 commercial properties and 13 applications covering a mix of commercial and residential properties. The assets of the institutions that submitted approved applications ranged from $15 million to $6.7 billion. The institutions which have been approved to continue or commence new real estate investment activity primarily have had composite ratings of 1 or 2 ratings under the Uniform Financial Institution Rating System (UFIRS). However, 2 institutions were rated 3 and 2 institutions were rated 4. The 4-rated institutions submitted applications to continue an orderly divestiture of real estate investments after December 19, 1996. Of the approved applications, 6 were to conduct new real estate investment activities, while 54 were submitted to continue holding existing real estate or to hold existing real estate after December 19, 1996 in order to pursue an orderly liquidation. The remaining 3 approved applications asked for consent to continue existing holdings and conduct new real estate activities. One application was partially approved and partially denied. This application involved a bank that applied for consent to continue direct real estate activities and consent to continue indirect real estate investment activities through a subsidiary. The FDIC approved the application to continue the real estate investment activity through the subsidiary and denied the application for the bank to engage directly in real estate investment activities.

In connection with the review of the above described applications, the FDIC undertook to determine what risk, if any, real estate investments pose to banks and ultimately to the deposit insurance funds. After reviewing, among other things, whether and to what extent real estate investments have played a role in the failure of institutions, the FDIC determined that real estate investments can pose significant risks, and that if such activities are to be permitted, prudential constraints should be imposed to control the various risks posed to both a financial institution and the deposit insurance fund. The results of that review are summarized below.

Risks of Real Estate Investment Activities

Investments in real estate, at any stage of the development process, or even completed properties, generally can be characterized as risky in that there is a high degree of variability or uncertainty of returns on invested funds. The cyclical downturn in the real estate market in the late 1980s and early 1990s, and the impact of that downturn on financial institutions, provides an illustration of the market risk presented by real estate investment activities. In addition to the high degree of variability, real estate investments possess many risks that, while not entirely unique, are not readily comparable to typical equity investments (e.g. common stock). Real estate markets are, for the most part, localized; investments are normally not securitized; financial information flow is often poor; and the market is generally not very liquid.

Real estate investment activities can increase interest rate risk; optimum investment periods are typically long-term; real estate is relatively lacking in liquidity; and real estate is subject to specialized risks such as environmental liability. The experience and expertise of management is a critical factor, and there is much anecdotal evidence to suggest that the lack of adequate management creates a significant level of risk of loss.

Due to the higher risk evident in real estate investments relative to more traditional banking activities, federally-chartered banks traditionally have been prohibited from acquiring or holding real estate solely for investment purposes. (Real estate investment activities remain permissible activities for subsidiaries of federally-chartered thrift institutions.) State-chartered banks also were allowed to engage in real estate investment activities, if permitted by state law, without application to the FDIC until FDICIA required state-chartered banks and their subsidiaries to obtain permission from the FDIC to engage in activities, including real estate investment activities, that are otherwise not permissible for national banks or subsidiaries of national banks.

The function of an equity investor is to bear the economic risks of the venture. Economic risk is traditionally defined as the variability of returns on an investment. If a single investor undertakes a project alone, all the risk is borne by the investor. If investors participate in an investment through a vehicle such as corporate stock ownership, that stock grants its holders pro rata participation in control of that corporation, and in its profits and losses. If that corporation is liquidated, the investor has a residual interest in any unencumbered assets.

An investor typically will have a required rate of return based on the historical track record of a particular company and/or type of investment project. Market participants face a general trade-off: The riskier the project, the higher the required rate of return. A key aspect of that trade-off is the notion that a riskier project will entail a higher probability of significant losses for the investor. Assessments of the degree of risk will depend on factors affecting future returns such as cyclical economic developments, technological advances, structural market changes, and the project's sensitivity to financial market changes.

The actual return on an investment, however, will depend on developments beyond the investor's control. If the actual return is higher than the expected rate, the investor benefits. If the project falls short of expected returns, the investor suffers. At the extreme, an

investor can lose all or some of the original investment.

Investments in real estate ventures follow this pattern. In fact, equity investments in commercial real estate have long been considered fairly risky because of the uncertainties in the income stream they generate. Both commercial and residential real estate markets in the post- World War II period have been marked by large cyclical swings. Two of those cyclical periods (the mid-1970s and the late 1980s through early 1990s) involved massive overbuilding of commercial projects. That overbuilding resulted in sharp declines in commercial property prices and serious losses to many investors. The historical performance of the industry clearly demonstrates considerable risk for investors.

If an investment is made solely using the funds of an investor, the investor bears all the risk. However, if the project is partially financed by debt, the risks are shared with the lender. Nonetheless, the equity investor typically still bears the bulk of the variation in the risk and rewards of an investment. As a rule, the lender is compensated at an agreed amount (or formula in the case of a variable rate loan). The lender is paid—both interest and principal—before the equity investor/borrower receives any rewards or return of investment. Thus, any downside outcome is borne first by the equity investor. In properly underwritten loan arrangements the lender bears the economic risk of significant losses only in the case of significant negative outcomes. Since the legal priority of the debt holder is higher in a liquidation or bankruptcy than that of the equity holder, the debt holders are hurt if the investment entity has very limited resources. Of course, the borrower/equity investor receives all of the up-side potential returns from the investment.

While a leveraged investor has less of his/her own funds at stake, the use of borrowed funds to finance an investment greatly magnifies the variability of the returns to the equity investor. That is to say, leverage increases the risks involved. For instance, a small decline in income in an unleveraged investment may only mean less positive returns; to the leveraged investor, it may mean out of pocket losses, as debt service may have already absorbed any income generated by the project. Conversely, a small increase in generated income may just moderately increase the rate of return on an all equity investment but have a major positive effect on the highly leveraged investor.

The fact that most commercial real estate investments are highly leveraged also affects overall market volatility. For instance, high interest rates will lower the expected rate of return for highly leveraged investments which will, in turn, lower effective demand. Thus, prices offered for commercial real estate during periods of high interest rates typically are lowered. For example, to the extent that there was a ''credit crunch'' for commercial real estate in the early 1990s and lenders were unwilling to extend credit, diminished effective demand for a property could have resulted in the elimination of a broad class of potential investors, rather than simply a lower price being bid.

The economic viability of any investment in real estate ultimately depends on the economic demand for the services it provides. Thus, fluctuations in the economy in general are translated into uncertainties in the underlying economics of most real estate investments. National economic trends, regional developments, and even local economic developments will affect the volatility of returns. A traditional problem for real estate investors in that regard is that, when the economy as a whole reaches capacity during an economic expansion, they are one of the sectors seriously affected by the resulting run-up in interest rates.

Much of the uncertainty associated with real estate investment, however, comes from the nature of the production itself—how new supply is brought to market. Investments in the construction of real estate typically have a long gestation period; this long planning period is especially characteristic of large commercial development projects. Given the traditional cyclicality of the economy and financial markets, the economic prospects for an investment can change radically during that period, altering timing and terms of transactions.

Moreover, real estate investors also typically have trouble getting full information on current market conditions. Unlike highly organized markets where participants can easily obtain data on market developments such as price and supply considerations, information in the commercial real estate market is often difficult, or impossible, to obtain. Also inherent in the investment process for commercial real estate is the fact that the market is relatively illiquid—particularly for very large projects. Thus, instead of having numerous frequent transactions that incorporate the latest market information and ensure that prices reflect true economic value, markets can be thin and the timing of a sale or rental contract can affect the value of the underlying investments.

In addition to the inherent illiquidity of commercial real estate markets, transactions often are ''private deals'' in which the major parameters of the investment are not available to the public in general and, in particular, to rival developers. For instance, the costs of construction are a private transaction between the developer and his contractor. Likewise, gauging selling prices or rental income is difficult since: (1) There are no statistical data on transaction prices available as there are for single-family structures and (2) even if there were data available, it would be impossible to account for the many creative financing techniques involved in commercial sales and in rental agreements (e.g., tenant improvements and rent discounting).

Because of imperfect market information and the length of the production process, prices of existing structures are often artificially bid up in market upswings. That is, short-term shortages fuel speculative price increases. Speculative price increases (whether it be for raw land, developed construction sites, or completed buildings) typically encourage even more construction to take place, leading to additional future overbuilding relative to underlying demand.

In addition to the inherent cyclicality of real estate markets, several underlying factors create additional uncertainties in the investment process. Changes in tax laws will affect the profitability of real estate investments. For example, tax changes were a major consideration in the 1980s, but changes in depreciation allowances and in tax rates have been commonplace in the post-World War II era.

Another uncertainty is the effect of other governmental actions, especially in the area of regulations. A prime example is Federal mandates requiring clean-up of existing environmental hazards that imposed unexpected costs on investors at the time they were passed. Similar uncertainties result from state and local laws that effect real estate and how it can be developed. For instance, changes in environmental restrictions of new construction can add unexpected costs to a project or even bar its intended use. Similarly, a zoning change can positively or negatively affect investment prospects unexpectedly. All of these factors add to the uncertainty of returns and thereby increase the risk of the investment.

Two other considerations often play into increasing risks in real estate investment. First, the efficient execution of a real estate investment usually

requires a ''hands on'' approach by an experienced manager. This level of involvement is especially true of a construction project where developers have to deal with a wide variety of problems ranging from governmental approvals to sub-contractors and changing commodity markets. For an investment in developed real estate, maintenance problems, replacing lost tenants, and adjusting rents to retain tenants all must be addressed in an environment of ever changing market conditions.

Many equity investors solve these problems by ''hiring'' someone else to manage the investment. The experience of the 1980s shows that there are specific risks involved in separating ownership from management. For instance, many tax-oriented investors in the early 1980s arguably knew little about the basic economics of the investments they were undertaking. In a perfect world, ''passive'' investment would work just as efficiently as direct, active investment. In reality, investment outcomes are likely to be more uncertain for equity investors when someone else is making decisions that affect the ultimate return.

Finally, an issue that plays into long-run risks in real estate investment is the fact that real estate markets—especially commercial real estate markets—are affected by both national and local developments. Even if knowledge were more widespread within local real estate markets, it is difficult to track all the relevant parameters of the investment decision geographically. Most commercial real estate investments have both a local and national component because firms demanding commercial floor space are typically geographically mobile. For example, the developer of an industrial park would have to be concerned about how existing and future developments located in close proximity to the project might affect the returns on the investment. However, operating income and the ability to attract and keep tenants also can be affected by market conditions around the country.

A financial institution—like any other investor—faces substantial risks when it takes an equity position in a real estate venture. If the investment were a direct, all-equity venture, the institution would bear all of the substantial economic risks in this highly-cyclical industry. If the entity making the investment is highly leveraged, a completely new set of financial risks are incurred. A poor investment outcome can quickly wipe out the leveraged equity investment. Finally, the risks also can easily be magnified if—because of the form of investment or debt instrument—the equity investor is separated from the day-to-day economic and financial decisions affecting the prospects for the venture.

Conditions Imposed in Connection With Approvals of Real Estate Applications

In view of the risks identified with real estate investment activities, the statutory requirement that approval should not be granted unless the FDIC determines that the activity does not pose a significant risk to the fund, and the FDIC's loss experience relating to institutions that failed either partly or principally because of real estate investment activity, staff determined that a number of prudential constraints may be necessary to control the risk to the individual bank and to the deposit insurance fund before concluding that real estate investment activities do not present a significant risk to the fund.

To date the FDIC has evaluated a number of factors when acting on applications for consent to engage in real estate investment activities. Where appropriate, the FDIC has fashioned conditions designed to address potential risks that have been identified in the context of a given application. In evaluating an equity real estate investment activity application the FDIC has usually considered the type of proposed real estate investment activity to determine if the activity is unsuitable for an insured depository institution. The FDIC also has reviewed the proposed subsidiary structure and its management policies and practices to determine if a bank is adequately protected from litigation risk and analyzed capital adequacy to ensure that a bank first devotes sufficient capital to its more traditional banking activities. In conjunction with this evaluation, the FDIC has evaluated capital adequacy with respect to a bank's ''consolidated'' and ''bank only'' leverage and risk-based capital ratios. In doing so, the FDIC excluded all investments in real estate investment subsidiaries from capital in the ''bank only'' capital calculation. The FDIC has evaluated limitations on investment in a subsidiary engaging in real estate investment activities to assure that the maximum risk exposure is nominal; evaluated policies relating to extensions of credit to third parties for subsidiary-related transactions to determine if they protect the bank from concentrations of risk; and reviewed policies on engaging in transactions in which insiders are involved to determine if they protect the bank from potential insider abuse. In addition, the FDIC has reviewed policies relating to the conditioning of loans on the purchase of real estate from the subsidiary and the extending of credit by the bank to third parties for the purpose of acquiring real estate from its subsidiary to determine if they prevent undesirable tying relationships and to determine if they are adequate to ensure that sound credit underwriting is maintained. Finally, the FDIC has reviewed and evaluated management's particular expertise relative to the activities in question.

In every instance in which the FDIC has approved an application to conduct a real estate investment activity a number of conditions have been imposed for prudential reasons due to the unpredictability of returns and other risks which are inherent in real estate investment activities as well as to mitigate potential insider conflicts of interest and to reduce risk to the insurance fund. In short, the FDIC has determined on a case-by-case basis that the conduct of certain real estate investment activities by a majority-owned subsidiary of an insured state bank will not present a significant risk to the deposit insurance fund provided certain conditions are observed. The conditions which have been imposed as well as the purpose intended to be achieved by imposing the conditions are discussed below. Not every condition has been imposed in connection with each approval. The conditions have been imposed on a case-by-case basis in light of the particular facts.

Capital

Most of the approval orders have a condition concerning capital. Often the statutory requirement to meet and maintain adequate capital is restated. In some instances, banks applying to conduct real estate investment activities that entail more inherent risk, such as undertaking a development project, have been required to maintain capital that equals or exceeds the level required for ''well capitalized'' institutions as defined in Part 325 after deducting the bank's investment in any subsidiaries engaged in real estate investment activities. The capital deduction has not been imposed in most approvals of applications when the bank is liquidating existing real estate investments. Indirect real estate investment activities for purposes of the orders typically has been defined to include equity interests in the real estate subsidiary, debt obligations of the subsidiary held by the bank, bank guarantees of debt obligations issued by the subsidiary, and extensions of credit or commitments of credit to any third party for the purpose of making a direct investment in the subsidiary or making

an investment in any investment in which the subsidiary has an interest. The purpose of requiring the bank to be well-capitalized on a bank-only basis is to ensure the continued viability of the bank, if the investment in the subsidiary were to be lost. Such a calculation serves as an ''acid test'' of the worst-case impact a real estate investment activity would have on an institution's capital position in the event that an institution's entire real estate-related investment were to be dissipated.

In instances in which the capital deduction has been imposed the bank has been required to take the deduction for call report purposes including for purposes of prompt corrective action and risk based premiums, except that the deduction is not taken when determining whether the bank is critically under-capitalized.

Transactions with Affiliates

Another condition that FDIC frequently has imposed requires that transactions between a bank and its real estate subsidiary comply with the restrictions that would apply under sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c and 371c–1) as between a bank and its affiliate. Among other things, section 23A requires that a bank limit its covered transactions with affiliates to no more than 10% of the bank's capital for one affiliate and 20% of its capital for all affiliates. For the purposes of 23A, capital and surplus is defined as Tier 1 and Tier 2 capital included in an institution's risk-based capital under the capital guidelines of the appropriate Federal banking agency, based on the institution's most recent consolidated Report of Condition and Income filed under 12 U.S.C. 1817(a)(3) and the balance of an institution's allowance for loan and lease losses not included in its Tier 2 capital for purposes of the calculation of risk-based capital by the appropriate Federal banking agency. The effect of the section 23A restrictions is to also prohibit the bank and its subsidiary from purchasing low-quality assets from each other unless a commitment was made to purchase the asset before its acquisition by the affiliate, pursuant to an independent credit evaluation.

Section 23B generally requires that covered transactions between a bank and its affiliate (including the purchase of services or assets from an affiliate under contract) are entered into under terms that are substantially the same, or at least as favorable to the bank as those prevailing at the time for comparable transactions with or involving other nonaffiliated companies. Section 23B also generally requires that affiliates not purchase as fiduciary any securities or other assets from any affiliate unless such purchase is permitted under the instrument creating the fiduciary relationship, by court order or by law. In addition, section 23B prohibits affiliates from publishing any advertisement or entering into any agreement stating or suggesting that the bank is in any way responsible for the obligations of its affiliates.

FDIC has imposed the above restrictions to keep the transactions between the bank and the real estate investment subsidiary at arm's length and to limit the bank's investment in the subsidiary. In instances in which an application has involved continuing investment in a subsidiary that at the time of application exceeds these limits, the FDIC has usually modified the limitation to allow the excess investment while imposing the amount limits on future transactions. The FDIC often has made an exception for the collateral and amount limitations imposed on loans from the bank to facilitate the sale of the real estate investments held by the subsidiary, provided that the loans are consistent with safe and sound banking practices, do not present more than the normal degree of risk of repayment, and the credit is extended on terms and under circumstances, including credit standards, that are substantially the same, or at least as favorable to the bank as those prevailing at the time for comparable transactions.

Real Estate Subsidiary Structure and Operations

There are numerous benefits which flow from ensuring that a parent and its subsidiary maintain a separate corporate existence. Such separation insulates banks and the deposit insurance fund from undue risk and potential liability stemming from litigation. To protect against ''piercing the corporate veil'' between the subsidiary and parent, thus mitigating litigation risks, the FDIC usually has required that the bank conduct real estate investment activities in a majority-owned subsidiary which is adequately capitalized; is physically separate and distinct in its operations from the operations of the bank; maintains separate accounting and other corporate records; observes corporate formalities such as holding separate board of directors' meetings; maintains a board of directors with one or more independent, knowledgeable outside directors and management expertise capable of conducting activities in a safe and sound manner; contracts with the bank for any service on terms and conditions comparable to those available to or from independent entities; and conducts business pursuant to separate policies and procedures designed to inform customers and prospective customers of the subsidiary that it is a separate organization from the bank, including the placement of specific language on any debt instrument or contract with a third party disclosing that the bank itself is not responsible for payment or performance. The FDIC has recognized that requiring total separation of the management of the subsidiary from the bank's management could enhance the corporate separateness of the subsidiary. However, in keeping with the FDIC's review and analysis of the downside risks real estate investments pose when separating ownership from management, the Board typically has required only a minimum of one independent director. In addition, FDIC has considered the presence of one or more outside directors to be a helpful deterrent to potential insider abuse, an enhancement to diversity and expertise and an opportunity to augment decision-making with a counterbalancing perspective.

Investment Limits

In order to maintain proper diversification and to effectively control the concentration of credit and investment risk, FDIC has required banks to identify and aggregate loans made to third parties for the purpose of investment in real estate held by the bank's subsidiary with the bank's own real estate investment activities and included that figure in the bank's investment in the real estate subsidiary. Generally, the FDIC has limited the amount of real estate investment activity to the amount contemplated in the business plan submitted with the application and requires the bank to notify the FDIC in the event of any significant change in facts or circumstances. This condition is designed to limit the exposure from the real estate investment activity and allow the FDIC to evaluate any additional real estate investment activity when contemplated by the bank.

Lending to Third Parties

The FDIC has conditioned approvals of applications to conduct real estate investment activity by including limits on the extension of credit to third parties for a direct investment in a bank subsidiary engaged in real estate investment activity to further limit the exposure of the state bank to real estate investment.

Insiders

Limiting buying and selling by bank insiders also has been imposed as a condition to the approval of applications to conduct real estate investment activity. These conditions generally require that the bank's subsidiary not be permitted to engage directly or indirectly with insiders in transactions involving the subsidiary's real estate investment activities without the prior written consent of the FDIC. These restrictions are in addition to the constraints on lending to insiders imposed by Regulation O (12 CFR 337.3). The bank is expected to identify conflicts of interest and their resolution by the Board should be documented.

Fiduciary and Trust Restrictions

In order to maintain safe and sound underwriting standards, to reduce or preclude the potential for breaches of fiduciary duties, and to protect the bank and the deposit insurance fund, FDIC has imposed one or more of the following conditions: (1) That the bank not condition any loan on the purchase or rental of real estate from any subsidiary engaged in real estate investment activities; and (2) that the bank not purchase real estate from the subsidiary in its capacity as a trustee for any trust, unless expressly authorized by the trust instrument, court order, or state law.

On occasion, FDIC has imposed a condition that any potential conflict of interest be identified, appropriately resolved, if possible, and approved by the bank's board of directors prior to the consummation of any transaction. This condition is considered a reasonable approach to avoiding the risk of loss from conflicts of interest while providing the bank with flexibility in resolving any such issue.

Life Insurance Investments

The Office of the Comptroller of the Currency (OCC) has established certain general guidelines for national banks to use in determining whether they may legally purchase a particular insurance product. These guidelines are contained in an OCC Banking Circular (BC 249), issued May 9, 1991. That circular indicates that the authority for national banks to purchase and hold an interest in life insurance is found in 12 U.S.C. section 24 (seventh) which permits national banks to exercise all such incidental powers as shall be necessary to carry on the business of banking.[1] The circular indicates that the OCC has further delineated the scope of that authority through regulations, interpretive rulings, and letters addressing the use of life insurance for purposes incidental to banking. Although the circular leaves open the possibility that there may be other uses of life insurance that are ''incidental to banking'' (the circular says the purposes ''include'' those described in the circular), the circular clearly indicates that there is no authority under 12 U.S.C. 24 (seventh) for national banks to purchase life insurance for their own account as an investment. If an insured state bank wishes to purchase an insurance product that does not meet the guidelines contained in BC 249, that purchase is considered to be an activity that is not permissible for a national bank within the meaning of part 362. The purchase by the state bank would therefore not be permissible unless the bank meets its minimum capital requirements and the FDIC determines that there is no significant risk to the deposit insurance funds. Under current regulations the bank must make application for consent to make or retain the investment and the FDIC then makes a determination based on the facts and circumstances of the particular case.

[1] In one instance the circular cites to 12 U.S.C. section 24 (fifth) which authorizes national banks to elect or appoint directors and to employ bank officials.

The BC 249 provides two tests for national banks to use in determining whether they may legally purchase a particular insurance product. Test A relates to key-person life insurance. Under Test A the insurance coverage must closely approximate the risk of loss. Test B relates to life insurance as an employee benefit and provides that, based upon reasonable actuarial benefit and financial assumptions, the present value of the projected cash flow from the policy (insurance proceeds) must not substantially exceed the present value of the projected cost of the associated compensation or benefit program (employee benefits). Insurance as an estate planning benefit is specifically recognized, but only as part of a reasonable compensation agreement or benefit plan.

Insurance proceeds include projected death benefits, loans against the policy before the death of the insured to fund retirement payments, and any other withdrawals by the bank. The projected cost of employee benefits includes the bank's actual cost associated with the insurance policy (the periodic mortality charges, loads, surrender charges, administrative charges and other fees that are expected to be assessed against the policy's cash surrender value during the term of the policy) plus the projected amount of any retirement or other deferred benefit payments that are expected to be paid out to employees or their beneficiaries.

It is well established that certain types of insurance products are actually ''securities'' under the Federal securities laws. Certain life insurance policies—common names include universal life or variable life—are ''securities.'' Banks may have to hold these investments through a subsidiary, rather than directly. If the life insurance policy in question is considered to be a security, and it does not qualify under either Test A or Test B of OCC BC 249, then the life insurance policy must be held through a subsidiary of the bank as required under section 24 and part 362.

Risks Associated With Life Insurance Investments

A bank holding a life insurance contract as an investment is exposed to a variety of risks, most of which are similar in nature to the types of risks banks are exposed to on both sides of the balance sheet: credit risks, liquidity risks, and interest rate risks. In addition, there is actuarial risk inherent in holding a life insurance policy that exposes banks to different risks than are usual in the banking industry. Unless the issuing company becomes insolvent, a life insurance policy investment gives a bank the potential for low returns over the life of the investment, rather than loss of principal.

Banks purchase various forms of life insurance contracts as either key-person protection for the bank or as a compensation benefit for the employee. In certain instances, the policies provide a benefit to executive officers who are also majority stockholders in the form of an estate planning tool. Many of these policies require large single premiums or periodic premiums of a substantial amount. These premiums may result in the build-up of significant cash surrender or investment values that cannot be easily liquidated without adverse tax consequences.

Since life insurance products represent an unsecured obligation of the issuing company, there is some credit risk involved in these products. As the companies are regulated by state insurance commissioners without any federal regulatory oversight, there will be some variation in the strictness of the regulatory regimes from state to state. If a state insurance commissioner declares a firm to be insolvent, the holders may receive payments from (1) other insurance companies (the industry has, in some past events, supported the policies of failed firms in order to promote investor confidence.); (2) liquidation of the issuer's assets and sale of the firm; (3) lawsuits; and/or (4)

state insurance funds. The existence, structure, and coverage provided by these funds varies, however, they typically are not pre-funded and may ultimately be unable to provide the required support.

Unlike other types of investments, no secondary market for insurance products exists, making some liquidity risk inherent in these investments. Cashing out the policy can be costly because of the tax consequences. The illiquidity of the policies may be mitigated by two factors: (1) Many policies have provisions that permit the holder of the policy to borrow against the current cash value at a minimal interest rate, and (2) a bank moving toward insolvency holding an insurance policy will probably be able to offset other losses with the taxable income that is realized by cashing out the policy.

The interest rate risks inherent in an insurance policy will vary with each insurance contract. The build-up of cash value depends on the performance of the underlying investment portfolio. Individual portfolios often have different interest rate risk characteristics. Insurance companies may write whole life policies with a single interest rate applied to the cash buildup, making the interest rate risk very high. Other policies may give the insurance company flexibility in determining the applicable future interest rates. These policies present actuarial risks because the maturity date of an insurance policy held until the death benefit is paid is unknown at the time the investor purchases the policy. Prior to the death of the insured party, comparing the investment returns provided by such a policy with alternative investments requires the calculation of an actuarial estimate of the life expectancy of the insured party. Should the insured die prior to his/her estimated life expectancy, the beneficiary reaps an investment windfall. However, if the insured's life exceeds the actuarially determined life expectancy, the ultimate performance of the investment will suffer (relative to the returns that would have been realized from alternative investments undertaken at the time). Insurance companies control the variance of results by applying actuarial principles to large populations of insured individuals. A bank holding policies on a handful of former employees cannot control the variability of the returns.

Various supervisory concerns can arise when banks invest in insurance policies. These concerns include potential violations of laws and regulations, a less than adequate rate of return, the illiquid nature of the investment, the potential for substantial tax obligations, and concentration of investment risk.

The FDIC scrutinizes bank purchases of life insurance for three particular potential violations other than section 24. Where a bank purchases split-dollar insurance to provide a fringe benefit to an executive officer of a bank, the executive must either reimburse the bank or report as additional taxable income the economic value of the benefits (as determined by the IRS). Otherwise, a violation of Federal Reserve Board Regulation O may occur (12 CFR part 215).

When a bank's holding company or other affiliate is a beneficiary of a life insurance policy purchased by a bank, the holding company must pay for its beneficial share of the premiums and periodic costs of the policy in order to comply with sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c and 371c–1). If, net of such reimbursements, the present value of projected insurance proceeds substantially exceeds the present value of employee benefits, the insurance arrangement will fail to meet the BC 249 standards.

For those insurance arrangements that will provide compensation or other benefits to employees or their beneficiaries, the amount of such expected benefits must be quantified and not exceed reasonable compensation levels when combined with other forms of compensation provided to those employees. Section 39 of the FDI Act prohibits excessive compensation as an unsafe or unsound act.[2]

The propriety of investing large sums in a policy that, over time, may provide a less than adequate rate of return is a consideration. However, these assets should be viewed in the context of the bank's overall asset and liability structure and not viewed in isolation to determine if they pose a significant risk to the fund.

Supervisory concern may exist over the long-term, illiquid nature of those insurance policies that cannot realistically be liquidated at the option of the bank without incurring sizeable surrender charges and adverse tax consequences. Liquidity should not be judged in isolation from other assets of the bank. Liquidity concerns may be mitigated if the bank has the ability to borrow against the policies without incurring adverse tax consequences or surrender charges.

[2] 12 U.S.C. 1831p–1(c).

Banks generally do not pay federal income taxes on the increases in the cash value of an insurance policy as long as the bank holds the policy until the death of the insured. As a result, banks that intend to hold the policy until the insured's death normally do not record any deferred tax liability for accounting purposes. However, should the bank surrender the policy prior to the insured's death, the bank would incur taxable income if the cash value received exceeded the amount of premium paid. The cash value build-up over time could result in sizable income taxes should the policy be surrendered early.

Due to the liquidity, credit, and tax considerations, unduly large concentrations in investments in life insurance policies could result if a bank does not adopt prudent constraints on the amount of its exposures.

Life Insurance Applications

As of June 4, 1996, the FDIC had acted upon 106 applications by insured state banks for consent to continue to hold investments in life insurance policies. 101 of these applications involved policies acquired prior the effective date of the activities restrictions of section 24 of the FDI Act (December 19, 1992). Four banks had policies that were acquired after December 19, 1992, and one bank had a combination of policies acquired before and after the effective date. Of the 106 applications, almost two thirds (67) of the institutions were operating with a UFIRS composite rating of 2. Thirty (30) applications were from institutions that had composite ratings of 1, seven with a rating of 3, and two had a UFIRS composite rating of 4. None were 5 rated.

The insurance policies held by any one bank ranged from less than 1.0% of Tier 1 capital to 52% of Tier 1 capital. Over ninety percent (88 of 106) of the banks held investments totaling less than 30% of Tier 1 capital. However, 63 of the 106 applications involved an aggregate investment that did not exceed 20% of Tier 1 capital with the majority (45 of 63) of those investments representing less than 10% of Tier 1 capital.

All of the applications were approved. The actions were taken either by the FDIC Board of Directors or by the Director of the Division of Supervision pursuant to delegated authority.

The FDIC required all of the banks receiving approval to adhere to specific conditions deemed necessary to limit the risk to the banks and thus the insurance fund. Among the conditions were: (1) that the bank continue to meet applicable capital standards, (2) that the

bank shall notify the FDIC of any significant changes in the facts or circumstances on which the approval was based, (3) that the bank may not modify the terms or conditions of the policies (except for redemption of same) without the prior written consent of the FDIC, (4) that the bank may not acquire any additional life insurance policies without prior written consent of the FDIC, (5) that the bank must reduce the cash surrender value of the policies, (6) that the bank must receive approval of its applicable state authority, (7) that the bank may not pay additional annual premiums without consent of the FDIC, and (8) that the timing and amounts of the holding company's proportionate share of overall insurance costs will be made in a manner which will preclude any violations of section 23A or 23B of the Federal Reserve Act. Some or all of these conditions were imposed where the facts warranted the imposition of the particular condition in order to protect the deposit insurance fund from risk.

Annuity Contracts

Interpretative guidance issued by the OCC states that national banks are not permitted to invest in annuities for their own account. If an insured state bank wishes to purchase an annuity contract, the purchase is considered an activity that is not permissible for a national bank and section 24 of the FDI Act applies. The purchase by the state bank would therefore not be permissible unless the bank meets it minimum capital requirements and the FDIC determines that there is no significant risk to the deposit insurance funds.

As noted above, certain types of life insurance policies and annuity contracts are considered to be ''securities'' under the federal securities laws. If the annuity contract in question is considered to be a security, and this would apply to variable rate annuity contracts, it must be held through a subsidiary of the bank as required under section 24 and part 362. Fixed rate annuity contracts are considered to be insurance products and may be held directly by the bank.

A bank holding annuity contracts in connection with a deferred compensation plan is exposed to a variety of risks, most of which are similar in nature to the types of risks banks are exposed when investing in life insurance policies: credit risks, liquidity risks, and interest rate risks.

Annuity contracts are similar to certificates of deposit in that the investor places money with an institution, such as an insurance company, in the expectation of the return of the investment plus earnings at a specified later date or on a specified schedule. Some annuities provide that the investor may select a lifetime payout, which provides a fixed income until the death of the annuitant. However, unlike a bank certificate of deposit, an annuity is uninsured, creating credit risk. An investor is not subject to the risk of loss of principal through market fluctuations, but the investor has credit risk based on the solvency of the issuing entity.

The lack of a secondary market for annuities gives rise to liquidity risk. Such investments are generally long term, subject to varying early withdrawal penalties and early redemption may cause a loss of tax deferral advantages.

Interest rate risk arises from fixed rate annuities, particularly in light of the long term nature of these contracts. Most insurance companies offer variable rate arrangements to mitigate interest rate risk. However, the issuing company generally determines interest rates on variable rate contracts and may not use a common index. For this reason, future yields are uncertain and likely to be lower than other available types of investments. However, interest rate floors may mitigate this risk. We see the same interest rate structure in certain types of life insurance policies wherein the return is dependent on an interest payment calculated on the cash surrender value of the policy.

Various supervisory concerns similar to those associated with investments in insurance policies arise when banks invest in annuity contracts. They include potential violations of laws and regulations, less than adequate rate of return, the illiquidity of the investments, and concentration of investment risks. For those annuities that will provide compensation or other benefits to employees or their beneficiaries, the amount of such expected benefits must be quantified and not exceed reasonable compensation levels when combined with other forms of compensation provided to those employees. As stated earlier, section 39 of the FDI Act prohibits excessive compensation as an unsafe or unsound act.[3]

A less than adequate rate of return is also a concern such that the propriety of investing large sums in an annuity contract or numerous contracts is also a consideration. However, as with insurance products, annuity contracts should be viewed in the context of the bank's overall asset and liability structure and not viewed in isolation in order to determine if they pose a significant risk to the fund.

Because of the illiquid nature of long-term annuity contracts, banks often find it difficult to liquidate the contracts without incurring sizeable surrender charges. The illiquid nature of the assets, however, should be viewed from an overall impact on the bank in conjunction with other assets of the bank. Liquidity concerns may also be mitigated if banks have the ability to borrow against the contracts without incurring adverse surrender charges or adverse tax consequences. Due to the liquidity and credit risks, unduly large concentrations in investments in annuity contracts could result if a bank does not adopt prudent constraints on the amount of its exposures.

Approved Annuity Applications

As of June 4, 1996, the FDIC has acted upon 2 annuity applications. These actions, all approvals, were taken by the Board of Directors. The actions were contingent upon conformance to specific conditions deemed necessary to limit the risk to the bank. Those conditions addressed concerns the FDIC Board of Directors had relative to these products.

Description of Proposed Exceptions

As stated earlier, the FDIC is proposing to amend part 362 to provide a notice process for certain insured state banks proposing to invest in or retain real estate or life insurance and annuity contracts. Currently all insured state banks wishing to indirectly retain or acquire impermissible real estate investments, or directly or indirectly invest in nonconforming life insurance and annuity contracts, must apply to the FDIC for approval under section 24 of the FDIA and part 362. As detailed above, the FDIC Board has had a significant amount of experience with both types of applications and has concluded that it is possible for an insured state bank to engage in such activities without posing a significant risk to the deposit insurance fund. The FDIC recognizes that the application process can be costly and time consuming for insured state banks. Based on the Board's experience and the goal of relieving regulatory burden on insured state banks, the FDIC is proposing to amend its regulations to permit certain highly rated banks to engage in such activities under certain circumstances without the need for an application. The proposed exceptions would be added to the list of activities found in § 362.4(c)(3) which the FDIC has found do not present a significant risk to the deposit insurance fund.

[3] 12 U.S.C. 1831p–1(c).

The FDIC proposes to permit certain highly rated insured state banks to file notices 60 days prior to making an indirect investment in real estate or a direct or indirect investment in life insurance or annuity contracts. The procedures for filing, review and action on both types of notices are the same, however, there are certain conditions which insured state banks must meet in order to be eligible for the notice processing. The conditions in the case of real estate investments are more numerous and detailed than the conditions in the case of life insurance and annuity contract investments. For instance, banks wishing to invest in real estate must use a subsidiary organized solely for such purpose whereas banks will be permitted to directly own life insurance and annuity contracts. The conditions for bank eligibility are discussed below. The amount and type of information required in the notices to be filed with the FDIC regional offices differs significantly depending upon whether the bank is proposing to invest in real estate or life insurance and annuities.

Notice Procedure

Notices are to be filed with, reviewed by and acted upon by the FDIC regional offices. Complete notices will normally be acted upon within 60 days of filing. Notices which do not include all the required information are not considered complete. The 60 day review period begins when all required information has been received by the FDIC regional offices. The FDIC regional offices will issue a letter to the insured state bank confirming receipt of the notice and advising the insured state bank of the date after which the bank may engage in the activity if the FDIC has not objected. The notice will be reviewed for the purpose of determining whether the bank is in fact eligible for the exception as well as for the purposes of determining whether particular facts and circumstances unique to the institution raise policy or legal concerns warranting additional action on the part of the FDIC. If safety or soundness issues are identified which do not rise to the level of presenting a significant risk to the deposit insurance fund, it is contemplated that the regional office will work with the bank during the notice period to correct the problems which have been identified.

FDIC Action on Notices

The FDIC regional offices can issue a letter of nonobjection before the end of the 60 day notice period advising the bank that it may proceed with the proposed investment or activity. The FDIC regional offices could also issue to a bank a letter of objection before the end of the 60 day review period. A letter of objection would mean that the FDIC regional offices have determined that either the insured state bank does not qualify for notice processing or that the activity raises legal or policy concerns given the particular circumstances. If the regional offices determine that the bank does not meet the eligibility requirements or raises legal or policy concerns, the notice can be converted at the bank's option into an application and be processed in accordance with other provisions of part 362.

The FDIC regional offices can extend the 60 day review period for an additional 30 days if it provides written notice of the extension to the insured state bank before the 60 day review period has run. The FDIC does not anticipate that extensions will occur frequently. FDIC regional offices should review and act on notices as quickly as possible, with the 60 day review period generally being seen as an outside limit.

Should the FDIC regional offices fail to take written action by the end of the 60 day period, or the 90 day period if a 30 day extension has been taken, the FDIC shall be deemed to have issued a letter of nonobjection. In such event the insured state bank may engage in the activity on the terms and conditions as described in its notice, subject to the continued obligation to comply with the conditions set out in the exception. It is the FDIC's intent to normally respond to notices rather than to simply allow the notice period to expire.

Issuance of a letter of nonobjection or permission to engage in the activity after the notice period expires does not preclude the FDIC from taking appropriate actions to address any safety and soundness concerns regarding the operation of a bank, any of its subsidiaries, or a particular investment in real estate or life insurance and annuities. If an insured state bank's financial or managerial resources suffer an adverse change, the FDIC retains its full authority to require the bank to take whatever steps FDIC deems appropriate.

Treatment of Outstanding FDIC Orders

As noted above, a large number of insured state banks previously applied for and received approval from the FDIC to invest in real estate or life insurance and annuity contracts. The terms of the FDIC orders approving such applications will remain in effect and not be modified by the enactment of the proposal. To the extent those orders differ from the notice provisions in the proposed regulation, insured state banks may apply to the appropriate FDIC regional office for relief (provided the bank meets the eligibility requirements) by submitting a notice as required by the regulation and attaching a copy of the FDIC order which they are seeking to have rescinded. The terms of the FDIC order would remain in effect pending completion of the notice process.

Pending Applications

If the proposal is adopted, insured state banks which have pending real estate or life insurance and annuity investment applications and which meet the conditions of eligibility in the proposed regulation may ''convert'' their applications to notices by submitting a letter to the appropriate FDIC regional office requesting such treatment. The letter requesting such treatment should show that the bank meets the conditions of eligibility and contain such additional information as may be necessary to complete the notice. The FDIC regional office will either issue a letter to the insured state bank which states that the application has been converted to a notice and advising the insured state bank of the date after which the bank may engage in the activity if the FDIC has not objected or issue a letter to the insured state bank stating that the FDIC objects to the conversion request. In the event of FDIC objection to the conversion request, the application will continue to be processed in accordance with the other provisions of part 362.

Continued Compliance with Eligibility Conditions

Banks which utilize the notice process to invest in real estate or life insurance and annuity contracts must continue to meet the conditions for eligibility set forth in the proposed regulation. Banks which fall out of compliance with any one of the eligibility conditions in the regulation are required to notify the FDIC regional office within 10 business days. The FDIC regional office shall review the notice and take such action as it deems necessary based on safety and soundness concerns. The FDIC regional offices have a broad range of authority with respect to the actions they can require the insured state bank to take. For example, the FDIC regional office may require the insured state bank to return to compliance within a specified period of time, to submit an application pursuant to § 362.4(d), to submit a capital restoration plan, or in appropriate cases to divest the investment.

Notice—Real Estate Investments

Section 362.4(c)(3)(vi)(A)—Conditions for Bank Eligibility

The notice process is available only to those insured banks which propose to hold their real estate investments through a majority-owned subsidiary. Structure is important with respect to real estate investments. As noted above, the holding of real estate investments through a subsidiary will provide some liability protection to the bank, and ultimately the deposit insurance fund, should there be any adverse litigation or hazardous environmental waste problems. In addition, the subsidiary must be ''solely'' for the purpose of real estate investments. Sole purpose subsidiaries will simplify reporting and monitoring of the real estate investments. Insured state banks which would like to operate mixed use subsidiaries for real estate investments will be required to go through the normal part 362 application process.

There are nine conditions for banks that want to invest in real estate using the notice process. The bank must have either a 1 or 2 UFIRS composite rating as assigned by the FDIC as of the most recent rating period. The FDIC believes that only those banks which have composite ratings of 1 or 2 are appropriate for the notice process. These institutions have shown that they have the requisite financial and managerial resources to run a financial institution without presenting a significant risk to the deposit insurance fund. While other lower rated financial institutions may have the requisite financial and managerial resources and skills to undertake real estate investments, the FDIC believes that those institutions should be subject to the formal part 362 application process as opposed to the streamlined notice process described herein.

The bank must be ''well capitalized'' as defined in part 325 of this title after deducting the proposed real estate investment from capital calculations. This eligibility condition reflects the FDIC's belief that only those insured state banks with strong capital positions should be investing in real estate. Bank capital is designed to act as a cushion in the event of losses. As noted above, the variability of returns on real estate investments is very wide. Banks can not count on any return on their real estate investments, and may in fact end up losing the entire investment. For this reason, the FDIC believes the capital deduction reflects a more accurate assessment of the bank's capital position.

As noted above, to be eligible for notice processing a bank must use a subsidiary for the real estate investment. The real estate subsidiary must meet several conditions. First, the subsidiary must meet the definition of ''bona fide subsidiary'' as contained in § 362.2(d), except a majority of the subsidiary's officers and directors may be directors or executive officers of the bank. However, the subsidiary must have at least one director who is knowledgeable with respect to real estate investment activities and is not an employee, officer or director of the bank. This requirement is to assure that the real estate subsidiary is in fact a separate and distinct entity. As discussed above, this requirement should insulate the bank and the deposit insurance fund from liabilities in excess of the bank's investment.

The FDIC believes that banks that want to engage in real estate investment should have subsidiaries with board members that will manage using proven experience in real estate as such experience will greatly increase the likelihood of successful investment. The independent board member must be an individual who is not an employee, officer or director of the bank and who is knowledgeable with respect to real estate investment activities. An independent director should bring valuable experience to the subsidiary's operations. Officers, directors or employees of the bank's holding company or of an affiliate of the bank are eligible to fill the independent director requirement.

The bank must have a written business plan for the real estate investment which is acceptable to the FDIC. Banks that want to engage in real estate investment should have a written business plan which is detailed and well thought out. Such a plan is yet another indicator that the financial institution has adequate managerial resources to engage in the proposed activity.

All transactions between the bank and the subsidiary should conform to the restrictions that would apply under sections 23A and 23B of the Federal Reserve Act as between a bank and its affiliate. This requirement is intended to make sure that adequate safeguards are in place for the dealings between the bank and its subsidiary. The FDIC invites comment on whether all the provisions of sections 23A should be imposed or whether just certain restrictions are necessary. For instance, should the regulation simply provide that the bank's investment in the real estate subsidiary is limited to 10% of capital and that there is an aggregate investment limit of 20% for all subsidiaries rather than in effect subject transactions between the bank and its real estate investment subsidiary to all of the restrictions of section 23A of the Federal Reserve Act. If the FDIC were to do so, it would be the Agency's intent to monitor transactions between the bank and its subsidiary as part of the FDIC's regulatory oversight of the bank and to address any concerns on a case-by-case basis.

Finally, two restrictions are imposed which are designed to address tying and insider abuse. First, with respect to tying, neither the bank nor the subsidiary may engage in any transaction which requires a customer of either to buy any product or use any service of either as a condition of entering into the transaction. This restriction on tying transactions is broader than the conditions in previous FDIC Board Orders in that it would cover any product or service which either the bank or the subsidiary offers. The FDIC requests comment on whether the tying restriction is broader than necessary. Commenters who believe the tying restriction should be limited to loans by the bank to customers of the real estate subsidiary should explain why these loans are the only problematic transactions.

The second restriction is neither the bank nor the subsidiary may engage in any transaction with a bank insider (or a related interest) which involves the real estate investment activities of the subsidiary unless the FDIC regional office approves the transaction in advance. This restriction does not apply, however, to extensions of credit which are subject to § 337.3 of this title. This exception carves out those extensions of credit by a bank to its executive officers, directors and principal shareholders, and their related interests, which comply with Regulation O. 12 CFR 215, subpart A.

Section 362.4(c)(3)(vi)(B)—Contents of Notice

Insured state banks which meet the conditions for eligibility would be required to file a notice with the appropriate FDIC regional office. The amount of information required in the real estate investments is greater than that required in the case of life insurance and annuity investments. The regulation sets forth seven (7) specific information requirements, which are:

(B)(1). *A brief description of the real estate investment activities.* The notice should describe the proposed investment, e.g., purchase of raw land, interest in a shopping center or construction of a small office building,

and identify where the real estate is located.

(B)(2). *A copy of the real estate investment business plan.* This written document should discuss all aspects of the proposed business, capitalization, cash flows, expenses, market variables, etc. Banks without written business plans will not be permitted to file notices.

(B)(3). *A description of the subsidiary's operations including management's expertise.* The FDIC believes that experienced real estate management is very important to the success of a subsidiary engaged in real estate activities. The notice shall contain a detailed discussion of management's real estate experience in the particular type of real estate investment contemplated. For instance, if the subsidiary is going to engage in residential real estate development, the application should discuss managements proven experience in residential real estate development.

(B)(4). *The amount of bank's aggregate investment in the subsidiary stated as a percentage of Tier 1 Capital.* The notice should state clearly the amount of investment which a bank has in the real estate subsidiary. This includes both direct (such as contributions of capital and loans to the subsidiary) and indirect investments (such as extensions of credit or commitments of credit to third parties who will be making direct investments in the subsidiary). Further, a bank shall also include in its calculation any extension of credit or commitment of credit to a third party which will be making an investment in any investment which the subsidiary has an interest. Banks should not include in their calculation of investment any retained earnings or the value of any assets which the subsidiary may hold. Notices should quantify and separately identify the direct and indirect real estate investments.

(B)(5). *Bank's capital after deducting the investment in real estate.* The notice should state clearly what the bank's capital position is after deducting the investment in real estate. The bank should set forth its 3 capital categories as of the latest call report in both dollars and percentages. The notice should also show on a pro forma basis what the bank's Tier 1 Capital will be, on both a dollar and percentage basis, after making the required deduction. Stating this information clearly in the notice will assist the FDIC regional office in reviewing and acting upon the bank's notice.

(B)(6). *A copy of the board of director's resolution authorizing the filing of the notice.* The notice should state the bank's board of directors has authorized the proposed investment in real estate, including the formation of a majority-owned subsidiary solely for the purpose of investing in real estate, and authorized the filing of the notice with the FDIC. A copy of the Board resolution(s) should be attached to the notice.

(B)(7). *The relevant state law which authorizes the bank subsidiary to conduct real estate investment activities.* The notice should identify the relevant state statute, regulation or guideline which permits the bank's subsidiary to invest in real estate. If an application or some other type of approval from the state banking regulator is required, the state banking regulator's approval or nonobjection should be referenced. A copy of such approval or nonobjection letter should be attached to the notice. The FDIC can not authorize insured state banks to invest in real estate unless they are permitted to do so under existing state law. For this reason it is important that banks identify the relevant state statutes, regulations or other provisions of law which permit them to engage in such activities. Again, such information will greatly assist the FDIC regional offices in reviewing the notices as expeditiously as possible.

Notice—Life Insurance and Annuity Products

Section 362.4(c)(3)(vii)—Condition for Bank Eligibility

The bank eligibility conditions are somewhat less restrictive for investing in life insurance and annuity products than for real estate investments. For instance, insured state banks wishing to invest in life insurance and annuities are generally not required to use a subsidiary for such investments and there is no capital ''deduction'' for life insurance and annuity investments. The less restrictive eligibility requirements are reflective of the FDIC's view that life insurance and annuity investments are generally less risky investments than real estate investments.

There are six conditions for banks wishing to invest in life insurance or annuity contracts pursuant to a notice. The bank must be well capitalized as defined in part 325. The bank's most recent UFIRS rating as assigned by the FDIC must be a ''3'' or better. The bank must have in place policies and procedures for monitoring the financial health of the companies issuing or underwriting the life insurance or annuity contracts.

There are two percentage of Tier 1 Capital investment limits for annuities and life insurance policies. The bank's total aggregate investment in annuity contracts and life insurance policies which are impermissible for national banks (nonconforming) can not exceed 30% of the bank's tier 1 capital. The bank's total aggregate investment in all types of annuity contracts and life insurance policies can not exceed 50% of the bank's Tier 1 capital. (A)(4). The 50% limit would include both the national bank permissible life insurance policies as well as those which are not permissible for national banks to hold. Banks are also required to diversify their annuity contract and life insurance policy risks. In order to be eligible for the notice process, a bank's total investment in conforming and nonconforming investments from anyone issuer cannot exceed a maximum of 15% of the bank's Tier 1 capital.

Banks are also required to purchase annuities and life insurance policies from highly rated issuers. Under the regulation, banks are not eligible for the notice process if they have purchased annuity contracts or life insurance policies from issuers that are not in the top two categories of a nationally recognized rating service. There are several national organizations which rate insurance companies: these organizations include A.M. Best, Standard & Poors and Moody's.

As noted above, banks are not generally required to purchase or hold life insurance policies or annuity contracts through a subsidiary. Some life insurance policies and annuity contracts are ''securities'' for purposes of the Federal securities laws. All annuity contracts which are considered to be ''securities'' must be held through a subsidiary of the bank. Those life insurance policies which do not qualify under OCC BC 249 and which are considered to be ''securities'' must also be held through a subsidiary of the bank. Holding such securities through a subsidiary of the bank is required pursuant section 24 and part 362.

Section 362.4(c)(3)(vii)(B)—Contents of Notice

Insured state banks which meet the six conditions for eligibility noted above would be required to file a notice with the appropriate FDIC regional office. The amount of information required in the life insurance and annuity investment notices is less than that required in the real estate investment notices. The regulation sets forth seven (7) specific information requirements for

the life insurance and annuity investment notices. They are:

(B)(1). *The aggregate amount of direct and indirect investment in life insurance policies and annuity contracts stated as a percentage of the bank's Tier 1 Capital.* The notice should state clearly the number of annuity contracts and life insurance policies which the bank owns (or intends to acquire), either directly or through a subsidiary. The notice should also state the dollar value of the annuity contracts and life insurance policies and what percentage of the bank's tier one capital that represents. Banks should *not* include in this provision any life insurance policies which a national bank would be permitted to own under either Test A or Test B of OCC Banking Circular 249.

(B)(2). *The aggregate amount of direct and indirect investment in all life insurance policies and annuity contracts as a percentage of the bank's Tier 1 capital.* This item includes conforming as well as nonconforming investments in life insurance policies. The notice should identify those life insurance policies which conform to either Test A or Test B of BC 249 and the value of such life insurance policies.

(B)(3). *The concentration of investment by issuer.* The notice shall clearly state the aggregate amount of bank investment in annuity contracts and life insurance policies from any one issuer. The FDIC is concerned about concentration of risk from one issuer, therefore banks should aggregate life insurance policies and annuity contracts issued by the same company.

Calculations shall be stated as a percentage of the bank's tier one capital. All life insurance policies, even those which may be permissible for a national bank under OCC BC 249, should be included in the calculation.

(B)(4). *The rating of the issuer(s) of the policies and annuity contracts.* The notice should state the most current rating of the issuer by the nationally recognized rating services which rate the issuer. The issuer must be in one of the top two rating categories of the rating service. If the issuer is not in one of the top two rating categories, the bank is not eligible for the notice process. If the issuer is rated by more than one of the nationally recognized rating services and the issuer is not in the top two rating categories of all services the FDIC may object to the notice.

(B)(5). *A description of the bank's monitoring procedures.* The notice shall identify and briefly describe the bank's procedures for monitoring the financial health of the issuer. The notice shall, at a minimum, identify the individual or committee responsible for monitoring the financial status of the issuer and how frequently the monitoring is done. If the procedures are in writing, they should be attached to the notice.

(B)(6). *The relevant state law which authorizes the bank investment in life insurance policies or annuity contracts should be identified.* The notice should identify the relevant state statute, regulation or guideline which permits insured state banks to invest in life insurance policies or annuity contracts. If an application or some other type of approval from the state banking regulator is required, the state banking regulator's approval or nonobjection should be referenced. A copy of such approval or nonobjection letter should be attached to the notice. The FDIC can not authorize insured state banks to invest in life insurance policies or annuity contracts unless they are permitted to do so under existing state law. For this reason it is important that banks identify the relevant state statutes, regulations or other provisions of law which permit them to engage in such activities. Again, such information will greatly assist the FDIC regional offices in reviewing and acting on the notices as expeditiously as possible.

(B)(7). *A copy of the board of director's resolution authorizing the filing of the notice.* The notice should state that the bank's board of directors have authorized the proposed investment in life insurance policies or annuity contracts and authorized the filing of the notice with the FDIC. A copy of the Board resolution(s) should be attached to the notice.

Regulatory Flexibility Analysis

The Board of Directors has concluded after reviewing the proposed regulation that the regulation, if adopted, will not impose a significant economic hardship on small institutions. This proposal simplifies and streamlines the timing and information small entities must file to engage in profit-making activities thereby reducing their regulatory burden. By expediting processing and allowing small entities to engage in profit-making activities more quickly, small entities may avoid lost opportunity costs. The Board of Directors therefore hereby certifies pursuant to section 605 of the Regulatory Flexibility Act (5 U.S.C. 605) that the proposal, if adopted, will not have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act (5 U.S.C. 601 et. seq.).

List of Subjects in 12 CFR Part 362

Administrative practice and procedure, Authority delegations (Government agencies), Bank deposit insurance, Banks, banking, Insured depository institutions, Investments, Reporting and recordkeeping requirements.

For the reasons set forth above, the FDIC hereby proposes to amend 12 CFR part 362 as follows.

PART 362—ACTIVITIES AND INVESTMENTS OF INSURED STATE BANKS

1. The authority citation for part 362 continues to read as follows:

Authority: 12 U.S.C. 1816, 1818, 1819[Tenth], 1831a.

2. Section 362.4 is amended by adding new paragraphs (c)(3)(vi) and (c)(3)(vii) to read as follows:

§ 362.4 Activities of insured state banks and their subsidiaries.

* * * * *

(c) * * *

(3) * * *

(vi) *Equity interests in real estate.* (A) An insured state bank may invest in and/or retain equity interests in real estate through a majority-owned subsidiary organized solely for such purpose provided that the bank has filed written notice as described in paragraph (c)(3)(vi)(B) of this section at least 60 days prior to making the initial investment, the FDIC has not objected to the investment prior to the expiration of the 60-day notice period nor extended the notice period an additional 30 days and objected to the investment prior to the expiration of the extended notice period, and the following conditions are, and continue to be, met:

(*1*) The bank is well-capitalized as defined in part 325 of this chapter exclusive of the bank's investment in the subsidiary as well as any extensions of credit or commitments of credit to any third party for the purpose of making a direct investment in the subsidiary or making an investment in any investment in which the subsidiary has an interest;

(*2*) The bank makes the deduction in paragraph (c)(3)(vi)(A)(*1*) of this section for purposes of determining capital as reported on the bank's report of condition and assessment risk classification purposes in part 327 of this chapter and prompt corrective action purposes under part 325 of this chapter provided, however, that the deduction shall not be used for the purposes of determining whether the bank is ''critically undercapitalized'' as defined under part 325 of this chapter;

(*3*) The bank's most current composite rating assigned by the FDIC under the Uniform Financial Institutions Rating System or such other comparable rating system as may be adopted by the FDIC in the future is 1 or 2;

(*4*) The subsidiary meets the definition of ''bona fide subsidiary'' as contained in § 362.2(d) except that the requirements of § 362.2(d)(6) and (d)(7) are waived provided that the subsidiary has at least one director who is knowledgeable with respect to real estate investment activities and is not an employee, officer or director of the bank;

(*5*) The subsidiary is managed by persons who have expertise in the real estate investment activities conducted by the subsidiary;

(*6*) The subsidiary has a written business plan regarding the real estate investment activities;

(*7*) Transactions between the bank and the subsidiary comply with the restrictions of sections 23A and 23B of the Federal Reserve Act (12 U.S.C. 371c and 371c–1) to the same extent as though the subsidiary were an affiliate of the bank as the term affiliate is defined for the purposes of section 23A and section 23B except that extensions of credit made by the bank to finance sales of assets by the subsidiary to third parties need not comply with the collateral requirements and investment limitations of section 23A provided that such extensions of credit are consistent with safe and sound banking practice, do not involve more than the normal degree of risk of repayment, and are extended on terms and under circumstances, including credit standards, that are substantially the same, or at least as favorable to the bank, as those prevailing at the time for comparable transactions;

(*8*) Neither the bank nor the subsidiary shall engage in any transaction which requires a customer of either to buy any product or use any service of either as a condition of entering into a transaction; and

(*9*) Neither the bank nor the subsidiary engages in any transactions (exclusive of those covered by § 337.3 of this chapter) with insiders of the bank as insider is defined in Federal Reserve Board Regulation O (12 CFR 215.2(h)), which relate to the subsidiary's real estate investment activities without the prior written consent of the appropriate regional director for the Division of Supervision.

(B) Notice filed pursuant to paragraph (c)(3)(vi)(A) of this section may be in letter form and should be filed with the regional director for the Division of Supervision for the FDIC region in which the bank's principal office is located. The regional office will send written acknowledgment of receipt of a completed notice to the bank which shall indicate the date after which the bank may initiate the investment activities if the FDIC has neither objected to the notice nor extended the notice period. The notice period will begin to run from the date the acknowledgment is sent. If the notice period is extended, the bank will be notified in writing and informed of the date after which the bank may initiate the investment activities if the FDIC does not object. Notices shall contain the following:

(*1*) A description of the real estate investment activities;

(*2*) A copy of the business plan concerning the real estate investment activities;

(*3*) A description of the subsidiary's operations including a discussion of management's expertise;

(*4*) The aggregate amount of the bank's investment in the subsidiary as defined in § 362.2(q), which does not include retained earnings, and the bank's extensions of credit and commitments of credit to third parties for the purpose of making a direct investment in the subsidiary or making an investment in any investment in which the subsidiary has an interest stated as a percentage of tier one capital;

(*5*) The bank's capital after adjustments are made for the deductions described in paragraph (c)(3)(vi)(A)(*1*) of this section;

(*6*) A copy of the board of directors' resolution authorizing the filing of the notice; and

(*7*) An identification of the relevant state statute, regulation or other authority which authorizes the subsidiary to conduct real estate investment activities.

(C) An insured state bank which falls out of compliance with any of the eligibility conditions in paragraph (c)(3)(vi)(A) of this section shall notify the FDIC regional office within 10 business days of falling out of compliance. The FDIC regional office shall review the notice and take such action as it deems necessary. Such actions may include, but are not limited to, requiring the insured state bank to file an application pursuant to paragraph (d) of this section, requiring the submission of a capital restoration plan or requiring the divestiture of such investment.

(vii) *Life insurance policies and annuity contracts.* (A) An insured state bank may invest in and/or retain life insurance policies and annuity contracts, either directly or indirectly through a majority-owned subsidiary of the bank, provided that the bank has filed written notice as described in paragraph (c)(3)(vii)(B) of this section at least 60 days prior to making the initial investment, the FDIC has not objected to the investment prior to the expiration of the 60-day notice period nor extended the notice period an additional 30 days and objected to the investment prior to the expiration of the extended notice period, and the following conditions are, and continue to be, met:

(*1*) The bank is well-capitalized as defined in part 325 of this chapter;

(*2*) The bank's most current composite rating as assigned by the FDIC under the Uniform Financial Institutions Rating System or such other comparable rating system adopted by the FDIC in the future is at least 3;

(*3*) The bank's total aggregate direct and indirect investment in annuity contracts and life insurance policies which do not conform to OCC Banking Circular 249 does not exceed 30% of the bank's tier one capital;

(*4*) The bank's total aggregate direct and indirect investment in all annuity contracts and life insurance policies (conforming and nonconforming) is no greater than 50% of the bank's tier one capital and the bank's total aggregate direct and indirect investment in all annuity contracts and life insurance policies (conforming and nonconforming) from the same issuer does not exceed 15% of the bank's tier one capital;

(*5*) The issuer(s) of the life insurance policies and annuity contracts (conforming and nonconforming) is (are) rated in the top two rating categories by a nationally recognized rating service; and

(*6*) The bank's board of directors has procedures in place to monitor the financial condition of the issuer(s) of the life insurance policies and annuity contracts (conforming and nonconforming).

(B) Notice filed pursuant to paragraph (c)(3)(vii)(A) of this section may be in letter form and should be filed with the regional director for the Division of Supervision in the region in which the bank's principal office is located. The regional office will send written acknowledgment of receipt of a completed notice to the bank which shall indicate the date after which the bank may initiate the investment activities if the FDIC has neither objected to the notice nor extended the notice period. The notice period will begin to run from the date the acknowledgment is sent. If the notice period is extended, the bank will be notified in writing and informed of the

date after which the bank may initiate the investment activities if the FDIC does not object. Notices shall contain the following:

(*1*) The aggregate amount of direct and indirect investment in annuity contracts and nonconforming life insurance policies stated as a percentage of the bank's tier one capital;

(*2*) The aggregate amount of direct and indirect investment in all annuity contracts and life insurance policies (conforming and nonconforming) stated as a percentage of the bank's tier one capital;

(*3*) The aggregate amount of direct and indirect investment in all annuity contracts and life insurance policies (conforming and nonconforming) from any one issuer stated as a percentage of the bank's tier one capital;

(*4*) The rating of the issuer(s) of the policies and annuity contracts;

(*5*) A description of the bank's monitoring procedures;

(*6*) The state statute, regulations or other authority which authorizes the bank to make the investment; and

(*7*) A copy of the board of directors' resolution authorizing the filing of the notice.

(C) An insured state bank which falls out of compliance with any of the eligibility conditions in paragraph (c)(3)(vii)(A) of this section shall notify the FDIC regional office within 10 business days of falling out of compliance. The FDIC regional office shall review the notice and take such action as it deems necessary. Such actions may include, but are not limited to, requiring the insured state bank to file an application pursuant to paragraph (d) of this section, requiring the submission of a capital restoration plan or requiring the divestiture of such investment.

§ 362.6 [Amended]

3. Section 362.6 is amended by adding ''the authority to act on notices filed pursuant to § 362.4(c)(3)(vi) (A) and (C) and § 362.4(c)(3)(vii) (A) and (C); the authority to rescind orders issued pursuant to § 362.4 where it is determined that the institution is eligible to engage in activities pursuant to an exception contained in § 362.4(c)(3);'' immediately after ''§ 362.3(d);''.

By Order of the Board of Directors.

Dated at Washington, D.C., this 13th day of August, 1996.

Federal Deposit Insurance Corporation.

Jerry L. Langley,

Executive Secretary.

[FR Doc. 96–21475 Filed 8–22–96; 8:45 am]

BILLING CODE 6714–01–P

DEPARTMENT OF TRANSPORTATION

Office of the Secretary

14 CFR Part 255

[Docket No. OST–96–1639; Notice No. 96–21]

RIN 2105–AC56

Fair Displays of Airline Services in Computer Reservations Systems (CRSs)

AGENCY: Office of the Secretary, Department of Transportation.

ACTION: Correction to notice of proposed rulemaking.

SUMMARY: This document contains a correction to the notice of proposed rulemaking proposing revisions to the Department's rules on the display of airline services in computer reservations systems (CRSs). That notice was published Wednesday, August 14, 1996 (61 FR 42208). The notice incorrectly stated that the docket number for this proceeding is OST–96–1145; the correct docket number is OST–96–1639.

FOR FURTHER INFORMATION CONTACT: Thomas Ray, Office of the General Counsel, 400 Seventh St. S.W., Washington, D.C. 20590, (202) 366–4731.

SUPPLEMENTARY INFORMATION: The notice of proposed rulemaking that is the subject of this correction proposed revisions to the Department's rules on the display of airline services in computer reservations systems (CRSs), 14 CFR 255.4. That notice incorrectly stated the docket number for this proceeding as OST–96–1145, which is instead the docket number for a different proceeding involving a proposed amendment to another section of the Department's CRS rules, 14 CFR 255.6; the correct docket number for this proceeding on CRS display rules is OST–96–1639.

Accordingly, the publication on August 14, 1996, of the Notice of Proposed Rulemaking on CRS display rules is corrected as follows:

On page 42208, the two citations of Docket No. OST–96–1145 [49812] are replaced with citations to Docket OST–96–1639.

This correction is issued pursuant to 49 CFR 1.57(l).

Issued in Washington, D.C. on August 17, 1996.

Nancy E. McFadden,

General Counsel.

[FR Doc. 96–21538 Filed 8–22–96; 8:45 am]

BILLING CODE 4910–62–P

FEDERAL TRADE COMMISSION

16 CFR Part 23

Extension of Time; Section 7 (Platinum) of the Guides for the Jewelry, Precious Metals and Pewter Industries

AGENCY: Federal Trade Commission.

ACTION: Extension of time for filing public comments.

SUMMARY: The Federal Trade Commission (the ''Commission'') requested public comments on May 30, 1996, on proposed revisions to 23.7 of the Guides for the Jewelry, Precious Metals and Pewter Industries (''the Guides''), 61 FR 27224. Section 23.7 of the Guides addresses claims made about platinum products. The Commission solicited comments until August 12, 1996. In response to a request from an industry group, the Commission grants an extension of the comment period.

DATES: Written comments will be accepted until September 30, 1996.

ADDRESSES: Comments should be directed to: Secretary, Federal Trade Commission, Room H–159, Sixth and Pennsylvania Ave., NW., Washington, DC 20580. Comments about these proposed changes to the Guides should be identified as ''Guides for the Jewelry, Precious Metals and Pewter Industry—16 CFR Part 23—Comment.''

FOR FURTHER INFORMATION CONTACT: Constance M. Vecellio or Laura J. DeMartino, Attorneys, Federal Trade Commission, Washington, DC 20580, (202) 326–2966 or (202) 326–3030.

SUPPLEMENTARY INFORMATION: On May 30, 1996, 61 FR 27178, the Commission announced revisions to its Guides for the Jewelry Industry, renamed Guides for the Jewelry, Precious Metals and Pewter Industries, 16 CFR Part 23.[1] The Guides for the Jewelry, Precious Metals and Pewter Industries (''the Guides'') address claims made about precious metals, diamonds, gemstones and pearl products. The Commission did not revise section 23.7 of the Guides for the Jewelry Industry, which addresses claims made about platinum products. Industry members had indicated the need to simplify current Commission guidance regarding claims that a product is composed of platinum and to bring this guidance into closure accord

[1] The Commission published a Federal Register notice soliciting public comment on amendments to the Jewelry Guides, including revisions to section 23.7 regarding platinum products. 57 FR 24996 (June 12, 1992). This Federal Register notice was published in response to a petition proposing changes, submitted by the Jewelers Vigilance Committee (''JVC'').