AMB Inside Look: Federal Reserve Board Guidance on Covered Savings Associations

The interpretation of the OCC's Covered Savings Association (CSA) rules has been a topic of some concern to the AMB for several years. Federal mutual associations are unable to compete on a level playing field with commercial banks and savings banks without exercising the powers conferred on covered associations. Unlike stock savings associations which can convert to a commercial bank, federal mutuals are subject to QTL so long as they maintain their mutuality. AMB had promoted a national bank mutual charter Bill but was rebuffed by the OCC in favor of the CSA legislation. The covered savings association election is the sole method a federal association has in accessing national bank powers and presumably avoiding QTL restrictions.

AMB submitted several recommendations during the regulatory CSA comment period to the OCC , which were subsequently adopted in the final 2018 OCC rule. The Federal Reserve Board in a pair of legal opinions directed to two grandfathered unitary savings and loan holding companies (popularly referred to as unicorns) stated its view that the CSA election of a savings and loan holding company ("SLHC") subsidiary association would trigger national bank treatment for the association and bank holding company ("BHC") treatment for its parent. At first blush, these opinions appeared to be of little consequence to mutuals, however, a FRB staff panel at the annual mutual forum revealed more serious consequences. In sum, a CSA would have to become a "Federal Reserve Bank member association" a unique status not contemplated by statute. Moreover, the inference that a MHC would not be a SLHC and thus not subject to Reg MM raised fundamental organic governance questions for existing MHCs and created confusion as to the applicable rules for associations contemplating reorganizing as MHCs. Finally, the staff comments raised issues of which agency would be the primary federal regulator for a MHC or CSA. AMB arranged several meetings with the OCC chief counsel and senior FRB legal staff to discuss these issues and seek clarification that would allay some of the concerns the staff interpretations raised. The FRB staff indicated that FAQs would be issued by year end resolving many of the issues raised. On December 30, 2021 the FRB staff released a series of FAQs clarifying many of the questions raised around CSAs. These FAQs appear to be based on the two opinions issued to the SLHC unicorns.

Addressing the scope of Section 5A of the Home Owners Loan Act

Under the FAQs, the FRB has reconfirmed that for purposes of the FRB's regulations CSAs will generally be **treated** as national banks. Additionally, a company that controls a CSA will be **treated** as a BHC. Curiously, the FAQs state that applying the same statute and regulations to a CSA that would apply to a national bank doesn't mean the savings association is a national bank. Similarly treating CSA parents as BHCs does not mean a SLHC becomes a BHC. It would

remain a SLHC. Thus, in an effort to prevent grandfathered SLHCs , popularly nicknamed "unicorns" from allowing their S&L subsidiaries to exercise the powers of national banks without being subject to the activities restrictions applying to BHCs, the decision throws out the baby with the bath water. While the sweeping generalizations in the FAQs may be consistent with historical FRB policy on BHC activities restrictions, they have little statutory basis and have created unicorns of a different color e.g.—a mutual CSA federal S&L Federal Reserve Bank member and a CSA BHC SLHC chartered under Reg MM that controls a member S&L not subject to QTL.

The FAQs also list the Section 5A specific "enumerated purposes" for which the FRB will treat CSAs as thrifts, and a controlling company as a Savings and Loan Holding Company (SLHC). The FRB's enumerated purposes are: (1) governance, including incorporation, bylaws, boards of directors, shareholders, and dividends; (2) consolidation, merger, dissolution, conversion (including conversion to a stock bank or to another charter), conservatorship, and receivership; and (3) those determined by regulation of the Comptroller of the Currency. The FRB makes plain that a CSA, or its holding company does not actually become a national bank or a BHC, but rather remains a thrift and SLHC. As such, an SLHC or thrift that elects to become a CSA does not need to apply for a new charter. Moreover, the enumerated powers are a guide as to which functions remain as they were before a CSA election and which will be treated as national bank or BHC functions

FRB Membership for CSAs

Whether or not CSAs must become FRB members was one of the key areas that remained ambiguous under previous rules. In this FAQ, the FRB notes that since all national banks must become FRB members, this decision extends to CSAs **whether or not they have a holding company parent.** Furthermore, The FAQs contain a clarifying answer which AMB sought that despite becoming members of the FRB, the OCC as primary regulator of a CSA will remain the same. This interpretation is consistent with the treatment of national banks which are required to be fed members and have the OCC as their primary regulator not the FRB. The open issue is whether the absence of any statutory language treating CSAs as national banks and Fed member banks will present conflicts with various other federal and state statutes which do not recognize these new unicorns.

CSA Filing Requirements

At first glance, the FRB's filing requirements for CSAs appear brief. For thrifts electing to become CSAs, Q3 of the FRB's FAQs requires the completion and submission of Form 2030a to the appropriate Federal Reserve bank. A company that controls a thrift electing to become a CSA must file Form FR Y-10. However, the FAQs require further clarification in that they suggest a contradiction. They state in one FAQ that an SLHC does not need to file for approval

to register as a BHC with the FRB to be considered a BHC. They then state that in Q7 that the HC must file all the reporting forms, and comply with all record keeping and disclosure requirements applicable to a BHC. Further, Under Transactions Involving a CSA…" the FAQs state that a CSA SLHC or national bank must submit the form that is required for a BHC or national bank under the same circumstances. This undoubtedly will try the patience of Federal Reserve Bank as application staff they too seek answers. Uhpijopijji

Inter Vivos Trusts

The FAQs apply the worst of both worlds to inter vivos trusts, i.e. an inter vivos trust would not be a BHC but would be treated as a SLHC. Under the two holding company acts inter vivos trusts are treated differently. Under the BHC Act they are not companies and therefore not required to be registered as BHCs but are companies under the SLHC Act subject to registration.

MHCs

One of the critical concerns raised by AMB was the legal inconsistency between the FRB ruling that a MHC would be treated as a BHC since a MHC is chartered and subject to comprehensive Reg. MM regulatory provisions that do not exist for BHCs. AMB was particularly concerned that the FRB interpretations cast a cloud on the corporate legitimacy of a MHC controlling a CSA, since it could be argued that CSA treatment as a BHC would effectively dissolve the MHC charter. The FAQ states (Q1 FAQ under mutual CSAs and MHCs) a MHC continues to be treated as a SLHC for the "enumerated purposes" primarily governance and retains its federal charter. Thus, the FRB has made it clear that Reg MM continues to apply which should resolve any charter legitimacy ambiguity.

Although a mutual SLHC that controls a CSA does not need to obtain a new charter, it will need to ensure that all of its activities are permissible for BHCs under Section 4(a)(2) of the Bank Holding Company Act. Essentially this means that a SLHC would have to divest or cease real estate investment activities not permitted to BHCs. This is inconsistent with the CSA legislation which was intended to broaden powers for savings associations not limit them. Of course, the continued application of Reg MM means the FRB will not be faced with arguments that dividend waiver prohibitions of Reg .MM will no longer apply to CSA MHCs. Indeed it confirms this position that the dividend prohibitions will continue to apply

QTL

A key issue for mutuals who elect to become CSAs is whether or not QTL still applies. Since that requirement is contained in the SLHC Act which is administered by the FRB, federal associations, while comforted by OCC opinions, have looked to the FRB for the final answer. On this matter, the FRB has once again deferred back to the OCC, leaning on their status as the

primary regulator for federals and CSAs to make a final determination. However, the FRB does note that the OCC has consistently ruled that CSAs do not have to comply with QTL. Given the FRB strongly stated view that CSAs will be treated as a national banks, it is difficult to appreciate why the staff still takes such a guarded position on QTL. Moreover, while the staff seems to have it both ways, it is inconceivable given its view that a CSA is a national bank for its regulatory purposes, it could opine that QTL still applies to a SLHC with a CSA subsidiary. AMB will continue to urge the FRB to further clarify its position on QTL and CSAs.

On a positive note, the FAQs contain a benefit for MHCs in that the staff does not believe that Section 239.8(a) activities restrictions apply to a Reg. MM CSA MHC. That section restricts MHC activities to those permitted to the bank under Section 10 of the HOLA. Instead, a Reg MM CSA MHC can exercise all the powers of a BHC. The FRB also notes that a mutual CSA is eligible to reorganize as a MHC under Reg MM.

Termination of CSA Status

A BHC applicant terminating CSA status must submit a Form FR Y-10 to report the deselection of CSA status. The association must file a FR 2086a to the appropriate Reserve Bank It must also divest of any BHC assets not permitted for a SLHC.

Conclusion

The FAQs offer a mixed set of interpretations some positive some disappointing. Overall they bring limited clarity to a series of significant issues. This is because they are in the nature of a staff guidance as opposed to a regulation with the force and effect of law. The absence of a binding legal document and may present some headaches to legal practitioners in coming to any l opinions that may be required by various parties to a typical transaction especially those not familiar with the lore of the FRB.

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