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Replaced. See OCC 2017-43.

New Activities and Services

Federal savings associations (FSAs) can offer a wide range of products and services that cover many savings association activities. There are many benefits of offering a wide range of products and services. Diversification contributes to the potential for increased income, decreased reliance on one activity, and the ability to maintain competitiveness. It is important that FSAs be cognizant of the risks of new activities and remain vigilant toward minimizing that risk. Highly profitable or rapidly growing activities are high risk and require a good internal control environment to avoid problems. Savings associations must identify, measure, monitor, and control new risks on a timely basis.

When savings associations engage in new activities, offer new products or services, or enter new markets, they must ensure that risk management keeps pace with the growth in the business activity. It is vital that savings associations ensure that they pay sufficient attention to internal controls when engaging in new activities.

LINKS

Program

Remember that offering an existing product line to a new set of customers can change the risks involved in conducting an activity. In addition, minor changes to an existing product line can increase risk. For instance, offering a traditional mortgage loan to subprime borrowers creates a different set of risks than when offering the same loan to prime borrowers. Services cover such things as on-line bill payment and overdraft protection service.

The Evolving Role of Federal Savings Associations

Before 1980, FSAs performed limited functions. Beginning in 1933, the Home Owners' Loan Act (HOLA), 12 USC § 1464(a), authorized the chartering of FSAs to provide savings accounts and home financing for ordinary consumers. FSAs were restricted to providing only these services for the next fifty years.

In the 1980's, the role of FSAs expanded. Congress granted FSAs broader statutory powers so they could attract deposits and increase their earnings base. Additionally, Congress declared that FSAs should be consumer oriented financial intermediaries. In 1980, under the Depository Institutions Deregulation and Monetary Control Act, Congress authorized FSAs to offer such consumer oriented services as checking accounts, NOW accounts, consumer loans, credit card loans, second-mortgage loans, construction loans, and trust services. In 1982, under the Garn-St. Germain Depository Institutions Act, Congress granted FSAs greater lending and investment powers in the following areas:

- Commercial checking accounts.
- Origination of secured and unsecured loans for commercial, corporate, business, or agricultural purposes.
- Education loans.
- Investments in all types of state and local government securities.
- Consumer and nonresidential real estate loan originations.
- Investments in commercial real estate and tangible personal property.

Congress enhanced FSA's ability to serve their business customers with enactment of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Under FIRREA, Congress authorized FSAs to offer demand deposit accounts to commercial customers on the same basis as to individuals and nonprofit corporations. Congress provided additional enhancements in the consumer lending area with the enactment of the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA). Under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), Congress further encouraged consumer and commercial lending activity. Under EGRPRA, FSAs could originate education loans without restrictions and could invest up to 20 percent of assets in small business loans.

Functional Regulation

The Gramm-Leach-Bliley Act (GLBA) made several changes to the way depository institutions engage in insurance and securities activities, including the imposition of a regulatory coordination scheme called functional regulation. Functional regulation provides for regulatory coordination and information sharing between the SEC, the banking agencies, and the state insurance agencies.

Purpose of This Handbook Section

This Handbook Section provides guidance to examiners who evaluate FSA activities. We focus on activities because experience shows that entering into or expanding a new or high-risk line of business encompasses new risks that the association must manage. This Handbook Section discusses the following topics:

- The various powers from which FSAs derive authority to engage in activities.
- The process for requesting OTS review to engage in certain new activities.
- The activity limitations that OTS may impose through approval conditions or because of the association's financial condition or capital level.

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This Handbook Section also points out differences between state and federal authority to engage in new activities, including the role that the FDIC plays in authorizing certain new activities. Finally, the Section turns to other issues that FSAs should consider before engaging in new activities.

OTS has various statutes, regulations, and interpretive opinions that authorize numerous activities in which FSAs can engage.

BACKGROUND

Authority

FSAs have the power to exercise all of the express, implied, and incidental powers conferred by Section 5 of the HOLA. However, these powers are subject to limits set by OTS when an activity presents a consumer or safety and soundness concern.

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Express and Implied Powers

These are powers expressly provided for by statute. Section 5 of HOLA lists the express powers of FSAs.

Example: HOLA authorizes FSAs to lend or invest in residential real property loans without a percentage of asset limitation (12 USC 1464(c)(1)(B)).

When OTS uses an express powers analysis to determine whether a FSA may engage in an activity, OTS first asks, "Is the activity expressly authorized by law?" To determine this, OTS reviews applicable statutes, generally, HOLA, and OTS regulations.

Certain implied powers, while not express, are inherent within the context of express powers. To determine whether a FSA has the implied power to engage in an activity, OTS analyzes whether the activity is reasonably necessary to accomplish its express powers.

If the FSA does not have the express or implied power to engage in an activity, OTS may permit the association to engage in the activity under the incidental powers analysis.

Incidental Powers

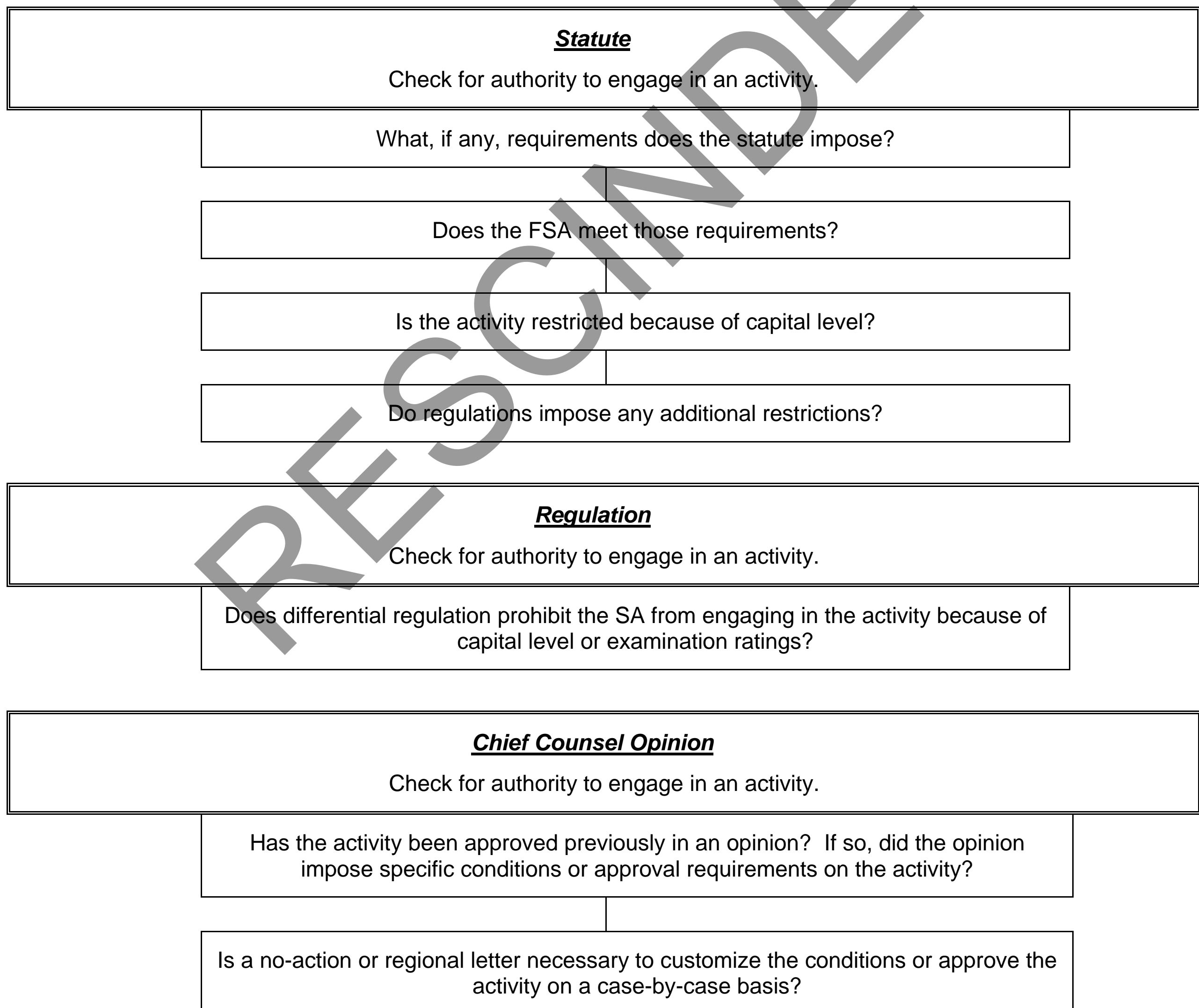
These powers result from or accompany the express powers to operate a FSA that are set forth under HOLA. HOLA does not list these activities. Therefore, if a FSA wishes to engage in an activity that is not authorized by express or implied powers, OTS may determine whether the activity is permissible under the FSA's incidental powers authority.

Example: FSAs have incidental authority to offer payroll processing services.

Determining if an Activity is Permissible

There are four steps involved in determining whether permission exists to engage in an activity:

- Review the applicable statutory authority.
- Check the regulations.
- Review opinion letters to determine if OTS has previously approved an activity.
- Determine whether a no-action letter exists. Although no-action letters are rare, one might address the activity in question.



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Opinion Request Process

If a FSA wants to engage in an activity that OTS has not authorized, the association can request that OTS opine on whether the activity is permissible by using the customer service plan process.

OTS created a formal Customer Service Plan for External Interpretive Opinions. See http://www.ots.treas.gov/docs/4/48784.html. The customer service plan provides advice on obtaining timely interpretive guidance. The plan requires:

- Consulting existing precedent.
- Consulting orally with regional or Washington staff.
- Specifying certain information in the form of a written request.

No-Action Letters

Sometimes OTS will require that an association obtain a no-action letter before engaging in or deviating from conditions on an approved activity. Other times an association might request a no-action letter before engaging in an activity when it is unsure whether one of the following is permissible: the activity itself, the manner in which the association will conduct an activity or the amount of investment in an activity.

If OTS requires the no-action letter as a prerequisite, the association should have the letter on file. A no-action letter is typically prospective in nature and relates to either a specific proposed transaction or types of transactions. A no-action letter represents only the position of staff and may be modified or superseded by subsequent OTS action. In addition, you should remember the following when considering no-action letters:

- They are rare.
- They are specific to one institution.
- They do not carry the full weight of the law.

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Application or Notice Requirements / Other Activity Restrictions

Application or Notice Requirements

The HOLA and its implementing regulations require savings associations to file applications or notices (Application) before entering into certain transactions, or to control or charter a savings association. Applications for a change in control, for a new charter, or to conduct activities through a subsidiary, frequently consider the proposed activities of the savings association. OTS may impose conditions on the proposed activity in acting on an application, and this affects how the association conducts the activity. You should determine whether the association has obtained the appropriate approvals to

conduct the activity and whether OTS has imposed any conditions related to the conduct of the activity in acting on an application.

Other Restrictions

Differential Regulation

Instead of applying regulatory requirements uniformly to all savings associations, OTS considers the risk level, size, or other conditions and characteristics of a savings association. OTS applies differential regulation to its application process by using a two-tier system for filing applications and notices to engage in new activities. The two tiers are expedited and standard. Savings associations with the highest supervisory ratings that comply with CRA may engage in certain new activities more quickly and less expensively than savings associations eligible for standard treatment. Associations eligible for expedited treatment need only submit a notice to OTS before engaging in certain activities. Additionally, such associations need only submit a notice to establish a new service corporation to engage in all preapproved activities.

Instead of applying regulatory requirements uniformly to all savings associations, OTS considers the risk level, size, or other conditions and characteristics of a savings association.

Savings associations with low supervisory, CRA, or compliance ratings are subject to standard treatment. Associations subject to standard treatment must submit an application to OTS before engaging in certain activities. In addition, they must submit an application before they can engage in certain activities through their service corporation, such as activities reasonably related to those of the savings association. This includes preapproved activities enumerated under § 559.4(b)-(i).

Interagency Rule on Risk of Nontraditional Activities (12 CFR § 567.3(b)(3) and (b)(9))

To ensure that the risk-based capital standards of financial institutions consider among other things, the risks of nontraditional activities, Congress enacted Section 305(b) of Federal Deposit Insurance Corporation Improvement Act of 1991. In response to Section 305(b), the financial regulators promulgated a joint rule to revise their risk-based capital standards. While neither Congress nor the financial regulators defined "nontraditional activities," the rule refers to such activities as those resulting from new developments in technology and the financial markets and those activities not traditionally considered part of the business of savings associations.

The risk-based capital standard incorporates the risk of nontraditional activities by considering several factors. The standard recognizes that the effect of a nontraditional activity on an institution's capital adequacy depends upon several things:

- The activity.
- The profile of the institution.
- The institution's ability to monitor and control the risks arising from that activity.

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Therefore, OTS evaluates how each new activity affects an institution's capital adequacy on a case-by-case basis. When appropriate, the federal banking regulators jointly issue examination guidelines on new activities.

Prompt Corrective Action Activity Restrictions

How OTS classifies a savings association for capital purposes will affect whether the savings association may engage in an activity. This is in part because § 38 of the Federal Deposit Insurance Act requires federal banking agencies to take action against any insured depository institution that is not adequately capitalized. Section 38 establishes the following capital categories:

- Well capitalized
- Adequately capitalized
- Undercapitalized
- Significantly undercapitalized
- Critically undercapitalized.

The statute prohibits a savings association from making capital distributions or paying management fees if, after the distribution or payment, the association would fall within one of the three undercapitalized categories.

Additionally, OTS may restrict compensation paid to senior executive officers of the association when the savings association is undercapitalized, significantly undercapitalized, or critically undercapitalized. Additionally, savings associations that are significantly undercapitalized are subject to greater limitations on their activities such as being required to do one or more of the following:

- Terminate, reduce, or alter any activity that OTS determines poses excessive risk to the association.
- Stop accepting deposits from correspondent depository institutions.
- Divest or liquidate a subsidiary that is in danger of becoming insolvent and poses a significant risk to the savings association, or that is likely to cause significant dissipation of the savings association's assets or earnings.

Critically undercapitalized savings associations have even greater restrictions on their activities and must receive prior written approval before engaging in the following:

- Entering into any material transaction outside of the normal course of business, including any investment, expansion, acquisition, sale of assets, or other similar action with respect to which the savings association is required to provide notice to the appropriate federal banking agency.

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- Extending credit for any highly leveraged transaction.
- Amending the charter or bylaws of the savings association, except to the extent necessary to carry out any other requirement of any law, regulation, or order.
- Making any material change in accounting methods.
- Engaging in any covered transaction (as defined in 12 USC § 371c(b)).
- Paying interest on new or renewed liabilities at a rate that would increase the savings association's weighted average cost of funds to a level significantly exceeding the prevailing rates of interest on insured deposits in the savings association's normal market areas.

See 12 CFR Part 565, Prompt Corrective Action.

Preemption

Federal law generally preempts state law restrictions that purport to apply to the activities of FSAs. When a state statute conflicts with federal law or imposes conditions that obstruct federal objectives, federal law generally preempts.

OTS will carefully study the relevant state and federal laws and regulations before making a determination regarding preemption. OTS may also consult with state officials in some instances.

OTS regulations provide that federal law preempts a number of state laws regarding:

- Deposits, 12 CFR § 557.11
- Lending, 12 CFR § 560.2
- Usury, 12 CFR Part 590

The regulations make clear that OTS occupies the fields of lending and deposit-related regulations for FSAs. However, OTS has determined that certain types of state law generally are not preempted to the extent they involve one of the following:

- Contract and commercial law
- Real property law
- Homestead laws specified in 12 USC § 1462a(f)
- Tort law
- Criminal law

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- Any other law that OTS finds furthers a vital state interest and either has only an incidental effect on lending or deposit operations or does not otherwise frustrate the purposes for which OTS promulgates regulations.

Subordinate Organizations and Pass-Through Investment Authority

FSAs may engage in permissible activities directly or indirectly. If they engage in the activities indirectly, they may do so through a number of different entities. FSAs may establish or obtain interests in operating subsidiaries or service corporations, provided the investment meets the requirements of 12 CFR § 559.3. Operating subsidiaries may engage in any activities authorized directly for the parent FSA. Service corporation activities include a broader range as follows:

- All activities (except deposit-taking) that a savings association is authorized to conduct.
- Any preapproved activity under 12 CFR § 559.4(b)-(i).
- Any other activity reasonably related to the activities of savings associations.

See Handbook Section 730 for a complete discussion of subordinate organizations.

Pass-through investments are investments in an entity that engages only in activities that the FSA may conduct directly and the investment must satisfy the requirements of 12 CFR § 560.32. When a FSA makes a pass-though investment, the association must comply with all the statutes and rules that would apply if the association were conducting the activity directly. When calculating investment limits, OTS aggregates the association's assets they hold directly with the association's percentage of ownership in the company's assets.

FSAs may make pass-through investments without giving notice to OTS provided they satisfy all of the following conditions:

- Investments in one company are limited to 15 percent of the FSA's total capital.
- The book value of the FSA's aggregate pass-through investments does not exceed 50 percent of its total capital after making the investment.
- The investment would not give the FSA direct or indirect control of the company.
- The FSA's liability is limited to the amount of the investment.
- The company is one of the following types:
  - A limited partnership.
  - An open-end mutual fund.

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— A closed-end investment trust.

— A limited liability company.

— An entity in which the FSA is investing to use the company's services.

If a pass-through investment does not meet all the above requirements, the FSA must give OTS 30 days advance notice. If OTS notifies the association within the 30-day period that the investment presents supervisory, legal, or safety and soundness concerns, the association must file an application with OTS. The application must comply with 12 CFR Part 516 and the association must receive written approval before making the investment. Should OTS impose any conditions on a pass-through investment, such conditions would be enforceable as a condition imposed in writing in connection with the granting of a request by a savings association under 12 USC §§ 1818(b) or 1818(i).

Special Purpose Entities

A special purpose entity (SPE) usually has narrow or specific objectives.

A special purpose entity (SPE) usually has narrow or specific objectives. SPEs legally isolate a high-risk project/asset from the holding company or association and allow other investors to take a share of the risk.

Often it is important that the SPE not be owned by the entity on whose behalf the SPE is being set up. For example, in the context of a loan securitization, when an association creates a SPE in order to securitize its own loans, if specific conditions are not satisfied, the SPE would be consolidated with the rest of the association's group for regulatory, accounting, and bankruptcy purposes, which would defeat the point of the securitization. Therefore, many SPEs are set up as orphan companies to ensure there is legal separation from the sponsor and to ensure compliance with regulatory restrictions, such as regulations relating to ownership of specific assets, limit the risk of bankruptcy, address a specific tax law, or mitigate other risks.

For example, an association may wish to issue a mortgage backed security whose payments come from a pool of loans. However, these loans need to be legally separate from the other obligations of the association. This is done by creating a SPE and then transferring the loans from the association to the SPE.

The transfer of loans and the SPE must meet strict requirements under U.S. GAAP in order to avoid consolidation of the SPE with the sponsoring association. Disclosure requirements vary depending on whether the SPE is consolidated with the association's financial statements or presented off the balance sheet.

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Activities May be Authorized but Impermissible Due to Safety and Soundness Concerns

OTS has the statutory authority to regulate, restrict, or even prohibit an activity that presents significant safety and soundness concerns, even though the activity is theoretically permissible. Congress mandated that OTS promulgate safety and soundness regulations and policies that are no less stringent than those established by the OCC.

Federal and State Charter Differences

It is important to review the savings association's charter when determining permissibility. The restrictions on activities may vary depending on whether the association has a state or federal charter.

Federal Charters

As the chartering agency for FSAs, OTS promulgates regulations that ensure FSAs operate in a safe and sound manner. OTS's governing regulations preempt state laws that purport to address FSA operations. State-chartered savings associations, however, are subject to their state's laws. See discussion on Preemption.

In general, FSAs have greater interstate branching rights than state-chartered savings associations. See § 545.92.

State Charters

Generally, a state-chartered savings association's authority to conduct activities cannot exceed the activities that FSAs are specifically permitted to engage in. State-chartered savings associations are subject to HOLA limitations, except as follows:

- If FSAs may not engage in a certain type of activity –

  Then, state-chartered savings associations may not engage as principal in the activity unless FDIC determines that the activity would not pose significant risk to the insurance fund and the association meets the fully phased-in capital standards prescribed under section 5(t) of the HOLA (12 USC § 1831e(a)).

- If FSAs may engage in an activity but not to the extent proposed –

  Then, a state-chartered savings association may engage as principal in that greater amount provided the FDIC has not concluded that engaging in the activity to that extent presents a significant risk to the insurance fund and the state-chartered savings association complies with the fully phased-in capital standards prescribed under section 5(t) of the HOLA (12 USC §1831e(b)). Separate rules govern equity investments, including investment in service corporations, by state-chartered savings associations (12 USC §1831e(c)). The FDIC has issued regulations implementing this authority at 12 CFR Part 362, Subpart C.

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"Wild card" Statutes

- Some state statutes automatically authorize state-chartered savings associations to engage in the same activities that OTS authorizes for FSAs.

FDICIA Provisions

The FDIC may determine that an activity is incompatible with deposit insurance thereby prohibiting Deposit Insurance Fund (DIF) members from engaging in that activity. For example, FDICIA § 28 prohibits a federal savings association and its subsidiaries from investing in unrated corporate debt securities.

OTHER CONSIDERATIONS

Savings associations can mitigate the risk of new activities. To determine the overall risk that a certain activity presents to the association, you should review the basic aspects of the particular activity and the savings association's controls for limiting risk. Some controls are systemic and would apply to all activities such as strong management, internal controls, experience, capital, and limited entry. Proper internal controls are essential and allow the association to contain risk, maintain profitability, and comply with applicable laws.

In particular, savings associations engaging in higher risk activities can use separate subsidiaries or affiliates with firewalls in place. If this is the case, you will want to perform the appropriate examination procedures in Handbook Section 730, Subordinate Organizations.

If necessary, regulators can require additional, more frequent regulatory reporting or disclosure to monitor a new activity. In addition, OTS may limit investment in new activities until the association becomes knowledgeable and experienced.

After you determine if an activity is permissible and determine if there are any application or notice requirements or other restrictions, then you may want to assess the extent the association is exposed to the following risks that arise when engaging in new activities. Remember that generally you will conduct this review in conjunction with review of the same area as the new activity, such as lending or deposits.

Risks of New Activities

Associations must review new or expanded activities and services for the basic accepted risks:

- Credit Risk
- Market Risk
- Liquidity Risk
- Operational Risk

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- Legal and Reputation Risk

Before an association engages in a new activity that is otherwise permissible or approved, the board of directors should determine whether the new activity presents any of these specific risks:

- Lack of expertise or experience
- Concentration Risk
- Third-party risk
- Independence risk
- Conflict of interest
- Usurpation of corporate opportunity.

You should review the savings association's report of proposed new major activities and business lines. You should also check the status of new activities by comparing current performance with prior projections and budgets. The association must have a realistic plan for assessing the performance of any new activity or business line. See Handbook Section 330, Management Assessment, and Section 340, Internal Control.

Insurance

Associations should review their existing insurance coverage before engaging in new activities to ensure that they have adequate coverage. Numerous insurance products today help mitigate the risks that financial institutions incur. They include:

- Directors and officers liability
- Key person insurance
- Errors and omissions
- Bankers blanket bond
- Employment practices liability
- Cyber risk
- Mortgage impairment
- Workers compensation

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- Terrorism
- Property
- Business interruption.

There may also be specialized insurance products related to the new activity that the association should investigate.

Lack of Expertise or Experience

Risk is inherent in any new activity. The potential for risk increases, however, when the savings association lacks expertise in an activity. You should carefully scrutinize the association if the association entered into a new activity or business venture without proper:

- Management expertise
- Policies and procedures
- Training
- Internal controls
- Consumer compliance risk management
- Independent reviews
- Supporting capital
- Information systems support
- Integration into management accounting
- Monitoring to ensure no unapproved deviation from the association's strategic or operational plans.

Training

Appropriate staff training is necessary to ensure that the staff are familiar with new products, services and processes, with due regard to their qualification, experience and quality assurance. For new products and services, the staff must have the necessary qualifications, experience and thorough knowledge of the laws, guidelines and risks.

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Compensation

New activities can provide opportunities for conflicts or risky compensation incentives. It is important for the association to think through all the ramifications of compensation incentives when deciding whether to enter into new or expanded activities.

Concentration Risk

Concentration risk management and mitigation is essential. OTS expects savings associations to develop risk management systems to ensure prudent underwriting and investment standards including explicit, board-approved, reasonable limits for higher-risk (and higher risk-weighted) asset concentrations and higher-risk liability concentrations. The board should review the risk management policies on a scheduled basis, including adjusting and refining concentration limits.

The board should establish limits based on a percentage of the savings association's capital (in most cases, Tier 1 (core) capital plus allowances for loan and lease losses (ALLL)). The board should set concentration limits at lower levels as a percentage of capital for business activities that pose significant risk. For example, non-traditional mortgage loan products, particularly those with layered risk features, should have lower limits than traditionally underwritten, prime, one- to four-family mortgage loans. OTS closely reviews all types of concentration risk, particularly if they exceed 100 percent of core capital plus the ALLL.

Third-Party Risk

If savings associations encounter unexpected difficulties in new or nontraditional businesses due to lack of experience, they might rely too much on consultants or third parties. Rather than relying extensively on consultants or third parties, the savings association should use the expertise that is available through its board of directors. Failure to involve the board of directors leads to increased risk. The board of directors has a duty to properly oversee and manage any new activities, especially those involving third-party relationships.

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Associations must adopt a risk management process that includes:

- A risk assessment to identify the association's needs and requirements.
- Proper due diligence to identify and select competent and qualified third-party providers.
- Written contracts that outline duties, obligations, and responsibilities of the parties involved, including a provision to allow OTS to terminate the contract without notice or penalty if the association becomes troubled.
- Ongoing oversight of the third parties and third-party activities. Appropriate oversight activities includes the identification of staff with the necessary expertise to oversee the provider and

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regular monitoring of the third party's financial condition, controls and the quality of its service and support.

Associations should be attentive to intangible benefits that they provide to third parties, whether affiliated or unaffiliated. The third party should compensate the savings association for intangibles such as goodwill, a reputation, or a name in the community.

For example, when there is significant exposure to purchased loans from third parties who control the servicing, disbursement, and collection processes, this relationship requires a more intensive review of the controls. OTS encourages the use of an independent, qualified third party to review and monitor these relationships. The third party can comprise internal or external staff, but should retain its independence. An independent review is particularly important when the relationship involves higher-risk loans or investments and the institution lacks a strong internal audit department or risk management system.

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Third-Party Contracts

Generally, the fundamental risks associated with activities operated through third parties are the same as if the savings association performed the activity directly. Savings associations must perform adequate due diligence, maintain adequate documentation, and ensure that there are prudent controls. In addition, savings associations must effectively oversee and monitor activities performed by third parties. See Thrift Bulletin (TB) 82a – Third-Party Arrangements. Generally, you will review the contract when you review the related activity.

As a matter of course, the board of directors must justify and approve such third-party contracts. In cases where a savings association has a CAMELS rating of 4 or 5, the contract is also subject to prior review by the Regional Director. You will need to verify that all necessary reviews took place. See Handbook Section 310, Corporate Governance and Oversight by the Board of Directors. In addition, you should check on the following items that the contract should address:

- Indemnification provisions. Indemnification provided by the association or subordinate organizations should not exceed the indemnification provided by the third party.
- Compliance with all applicable regulatory provisions, including privacy provisions.
- Appropriate compensation to the association for providing access to their customers and the physical setting as well as any administrative support.

Independence Risk

Some savings associations are parts of highly integrated corporate structures. Complex corporate structures can raise significant questions as to whether there is sufficient independence of the association. Officers and directors must ensure that the actions of other entities within the corporate structure do not threaten the association's separateness and independence.

Some safeguards that will preserve separate corporate identity and limit liability of the association include:

- Maintaining physically separate and distinct operations and holding themselves out to the public as separate enterprises.
- Ensuring that the depository institution is not responsible for and does not guarantee the obligations of any of the other entities within the corporate structure.
- Maintaining a certain amount of dedicated staff to oversee the activity or service.

Risks of Over Reliance on Dual Employees

Associations that engage in new activities sometimes use dual or shared employees to expand financial opportunities and enhance financial performance. The board of directors and management must be aware, however, that the use of dual or shared employees does not diminish their responsibility to appropriately manage the employees and ensure that employees act in a safe and sound manner and comply with applicable laws. The board of directors must properly oversee and manage these activities in accordance with the best interests of the association to ensure that:

- Senior management hires and retains persons whose corporate loyalties run exclusively to the association to evaluate and manage dual employee activities.
- The association clearly sets forth in properly drafted and administered employment contracts all dual employment relationships.

Conflicts of Interest

Determining the existence of conflicts is an important aspect of your review since members of the board of directors may engage in similar or related activities. You should familiarize yourself with the types of regulatory concerns addressed in OTS's conflicts of interest regulation at § 563.200. Specifically, no person may advance their own personal or business interests, or those of others with whom they have a personal or business relationship, at the expense of the association. If directors or employees have an interest in a matter before the board, they should:

- Disclose to the board of directors all material nonprivileged information relevant to the board's decision. Such information includes the existence, nature and extent of the conflicting interest and any facts known to the person concerning the activity under consideration.
- Refrain from participating in any board discussion of the matter.
- Recuse themselves if they are directors.

For additional guidance, see Handbook Section 380, Transactions with Affiliates and Insiders.

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Usurpation of Corporate Opportunity

OTS regulation § 563.201 prohibits natural persons and companies who owe a fiduciary duty to a savings association from taking advantage of corporate opportunities belonging to their savings association or its subsidiaries. Before engaging in any new activity, the board of directors should be alert to the following situations:

- The opportunity is within the corporate powers of the savings association or its subsidiary.
- The opportunity is or will be a practical advantage to the savings association, directly or through its subsidiary.

When evaluating whether an opportunity poses an advantage to the savings association, fiduciaries should consider the following factors:

- The financial condition and management resources of the association.
- Both the level of risk that the opportunity presents and the potential profit from the opportunity weighed against any profits that might arise from the transfer of the opportunity.

OTS has opined that usurpation of corporate opportunity does not apply in the following situations:

- An institution received fair market value consideration for transfer of the opportunity.
- A disinterested and independent majority of the savings association's board of directors, upon receiving a complete and unbiased presentation of the matter, rejected the opportunity as a matter of sound business judgment.

Usurpation of corporate opportunity applies to dealings between savings associations and their holding companies. Therefore, when you review any savings association activities that involve the holding company, you should consult with the holding company examiners. See also, Examination Handbook Section 380, Transactions with Affiliates and Insiders, and the Holding Company Handbook.

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Quality Control

Before initiation of any new activity, the association should perform a comprehensive review to ensure that there is a risk management process in place to adequately assess, control, and monitor any risks arising from the proposed new activity.

Lack of follow-up is the biggest problem with most new activities. A formal follow-up program helps the association to ensure that the association achieves the results it desires. Plans and execution can be perfect, but lack of follow-up limits the chances for success and minimizes the association's effectiveness. Savings associations should not only monitor new activities and services but review as part of their follow up procedures the scope, design, implementation, testing, risk and quality assurance process, approval, delivery, training, sales, and stress-testing process to identify and resolve any problems with implementation.

REFERENCES

United States Code (12 USC)

Depository Institutions Deregulation and Monetary Control Act, Pub. L. 96-221, March 31, 1980

Garn-St. Germain Depository Institutions Act, Pub. L. 97-320, October 15, 1982

Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. 101-73, August 9, 1989

Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), Pub. L. 102-242, December 19, 1991

Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA)

Home Owners' Loan Act (HOLA) 57 FR 48942, 48943 (October 29, 1992)

§ 1462a(b) Establishment of Position of Director

§ 1463(a) Federal Savings Associations

§ 1463(c) Stringency of Standards

§ 1464(a), (b), and (c) In general, Deposits and related powers, and Loans and investments

Federal Deposit Insurance Act

§ 1828(m) Activities of Thrifts and Subsidiaries

§ 1831e Activities of Savings Associations

Code of Federal Regulations (12 CFR)

FDIC Rules

Part 327 Assessments

Part 362 Activities of Insured State Banks and Insured Savings Associations

OTS Rules

Part 516 Application Processing Procedures

§ 545.2 Federal Preemption

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§ 545.16(a)(4)(b)	Authority to Act as Surety for Public Deposits
§ 545.92	Branch Offices
§ 545.101	Fiscal Agency
Part 557	Deposits
§ 559.3	Characteristics of and the Requirements that Apply to Subordinate Organizations of Federal Savings Associations
§ 559.4	Activities Approved for Service Corporations
§ 560.2	Lending and Investments - Applicability of Law
§ 560.30	General Lending and Investment Powers of Federal Savings Associations
§ 560.32	Pass-through Investments
Part 562	Regulatory Reporting Standards
§ 563.39	Employment Contracts
§ 563.41	Loans and Other Transactions with Affiliates and Subsidiaries
§ 563.190	Bonds for Directors, Officers, Employees, and Agents; Form of and Amount of Bonds
§ 563.200	Conflicts of Interest
§ 563.201	Corporate Opportunity
Part 565	Prompt Corrective Action
Part 567	Capital
Part 590	Usury

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Office of Thrift Supervision Guidance

Regulatory and Thrift Bulletins

RB 3b	Policy Statement on Growth for Savings Associations
RB 18 series	Enforcement Policy

TB 13a	Management of Interest Rate Risk, Investment Securities, and Derivative Activities
TB 72a	Interagency Guidance on High Loan-to-Value Residential Real Estate Lending
TB 82a	Third-Party Arrangements

CEO Letters

CEO Letter 311	Risk Management: Asset and Liability Concentrations, July 9, 2009

Other Guidance

Directors' Responsibilities Guide, April 2008.

Directors' Guide to Management Reports, April 2008.

OTS Customer Service Plan, External Interpretive Opinions, April 2000.

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