

FORM OF ORDER AND TRANSMITTAL BY AGENCY HAVING SINGLE HEAD

State of Washington

Department of General Administration

(agency name)

Administrative Order No. 69

(1) I, Thomas H. Oldfield, director of the Division of Banking, Department of General Administration

do promulgate and adopt at Olympia, Washington (place)

the annexed rules relating to:

Adding new sections to Chapter WAC 50-12, regarding legal lending limits and extension of credit guidelines.

(2) ALTERNATIVE A. Use only for Adoption of Permanent Rules.

This action is taken pursuant to Notice No. 87-16-108 filed with the code reviser on 8-5-87. These rules shall take effect: [X] thirty days after they are filed with the code reviser pursuant to RCW 34.04.040(2). [] at a later date, such date being

(2) ALTERNATIVE B. Use only for Adoption of Emergency Rules.

I, find that an emergency exists and that this order is necessary for the preservation of the public health, safety, or general welfare and that observance of the requirements of notice and opportunity to present views on the proposed action would be contrary to public interest. A statement of the facts constituting the emergency is:

These rules are therefore adopted as emergency rules to take effect upon filing with the code reviser.

(3) Pursuant to the requirements of RCW 34.04.026 that "every agency shall incorporate the most specific, but in no case omit all, of the following language alternatives when adopting or amending rules" fill in statement (a), (b), or (c) as appropriate:

[X] (a) This rule is promulgated pursuant to RCW 30.04.111 and is intended to administratively implement that statute.

[] (b) This rule is promulgated pursuant to RCW which directs that the

(agency) has authority to implement the provisions of

(name of act or RCW citation)

[] (c) This rule is promulgated under the general rule-making authority of the

(agency) as authorized in RCW

(4) The undersigned hereby declares that the agency has complied with the provisions of the Open Public Meetings Act (chapter 42.30 RCW), the Administrative Procedure Act (chapter 34.04 RCW) and the State Register Act (chapter 34.08 RCW) in the adoption of these rules.

(5) This order, after being first recorded in the order register of this agency, is herewith transmitted to the Code Reviser for filing pursuant to chapter 34.04 RCW and chapter 1-12 WAC.

APPROVED AND ADOPTED September 30 19 87

STATE OF WASHINGTON FILED

SEP 30 1987

By Thomas H. Oldfield, Supervisor Division of Banking Title

CODE REVISER'S OFFICE WSR 87.20.022

NEW SECTION

WAC 50-12-210 PROMULGATION. The division of banking, hereinafter referred to as the "division," after due and proper notice, and pursuant to the provisions of RCW 30.04.111 hereby adopts and promulgates the following rules and regulations, effective September 9, 1987.

NEW SECTION

WAC 50-12-220 PURPOSE. These rules and regulations are intended to prevent one individual, or relatively small group, from borrowing an unduly large amount of the bank's funds. Further, the intention is also to safeguard the bank's depositors by spreading the loans among a relatively large number of persons engaged in different lines of business.

NEW SECTION

WAC 50-12-230 DEFINITIONS. (1) The term "person" shall include an individual, sole proprietor, partnership, joint venture, association, trust, estate, business trust, corporation, sovereign government or agency, instrumentality, or political subdivision thereof, or any similar entity or organization.

(2) The term "loans and extensions of credit" means any direct or indirect advance of funds to a person made on a basis of any obligation of that person to repay the funds, or repayable from specific property pledged by or on behalf of a person. "Loans and extensions of credit" also includes a "contractual commitment to advance funds" as that term is defined in this section, and includes a renewal, modification, or extension of the maturity date of a loan or extension of credit.

(3) The term "contractual commitment to advance funds" means:

(a) An obligation on the part of the bank to make payments (directly or indirectly) to a designated third party contingent upon a default by the bank's customer in the performance of an obligation under the terms of that customer's contract with the third party; or

(b) An obligation to guarantee or stand as surety for the benefit of a third party. The term includes, but is not limited to, standby letters of credit, guarantees, puts, and other similar arrangements. Undisbursed loan funds, loan commitments not yet drawn upon which do not fall under this definition, and commercial letters of credit or similar instruments are not considered contractual commitments to advance funds.

(4) The term "readily marketable collateral" means financial instruments and bullion which are saleable under ordinary circumstances with reasonable promptness at a fair market value determined by daily quotations based on actual transactions on an auction or a similarly available daily bid and ask price market.

(5) The term "financial instruments" shall include stocks, notes, bonds, and debentures traded on a national securities exchange, "OTC margin stocks" (as defined in Regulation U of the Federal Reserve Board), commercial paper, negotiable certificates of deposit, bankers' acceptances, and shares in money market and mutual funds of the type which issue shares in which banks may perfect a security interest.

(6) The term "current market value" means the bid or closing price listed for an item in a regularly published listing or an electronic reporting service.

(7) The term "capital" will include the amount of common stock outstanding and unimpaired, the amount of preferred stock outstanding and unimpaired, and capital notes or debentures issued pursuant to chapter 30.36 RCW.

(8) The term "surplus" shall include capital surplus, reflecting the amounts paid in excess of the par or stated value of capital stock, or amounts contributed to the bank other than for capital stock, and amounts transferred to surplus from undivided profits pursuant to resolution of the board of directors.

(9) The term "subsidiary" means:

(a) Any company twenty-five percent or more of whose voting shares (excluding shares owned by the United States or by any company wholly owned by the United States) is directly or indirectly owned or controlled by such person, or is held by it with power to vote;

(b) Any company the election of a majority of whose directors is controlled in any manner by such person; or

(c) Any company with respect to the management or policies of which such person has power, directly or indirectly, to exercise a controlling influence, as determined by the division, after notice and opportunity for hearing.

NEW SECTION

WAC 50-12-240 GENERAL LIMITATIONS. The total loans and extensions of credit by a state bank or trust company to a person outstanding at one time and not fully secured by collateral in a manner defined in WAC 50-12-250 shall not exceed twenty percent of the capital and surplus of the bank or trust company.

NEW SECTION

WAC 50-12-250 GENERAL LIMITATION--LOANS FULLY SECURED BY READILY MARKETABLE COLLATERAL. (1) Loans or extensions of credit by a state bank to a person outstanding at one time and fully secured by readily marketable collateral having a market value, as determined by reliable and continuously available price quotations, shall not be subject to any limitations based on capital and surplus. However, if the total of such loans and extensions of credit, together with loans made under general limitations pursuant to WAC 50-12-040 exceed forty-five percent, the division of banking will review the credits as a possible concentration, with regard to both risk diversification within the bank's asset structure and diversification or other risk in the marketable collateral securing the loan. This limitation shall be separate and in addition to the general twenty percent limitation set forth in WAC 50-12-240.

(2) Each loan or extension of credit based on the foregoing limitation shall be secured by readily marketable collateral having a current market value of at least one hundred fifteen percent of the amount of the loan or extension of credit at all times.

(3) Financial instruments may be denominated in foreign currencies which are freely convertible to United States dollars. If collateral is denominated and payable in a currency other than that of the loan or extension of credit which it secures, the bank's procedures must require that the collateral be revalued at least monthly, using appropriate foreign exchange rates, in addition to being repriced at current market value.

(4) Each bank must institute adequate procedures to ensure that the collateral value fully secures the outstanding loan at all times. If collateral values fall below one hundred fifteen percent of the

outstanding loan, to the extent that the loan is no longer in conformance with this section and exceeds the general twenty percent limitation, the loan must be brought into conformance within five business days, except where judicial proceedings, regulatory actions, or other extraordinary occurrences prevent the bank from taking actions.

NEW SECTION

WAC 50-12-260 COMBINING LOANS TO SEPARATE BORROWERS. (1) Loans or extensions of credit to one person will be attributed to other persons when:

(a) The proceeds of the loans or extensions of credit are to be used for the direct benefit of the other person or persons; or

(b) A "common enterprise" exists between the persons.

(2) Determination of whether a "common enterprise" exists depends upon a realistic evaluation of the facts and circumstances of the particular transaction. A "common enterprise" is presumed to exist when:

(a) The expected source of repayment for each loan or extension of credit is the same for each person; or

(b) Separate persons borrow from a bank for the purpose of acquiring a business enterprise of which those persons will own more than fifty percent of the voting securities; or

(c) The loans or extensions of credit are made to persons who are related by common control and (i) are engaged in interdependent business or (ii) there is substantial financial interdependence among them.

(3) Substantial financial interdependence occurs when fifty percent or more of one person's gross receipts or gross expenditures (on an annual basis) are derived from transactions with one or more persons related through common control. Gross receipts and expenditures include gross revenues/expenses, intercompany loans, dividends, capital contributions, and similar receipts or payments.

(4) Throughout this section the term "control" is presumed to exist when one or more persons acting in concert directly or indirectly:

(a) Own, control, or have power to vote twenty-five percent or more of any class of voting securities of another person;

(b) Exercise a controlling influence over the management or policies of another person; or

(c) Control in any manner the election of a majority of the directors, trustees or other persons exercising similar functions of another person. "Common control" includes control of one person by another person.

NEW SECTION

WAC 50-12-270 LOANS TO CORPORATIONS. Loans or extensions of credit to a person and its subsidiaries or to subsidiaries of one person need not be combined where the bank has determined that the person and subsidiaries involved are not engaged in a "common enterprise." If members of a corporate group (a person and all its subsidiaries) are either:

(1) Substantially financially interdependent; or

(2) Engaged in "common enterprise," then the total amount of loans or extensions of credit to these persons must be attributed to each of the other persons in the corporate group. Conversely, if members of a corporate group are neither substantially financially interdependent nor engaged in "common enterprise," then the loans to

different members are separately subject to a twenty percent limitation. In no event may the total amount of loans or extensions of credit by a state bank to a corporate group exceed fifty percent of the bank's capital and surplus.

NEW SECTION

WAC 50-12-280 LOANS TO PARTNERSHIPS, JOINT VENTURES, AND ASSOCIATIONS. (1) Loans or extensions of credit to a partnership, joint venture, or association shall, for purposes of WAC 50-12-210 through 50-12-300, be considered loans or extensions of credit to each member of such partnership, joint venture, or association.

(2) Loans or extensions of credit to members of a partnership, joint venture, or association are considered loans or extensions of credit to the partnership, joint venture, or association if one or more of the tests presented in WAC 50-12-260(1) is satisfied with respect to one or more of the members. However, loans to members of a partnership, joint venture or association will not be attributed to other members of the partnership, joint venture, or association unless one or more of the tests set forth in WAC 50-12-260(1) is satisfied with respect to such other members. The tests set forth in WAC 50-12-260(1) shall be deemed satisfied when loans or extensions of credit are made to members of a partnership, joint venture, or association for the purpose of purchasing an interest in such partnership, joint venture, or association.

(3) The rule set forth in subsection (1) of this section is not applicable to limited partners in limited partnerships or to members of joint ventures if such partners or members, by the terms of the partnership or membership agreement are not to be held liable for the debts or actions of the partnerships, joint venture, or association. However, the rules set forth in WAC 50-12-260(1) are applicable to such partners or members.

NEW SECTION

WAC 50-12-290 EXCEPTIONS TO THE LENDING LIMITS. (1) Discount of commercial or business paper: Loans or extensions of credit arising from the discount of commercial or business paper evidencing an obligation to the person negotiating it with recourse shall not be subject to any limitation based on capital and surplus.

(a) This exception applies to negotiable paper given in payment of the purchase price of commodities in domestic or export transactions purchased for resale or to be used in the fabrication of a product, or to be used for any other business purposes which may reasonably be expected to provide funds for payment of the paper. Loans or extensions of credit arising from the discount of paper must bear the full recourse endorsement of the owner. However, loans or extensions of credit arising from the discount of such paper in export transactions may be endorsed by such owner without recourse or with limited recourse, or may be accompanied by a separate agreement for limited recourse; provided, that if transferred without full recourse the paper must be supported by an assignment of appropriate insurance covering the political, credit, and transfer risks applicable to the paper.

(b) Since the basis for unlimited credit stems from the anticipated sale of a commodity to provide funds for payment of the paper, failure to pay either principal or interest when due removes the reason for unlimited credit. Consequently, although the line of credit

to the maker or endorser should not be classified as excessive by reason of such default, the paper on which the default occurred must thereafter be taken into consideration in determining whether additional loans or extensions of credit may be made. These same principles of disqualification apply to any renewal or extension of either the entire loan or an installment thereof.

(2) Bankers' acceptances: The purchase of banker's acceptances of the kind described in section 13 of the Federal Reserve Act and issued by other banks shall not be subject to any limitation based on capital and surplus.

(a) Acceptances by a state bank of "ineligible" drafts, i.e., time drafts which do not meet the requirements for discount with a Federal Reserve Bank, are subject to the general twenty percent limitation of RCW 30.04.111.

(b) During any period within which a state bank holds its own acceptances, eligible or ineligible, having given value therefor, the amount given is considered to be a loan or extension of credit to the customer for whom the acceptance was made and is subject to the lending limits. To the extent that a loan or extension of credit created by discounting the acceptance is covered by a bona fide participation agreement, the discounting bank need only consider that portion of the discounted acceptance which it retains as being subject to appropriate limitations.

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

(a) This exception allows a state bank to make loans or extensions of credit to one person in an amount equal to thirty-five percent of its capital and surplus in addition to the general twenty percent limitation.

(b) A readily marketable staple means an article of commerce, agriculture, or industry of such uses as to make it the subject of dealings in a ready market with sufficiently frequent price quotations as to make (i) the price easily and definitely ascertainable, and (ii) the staple itself easy to realize upon sale at any time at a price which would not involve any considerable sacrifice from the amount at which it is valued as collateral. Staples eligible for this exception must be nonperishable, may be refrigerated or frozen, and must be fully covered by insurance when such insurance is customary. This exception is intended to apply primary to basic commodities, such as wheat and other grains, cotton, wool, and basic metals such as tin, copper, lead, and the like. Whether a commodity is readily marketable depends upon existing conditions and it is possible that a commodity that qualifies at one time may cease to qualify at a later date. Fabricated commodities which do not constitute standardized interchangeable units and do not possess uniformly broad marketability do not qualify as readily marketable staples.

(c) Commodities sometimes fail to qualify as nonperishable because of the manner in which they are handled or stored during the life of the loan or extension of credit. Accordingly, the question as to whether a staple is nonperishable must be determined on a case-by-case basis.

(d) This exception is applicable to a loan or extension of credit arising from a single transaction or secured by the same staples for (i) not more than ten months if secured by nonperishable staples, and (ii) not more than six months if secured by refrigerated or frozen staples.

(e) The important characteristic of warehouse receipts, order bills of lading, or other similar documents is that the holder of such

documents has control of the commodity and can obtain immediate possession. (However, the existence of brief notice periods, or similar procedural requirements under state law, for the disposal of the collateral will not affect the eligibility of the instruments for this exception.) Only documents with these characteristics are eligible security for loans under this exception. In the event of default on a loan secured by one of these documents, the bank must be in a position to sell the underlying commodity and promptly transfer title and possession to the purchaser, thus being able to protect itself without extended litigation. Generally, documents qualifying as "documents of title" under the Uniform Commercial Code are "similar documents" qualifying for this exception.

(f) Field warehouse receipts are an acceptable form of collateral when they are issued by a duly bonded and licensed grain elevator or warehouse having exclusive possession and control of the commodities even though the grain elevator or warehouse is maintained on the commodity owner's premise.

(g) Warehouse receipts issued by the borrower-owner which is a grain elevator or warehouse company, duly-bonded and licensed and regularly inspected by state or federal authorities, may be considered eligible collateral under this exception only when the receipts are registered with a registrar whose consent is required before the commodities can be withdrawn from the warehouse.

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

(a) This exception applies only to loans or extensions of credit which are fully secured by the current market value of obligations of the United States or guaranteed by the United States.

(b) If the market value of the collateral declines so that the loan is no longer in conformance with this exception and exceeds the general twenty percent limitation, the loan must be brought into conformance within five business days.

(c) Securities issued by any department, agency, bureau, board, commission or establishment of the United States, or any corporation wholly owned, directly or indirectly, shall not be considered eligible collateral for purposes of this section, unless such securities shall be direct obligation of or fully guaranteed as to principal and interest by the United States.

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

(a) This exception may apply to only that portion of a loan or extension of credit that is covered by a federal guarantee or commitment.

(b) For purposes of this exception, the commitment or guarantee must be payable in cash or its equivalent within sixty days after demand for payment is made.

(c) A guarantee or commitment is unconditional if the protection afforded the bank is not substantially diminished or impaired in the case of loss resulting from factors beyond the bank's control. Protection against loss is not materially diminished or impaired by procedural requirements, including default over a specific period of time, a requirement that notification of default be given within a specific period after its occurrence, or a requirement of good faith on the part of the bank.

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

(a) Deposit accounts which may qualify for this exception include deposits in any form generally recognized as deposits. In the case of

the secured loan, the bank must establish internal procedures which will prevent the release of the security.

(b) The bank must ensure that a security interest has been perfected in the deposit, including the assignment of a specifically identified deposit and any other actions required by state law.

(c) A deposit which is denominated and payable in a currency other than that of the loan or extension of credit which it secures may be eligible for this exception if it is freely convertible to United States dollars. The deposit must be revalued at least monthly, using appropriate foreign exchange rates, to ensure that the loan or extension of credit remains fully secured. This exception applies to only that portion of the loan or extension of credit that is covered by the United States dollar value of the deposit. If the United States dollar value of the deposit falls to the extent that the loan is in nonconformance with this exception and exceeds the general twenty percent limitation, the loan must be brought into conformance within five business days, except where judicial proceedings, regulatory actions, or other extraordinary occurrences prevent the bank from taking such action. This exception is not authority for state banks to take deposits denominated in foreign currencies.

(7) Unpaid purchase price of sale of bank property: The unpaid portion of the purchase price of a sale of bank property, if secured by that property, shall not be subject to any limitation based on capital and surplus.

(a) Any sale of bank property, resulting in an unpaid purchase price exceeding the bank's lending limit must be approved in advance of the sale by the board of directors, including the terms of payment of such unpaid purchase price, and if the purchase is by a director, officer or employee of the bank, shall conform to Regulation O of the Federal Reserve System and RCW 30.12.050.

(b) The bank must ensure that a security interest has been perfected in the collateral, including execution and recording or filing of documents and any other action required by state law.

(8) Discount of installment consumer paper.

(a) Loans and extensions of credit arising from the discount of negotiable or nonnegotiable installment consumer paper which carries a full recourse endorsement or unconditional guarantee by the person transferring the paper shall be subject under this section to a maximum limitation equal to twenty per centum of capital and surplus.

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

(c) This exception allows a bank to discount negotiable or nonnegotiable installment consumer paper of one person in an amount equal to twenty per centum of its capital and surplus if the paper carries a full recourse endorsement or unconditional guarantee by the seller transferring such paper. The unconditional guarantee may be in the form of a repurchase agreement or a separate guarantee agreement. A condition reasonably within the power of the bank to perform, such as the repossession of collateral, will not be considered to make conditional an otherwise unconditional agreement.

(d) For purposes of this subsection, "consumer" means the user of any products, commodities, goods, or services, whether leased or purchased, and does not include any person who purchases products or commodities for the purpose of resale or for fabrication into goods for sale.

(e) For purposes of this subsection, "consumer paper" includes paper relating to automobiles, mobile homes, residences, office equipment, household items, tuition fees, insurance premium fees, and similar consumer items. Also included is paper covering the lease (where

the bank is not the owner or lessor) or purchase of equipment for use in manufacturing, farming, construction, or excavation.

(f) Under certain circumstances, installment consumer paper which otherwise meets the requirements of this exception will be considered a loan or extension of credit to the maker of the paper rather than the seller of the paper. Specifically, where (i) through the bank's files it has been determined that the financial condition of each maker is reasonably adequate to repay the loan or extension of credit and (ii) an officer designated by the bank's chairman or chief executive officer pursuant to authorization by the board of directors certifies in writing that the bank is relying primarily upon the maker to repay the loan or extension of credit, the loan or extension of credit is subject only to the lending limits of the maker of the paper. Where paper is purchased in substantial quantities, the records, evaluation, and certification may be in such form as is appropriate for the class and quantity of paper involved.

(g) If a loan under this section is in default and the dealer or seller of the loan has contractually committed to repurchase the paper, then the loan will be aggregated with the dealer or seller's other outstanding debt for lending limit purposes and will be subject to the twenty per centum limitation.

(h) If loan payments are received and/or controlled by the dealer or seller of the paper and remitted to the bank, then those loans will be aggregated with the dealer or seller's other outstanding debt for lending limit purposes and will be subject to the twenty per centum limitation.

NEW SECTION

WAC 50-12-300 TRANSITIONAL RULES. (1) Loans or extensions of credit which were in violation of RCW 30.04.111 prior to the relevant effective dates of WAC 50-12-210 through this section will be considered to remain in violation of law until they are paid in full, regardless of whether the loans or extensions of credit conform to the rules established in WAC 50-12-210 through this section. Renewals or extensions of such loans or extensions of credit will also be considered violations of law.

(2) A state bank which has outstanding loans or extensions of credit to a person in violation of RCW 30.04.111 as of the relevant effective dates of WAC 50-12-210 through this section may make additional advances to such person after those dates if the additional advances are permitted under WAC 50-12-210 through this section. The additional advances, however, may not be used directly or indirectly to repay any outstanding illegal loans or extensions of credit.

(3) Loans or extensions of credit which were in conformance with RCW 30.04.111 prior to the relevant effective dates of WAC 50-12-210 through this section but are not in conformance with the rules established in WAC 50-12-210 through this section will not be considered to be violations of law during the existing contract terms of such loans or extensions of credit. Renewals or extensions of such loans or extensions of credit which are not in conformance with WAC 50-12-210 through this section may be made on or after the effective dates of WAC 50-12-210 through this section, if the nonconformity is caused by the amendments to Title 30 RCW contained in ESSE 4917; however, all loans or extensions of credit made under such renewals or extensions must conform with WAC 50-12-210 through this section no later than April 1, 1988. Loans or extensions of credit which are not in conformance with WAC 50-12-210 through this section for any other reason (i.e., a reduction in the bank's capital) must conform to this section upon renewal or extension.

(4) If a state bank, prior to the relevant effective dates of WAC 50-12-210 through this section, entered into a legally binding commitment to advance funds on or after those dates, and such commitment was

in conformance with RCW 30.04.111, advances under such commitment may be made notwithstanding the fact that such advances are not in conformance with WAC 50-12-210 through this section. The bank must, however, demonstrate that the commitment represents a legal obligation to fund, either by a written agreement or through file documentation. Advances under renewals or extensions of such extension of the commitment is made on or after the relevant effective dates of WAC 50-12-210 through this section.