Dated at Rockville, Maryland, this 11th day of December, 1996.

For the Nuclear Regulatory Commission.

John C. Hoyle,

Secretary of the Commission.

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DEPARTMENT OF THE TREASURY

Office of the Comptroller of the Currency

12 CFR Part 23

[Docket No. 96–28]

RIN 1557–AB45

Leasing

AGENCY: Office of the Comptroller of the Currency, Treasury.

ACTION: Final rule.

SUMMARY: The Office of the Comptroller of the Currency (OCC) is revising its rules governing the personal property lease financing transactions of national banks. This final rule, which is another component of the OCC's Regulation Review Program, updates and streamlines the rules. The final rule is substantively similar to the OCC's proposal but incorporates modifications reflecting suggestions made by commenters and further clarifies and simplifies the rule.

EFFECTIVE DATE: January 17, 1997.

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SUPPLEMENTARY INFORMATION:

Introduction

The OCC is revising 12 CFR part 23, which governs personal property lease financing transactions by national banks. This final rule is another component of the OCC's Regulation Review Program. The principal goal of the Program is to review all of the OCC's rules with a view toward eliminating or revising provisions that do not contribute significantly to maintaining the safety and soundness of national banks or to accomplishing the OCC's other statutory responsibilities. Another important goal is to clarify regulations to more effectively convey the standards the OCC seeks to apply.

As the OCC indicated in its notice of proposed rulemaking (proposal), the agency's experience suggests that, while a wholesale substantive rewrite of part 23 is not warranted,[1] changes to improve clarity and to provide some additional flexibility would be appropriate. See 60 FR 46246 (Sept. 6, 1995). Accordingly, the proposal shortened and streamlined part 23; reorganized many of its provisions; added paragraph headings; and conformed its style to that of the OCC's other rules. In addition, the OCC identified and specifically requested comment on several areas where substantive changes to the regulation might be appropriate, depending on the responses received.

The OCC received 11 comments in response to the proposal, which the OCC has carefully considered in preparing this final rule. The commenters included national banks, a national bank subsidiary, and trade associations representing both banks and leasing companies. The commenters generally supported the proposal, and a few suggested further modifications or improvements. The final rule incorporates suggestions made by some of the commenters, and the OCC has made additional changes to clarify and simplify the regulatory text. The final rule also makes other minor technical changes.

The *Discussion* portion of this preamble contains a section-by-section description of the final rule and the significant changes from the proposed version. A derivation table showing modifications from the former part 23 appears at the conclusion of this preamble.

Background

National banks may engage in leasing activities pursuant to two independent sources of authority. First, under 12 U.S.C. 24 (Seventh), a national bank may acquire tangible and intangible personal property for the purpose of, or in connection with leasing that property when the lease is the functional equivalent of a loan (Section 24 (Seventh) Leases).[2] The OCC has interpreted the functional equivalency requirement to mean that a Section 24 (Seventh) Lease must be a ''net,'' ''full-payout'' lease and any unguaranteed portion of the estimated residual value of the leased property must not exceed 25% of the original cost of the property. The ''net'' lease requirement means that the lessor national bank may not be obligated to provide specified services such as repairs or maintenance, or purchase insurance on the lessee's behalf in connection with the leased property. The ''full-payout'' requirement means that the bank must expect to recover the full costs of acquiring the property to be leased and financing the leasing transaction from sources that include rentals, estimated tax benefits, and the estimated residual value of the property at the end of the lease. For a Section 24(Seventh) Lease, however, the bank may rely on the unguaranteed portion of the estimated residual value of the leased property only to a limited extent—not more than 25% of the original cost of the property. There is no percentage-of-assets limit on a national bank's investment in Section 24 (Seventh) Leases.

In 1987, Congress gave national banks a second, explicit source of authority to engage in personal property lease financing. The Competitive Equality Banking Act (CEBA)[3] amended 12 U.S.C. 24 by adding paragraph Tenth, which allows a national bank to invest in tangible personal property, including vehicles, manufactured homes, machinery, equipment, and furniture, for lease financing transactions (CEBA Leases). Investment in personal property to be leased under the authority of 12 U.S.C. 24(Tenth) may not exceed 10 percent of a national bank's assets. A CEBA Lease also must be a ''net'' lease and a ''full-payout'' lease, but is not subject to a maximum estimated residual value limit. Both Section 24(Seventh) Leases and CEBA Leases are governed by standards set forth in part 23.

Discussion

Subpart A—General Provisions

Authority, Purpose, and Scope (§ 23.1)

The proposal retained the authority provision of the former regulation but added paragraphs describing the purpose of part 23 and the scope of its respective subparts. The final rule retains the structure described in the scope section of the part 23 proposal.

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[1] The OCC first adopted part 23 in mid-1991. 56 FR 28314 (June 20, 1991). Part 23 replaced an earlier OCC interpretive ruling on lease financing transactions, which had been codified at 12 CFR 7.3400.

[2] *See M & M Leasing Corp.* v. *Seattle First National Bank*, 563 F.2d 1377 (9th Cir. 1977), *cert. denied*, 436 U.S. 956 (1978) (upholding national banks' authority under 12 U.S.C. 24(Seventh) to engage in personal property lease financing transactions if the lease is the functional equivalent of a loan) (*M&M Leasing*).

[3] Pub. L. 100–86, sec. 108, 101 Stat. 552, 579 (Aug. 10, 1987). See also S. Rep. No. 19, 100th Cong., 1st Sess. 43 (1987) (explanation of purpose of CEBA's expansion of national banks' leasing authority).

Subpart A contains definitions and standards applicable to both Section 24 (Seventh) Leases and CEBA Leases. Subpart B contains standards unique to CEBA Leases, and subpart C contains standards unique to Section 24 (Seventh) Leases. The scope section of the final rule also is revised to state that part 23 applies to the acquisition of personal property by a national bank for the purpose of, or in connection with, the leasing of that property.

Definitions (§ 23.2)

The proposal added to part 23 a new section defining significant terms, including *CEBA Lease, conforming lease, off-lease property,* and *Section 24 (Seventh) Lease,* for the purpose of making the operative provisions of the regulation shorter and easier to read. These terms are adopted substantially as proposed. The OCC has shortened the definition of the term *net lease* by removing the explicit acknowledgment that a national bank may lease improvements and additions to the leased property to the lessee in accordance with any applicable residual value requirements. The OCC believes that this portion of the text was unnecessary because the activity it describes is not otherwise prohibited by the regulation. Thus, the removal of this language does not substantively alter a national bank's ability to lease improvements and additions to its lessees.

As is explained in this discussion under ''Investment in personal property,'' the final rule permits a national bank to acquire property for leasing purposes even if the bank has not entered into a conforming lease, a commitment to enter into a conforming lease, or an indemnification agreement. For prudential reasons, however, this authority is subject to an aggregate limit based on the bank's capital and surplus. Accordingly, the OCC has added to the final rule a definition of the term *capital and surplus* that is consistent with the way this term is defined in other OCC regulations, such as 12 CFR part 32, which governs national banks' lending limits.

The OCC has also added to this section a revised definition of the term affiliate that cross-references the definition of that term at § 23.6. The definition had appeared in § 23.7 of the proposal.

The OCC proposed to define a *full-payout lease* as a lease financing transaction in which any unguaranteed portion of the estimated residual value relied upon by the bank to yield the return of its full investment in the leased property, plus the estimated cost of financing the property over the term of the lease, does not exceed 25 percent of the original cost of the property to the lessor. The OCC asked commenters to address whether the 25 percent limit contained in this definition should be increased or modified. As discussed in the proposal, the OCC had selected the 25 percent limit in 1979 based in part on its experience at that time in examining and supervising banks engaged in Section 24(Seventh) lease financing activities.[4] Congress subsequently gave national banks authority to enter into CEBA Leases, which are not subject to a maximum residual value limit (though the aggregate cost of the personal property acquired for the purpose of CEBA Lease transactions is restricted in aggregate amount to 10 percent of a national bank's total consolidated assets). The proposal noted, however, that national banks did not appear to be engaged in CEBA leasing to the full extent of their statutory authority and it asked whether, under these circumstances, a change in the residual value limit for Section 24(Seventh) Leases was appropriate. Commenters supporting a more flexible limit were asked to identify any increased risk that would accompany a new limit and to discuss how the OCC should address that risk.

Five commenters addressed this issue. The majority favored no modification to the limit, pointing out that whenever it is appropriate to exceed the 25 percent limit, banks may use their CEBA leasing authority instead. Based on the comments and the OCC's more recent experience with national banks' lease financing activities, the OCC has concluded that the 25 percent residual value limit for Section 24(Seventh) Leases does not inhibit national banks from competing effectively with other providers of lease financing. The final rule retains the 25 percent residual value requirement for Section 24(Seventh) Leases,[5] but the requirement is relocated to subpart C, which applies only to Section 24(Seventh) Leases.

The OCC has concluded that combining the cost recovery requirement with the residual value limit, which was the approach taken in the proposed version of part 23, is confusing because it obscures the fact that a bank must receive its acquisition and financing costs in order for any lease, including a CEBA Lease, to be economically viable. The OCC believes that part 23 will be easier to read and to use if the requirement for cost recovery is separately stated in the subpart applicable to both Section 24(Seventh) Leases and CEBA Leases, and the percentage limit on residual value continues to appear in the subpart addressing Section 24(Seventh) Leases, which are the only leases subject to that limit. Accordingly, the OCC has revised the proposed definition of the term *full-payout lease.* The final rule defines that term to specify the sources on which a national bank may rely to recover both its investment in the leased property and the estimated cost of financing the property over the lease term. The 25 percent residual value limit applicable to Section 24(Seventh) Leases is relocated to § 23.21 of the final rule.

Lease Requirements (§ 23.3)

The former rule and proposed § 23.3 both required that a national bank entering into a lease financing transaction must reasonably expect to recover its full investment in the leased property, as well as its estimated financing costs over the life of the lease, from three sources: rentals, estimated tax benefits, and the estimated residual value of the leased property. The cost recovery requirement applies both to CEBA Leases and to Section 24(Seventh) Leases. As described in the preceding section, the final rule defines the term *full-payout lease* to specify these three sources of cost recovery. Thus, § 23.3(a) of the final rule simply states the requirement that all of a national bank's leases must be full-payout leases. These changes in the final rule—the revised definition of *full-payout lease,* the relocation of the 25 percent residual value limit to subpart C, and the statement of the full-payout requirement in § 23.3(a)—do not change the substantive effect of the revisions as proposed.

The proposal also added to the regulation a new paragraph containing an explicit statement of the requirement that a national bank may engage in a lease financing transaction, and in activities incidental to the transaction, provided the lease is a net lease. The incidental activities clause in proposed

[4] See 44 FR 22388, 22390 (April 13, 1979) (adoption of interpretive rule establishing estimated residual value limit of 25 percent for leases that serve as the functional equivalent of loans).

[5] The 25 percent limit is the same as the limit that the Federal Reserve Board (FRB) currently applies to full-payout personal property leasing by bank holding companies (BHCs) and their subsidiaries under Regulation Y (addressing the permissible non-banking activities of BHCs). See 12 CFR 225.25(b)(5). The FRB, however, has recently proposed revisions to Regulation Y that could result in changes to its personal property leasing standards. See 61 FR 47242, 47251–52, 47273–74 (Sept. 6, 1996).

The Office of Thrift Supervision has recently increased its analogous residual value limit from 20 percent to 25 percent. See 61 FR 50951, 50960 (Sept. 30, 1996).

§ 23.4(a) reflected the OCC's long-standing interpretations authorizing national banks to engage in activities incidental to leasing. The proposal also confirmed the OCC's position that there is no safety or soundness reason for treating activities incidental to leasing differently depending on the underlying source of statutory authority for the leasing transaction, and that a national bank may therefore engage in approved incidental activities with respect both to Section 24(Seventh) Leases and CEBA Leases. Since both the ''full-payout'' requirement and the ''net'' lease requirement apply to Section 24(Seventh) Leases and CEBA Leases, § 23.3(a) of the final rule contains the general requirement that a national bank may acquire personal property for the purpose of, or in connection with leasing that property, provided the lease qualifies as a full-payout lease and a net lease. Section 23.3(a) also provides that national banks may engage in activities that are incidental to permissible personal property acquisition and leasing transactions.

In the proposal, the OCC did not include a list of permissible activities incidental to leasing, but it invited commenters to address the desirability of retaining a case-by-case approach to determining permissible incidental activities. Six commenters responded to this request. All but one commenter urged that the OCC retain the case-by-case approach because any ''laundry list'' appearing in the regulation would become out of date quickly. The OCC agrees with the commenters that a list would soon become obsolete and will therefore retain the case-by-case approach.

The OCC also requested comment on whether it should, on a case-by-case basis, permit national banks to acquire and lease real estate when the real estate acquisition and lease is incidental to a personal property lease financing transaction. The incidental leasing of real estate could occur, for example, in a so-called ''facility'' leasing transaction, which one commentator has described as follows:

> [A] facility is a ''stand-alone'' complex that functions either as a separate operating unit or as a discrete component of an integrated operating system. A facility has at least four basic components: An interest in the real property site upon which the rest of the facility is situated; improvements to the site, usually including a structure of some sort; equipment or other tangible personal property, usually the asset actually being financed in the transaction; and intangible property such as contracts, licenses, or other ancillary rights and benefits that are necessary or desirable for the operation or support of the other components of the facility. A facility is practicably immovable as an entirety.[6]

The six commenters who addressed this issue urged that the OCC permit real estate leasing if it is incidental to the lease financing of personal property. The commenters asserted that, in a competitive leasing environment, national banks and national bank-owned leasing companies suffer a competitive disadvantage with respect to certain types of transactions—particularly facility lease financing arrangements—if they are prohibited from acquiring and leasing real estate in all circumstances.

The commenters also thought that acquiring and leasing real estate as a component of a personal property lease financing transaction would better protect the bank's collateral interest in the leased property and therefore enhance the safety and soundness of the transaction. For example, they said, improvements to fuel storage facilities, manufacturing facilities or other installed equipment have a greater collateral value ''in place, in use'' than they would have if they were removed and re-sold in the event of default. Thus, if a lessee defaults under a personal property lease of this type, a lessor bank having the right to foreclose on and sell or re-lease the personal property in place on the site or in the building is in a better financial position than a bank that must remove the equipment and dispose of it separately.

The OCC agrees that under some circumstances real estate leasing may be an incidental component of a personal property leasing transaction. Therefore, consistent with its decision to retain a case-by-case approach to activities incidental to leasing generally, the OCC will determine the permissibility of personal property lease financing transactions that have a real estate leasing component based upon the facts of a given lease financing transaction (or multiple lease financing transactions, if they present essentially similar facts). This will enable the OCC to review any safety or soundness or other supervisory concerns that particular transactions may present.

The OCC notes that the activities incidental to leasing that it has authorized to date for national banks acting as lessors include providing management, marketing, and administrative services and offering credit life insurance to lessees.[7] The OCC has also authorized national banks to engage in incidental activities with respect to lease financing transactions to which the bank is not a party. These activities include providing lease consulting services such as financial advice; providing management, brokerage, and finder services; and performing lease servicing for third parties.[8]

Finally, § 23.3(b) includes provisions (proposed as § 23.4(b)) specifying the conditions under which a national bank may take appropriate action to protect its interests and the distress clause permitting a national bank to take certain actions to salvage or protect its investment. Section 23.3(b) of the final rule has been shortened and slightly revised, but these changes do not change the substantive effect of the provision.

Investment in Personal Property (§ 23.4)

Like the former rule, proposed § 23.5(a) specifically authorized a national bank to acquire personal property to be leased after the bank had entered into either a legally binding agreement indemnifying the bank against loss in connection with the acquisition or a legally binding commitment to enter into a conforming lease. The purpose of this provision was to prevent the speculative acquisition of personal property. The OCC believes, however, that measures other than flatly prohibiting a national bank from acquiring property before the leasing arrangements are essentially completed will provide adequate safeguards against speculation. Accordingly, § 23.4(b) of the final rule authorizes a national bank to acquire property to be leased in the absence of a commitment to enter into a conforming lease, or an indemnification agreement, if the bank satisfies certain conditions demonstrating that the acquisition of property is not speculative. These

[6] Anthony D. Schlesinger, Special Concerns in Facility Leveraged Lease Transactions, 1 *Equipment Leasing—Leveraged Leasing* 987, 987 (B. Fritch, A. Reisman & I. Shrank eds. 1988) (Practicing Law Institute Publication No. A3–1406).

[7] See, e.g., Letter from H. Joe Selby, First Deputy Comptroller for Operations, Nov. 24, 1976 (unpublished); Letter from Peter Liebesman, Assistant Director, Legal Advisory Services Division, Jan. 14, 1985 (unpublished). Copies of unpublished OCC staff interpretive letters are available (in redacted form) upon request from the Communications Division, 250 E Street, SW., Washington, DC 20219 (202) 874–4700.

[8] See, e.g., 12 CFR 7.1002; OCC Interpretive Ltr. No. 567 (Oct. 29, 1991) reprinted in [1991–92 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶83,337; Letter from Wallace S. Nathan, District Counsel, Oct. 28, 1985 (unpublished); Letter from Peter Liebesman, Assistant Director, Legal Advisory Services Division, June 15, 1981 (unpublished). See also OCC Interpretive Ltr. No. 741 (Aug. 19, 1996) reprinted in [Current Binder] Fed. Banking L. Rep. (CCH) ¶81–105. Copies of the unpublished letters are available from the Communications Division, see note 7 above.

conditions require that: (1) The acquisition of the property either be consistent with the leasing business then conducted by the bank or with a business plan for the expansion of the bank's existing leasing business or for entry into the leasing business; and (2) the bank's aggregate investment in property under this provision not exceed 15 percent of the bank's capital and surplus.

The 15 percent limit applies to all property acquired under § 23.4(b) of the final rule, whether the lease will be entered into pursuant to 12 U.S.C. 24(Seventh) or 24(Tenth). However, property acquired under this provision does not count toward the 10 percent volume limitation on CEBA Leases until the bank enters into a conforming lease, a legally binding commitment to lease, or an indemnification agreement pursuant to § 23.10 of the final rule.

The OCC has also added to § 23.4(a) of the final rule an explicit statement that a national bank may acquire property after entering into a conforming lease, as well as after entering into a lease commitment or an indemnification agreement. The OCC has incorporated this change, which was requested by a commenter, to clarify the flexibility available under the regulation.

The former rule required that a national bank dispose of or re-lease off-lease property as soon as practicable, but not later than two years from the date the lease expires. Proposed § 23.2(e) defined *off-lease* property as property that reverts to a bank's possession or control upon the expiration of a lease or upon the default of the lessee. Proposed § 23.5(b) was substantively the same as the former rule, but it specifically provided that the two-year holding period runs either from the date the lease expires (including any renewals or extensions with the same lessee) or the date of the lessee's default. Both Section 24(Seventh) Leases and CEBA Leases are subject to this holding period limitation.

Extension of off-lease holding period. The preamble to the proposal indicated that the OCC was considering whether to extend the holding period for off-lease property but lacked data on the experiences national banks have had in attempting to liquidate or re-lease specific kinds of off-lease property within the two-year holding period. The proposal did not change the holding period but requested comment on four issues:

(1) Should the holding period be extended and, if so, should it be extended for all categories of assets or only for particular categories?

(2) If the holding period were extended, what would be a reasonable additional time period, in general or for particular categories of assets?

(3) What evidence supports extension of the holding period?

(4) If the holding period were extended, how should the OCC ensure that banks do not use the longer period to retain property for essentially speculative purposes?

The proposal also invited banks to provide specific comment on their experiences in attempting to sell or re-lease specific kinds of off-lease personal property with respect to the issue of extending the holding period.

Seven commenters responded. One commenter thought that in most cases the two-year holding period is appropriate. The others offered various suggestions for liberalizing the regulation, including: Extending the holding period for specific assets—such as airplanes, rail cars, vessels, oil rigs, machine tools, manufacturing equipment—characterized as ''historically cyclic''; extending the holding period generally but with conditions, such as requiring banks to make diligent sales efforts or obtain annual appraisals of the off-lease assets; substituting the holding period regulations applicable to other real estate owned property (OREO) for the existing provision;[9] or simply extending the holding period in cases of market distress.

In light of the discussion provided by the commenters on this point, the OCC concludes that it is appropriate to provide for a longer holding period for off-lease property. Section 23.4(c) of the final rule adopts a five-year holding period generally and provides for the holding period to be extended for up to an additional five years if the bank provides a clearly convincing demonstration as to why any additional holding period is necessary. The initial five-year rule is consistent with the time prescribed for the disposition of OREO, but the OCC expects that a bank will usually be able to dispose of off-lease personal property more quickly than real estate. Accordingly, the OCC will require a ''clearly convincing'' demonstration of necessity in order to justify any extension of the holding period for off-lease property beyond five years.

Section 23.4(c) of the final rule retains the requirement that off-lease property be valued at the lower of fair market or book value. The OCC notes that, consistent with generally accepted accounting principles, this valuation should occur promptly after the property comes off-lease.

Commencement of off-lease holding period. As indicated earlier in this discussion, the holding period for off-lease property commences on either the date of expiration of the lease or the date of the lessee's default, depending on the reason that the national bank takes possession or control of the leased property. This language conveys that the holding period begins when the bank is in a position to dispose of or re-lease the property, that is, when it takes possession or control.

Five commenters, however, asked for further clarification on when the holding period commences in the event the lessee defaults before the expiration of the term of the lease. Some commenters pointed out that while the preamble to the proposal and the proposed definition of *off-lease property* refer to a national bank's taking possession or control of the leased property, the proposed regulatory text itself did not contain the ''possession or control'' language. Moreover, as the commenters pointed out, *actual* possession or control of an asset alone may not allow the bank to dispose of it or re-lease it. In foreclosure or bankruptcy situations, the bank may need to obtain a court order establishing its *legal* right to do so.

The OCC agrees with the commenters that the provision requires clarification and adjustment to cover situations such as bankruptcy or foreclosure. Section 23.4(c) of the final rule therefore provides that the OCC will measure the five-year period beginning on the date that the national bank obtains the legal right to possession or control of the asset. This date could be the date that the lease expires or the date that the lessee defaults if, for example, the national bank has a clear contractual right to repossess the property at that time and the lessee does not physically impede it from doing so. Where the bank must establish its legal right to the property, however, the five-year period will begin when the bank has completed that step. The OCC notes that this treatment is consistent with the way it administers the holding period for OREO.[10]

[9] 12 U.S.C. 29 requires a national bank to dispose of OREO within five years from the date of acquisition and authorizes the OCC, under certain circumstances, to grant a bank an additional five years in which to dispose of the property.

[10] *See* 12 CFR 34.82 (b) and (c) (five-year holding period for OREO does not begin until after ownership of property is transferred to the bank; in foreclosure situations in states with statutory rights of redemption, holding period does not begin until statutory redemption period has expired).

Section 23.4(d) of the final rule reflects minor technical changes from the proposal to conform with the revised off-lease holding period provision in § 23.4(c).

Requirement for Separate Records (§ 23.5)

Proposed § 23.6 retained the requirement in the former rule that national banks maintain separate records for CEBA Leases and Section 24(Seventh) Leases. The OCC received no comments on this provision and adopts it as proposed, except to renumber it as § 23.5.

Application of Lending Limits; Restrictions on Transactions With Affiliates (§ 23.6)

Like the former rule, proposed § 23.7 subjected lease financing transactions to lending limits and transactions-with-affiliates restrictions. The proposal, however, clarified that the transactions-with-affiliates restrictions apply only if the lessee is an affiliate of the lessor bank. In any other case, lending limits restrictions apply. The proposal also retained the reservation of the OCC's authority to impose other limits or restrictions.

One commenter requested that the OCC state specifically that nonrecourse debt is excluded from the value of the leased property in computing the appropriate lending limit position. This commenter noted that although the regulatory text did not address the point, the preamble to the former rule specifically addressed the issue.[11]

This issue typically arises in leveraged lease transactions, that is, transactions in which a national bank borrows from a third-party creditor a portion of the funds necessary to purchase the property to be leased. In these cases, the third-party creditor's loan to the bank is often on a nonrecourse basis, so that the creditor looks only to the lease payments and its security interest in the leased property as the source of repayment for its loan to the bank and does not rely on the general credit of the bank. In this type of transaction, the bank's exposure to loss in the event of the lessee's default is mitigated to the extent that the bank has used outside funding to finance the transaction. For this reason, the OCC permits a national bank to use the recorded investment in a lease net of any nonrecourse debt the bank has incurred to finance the acquisition of the asset to be leased, for the purpose of measuring whether the bank's leases comport with the appropriate lending limits. This treatment is also consistent with generally accepted accounting principles.

The commenter is therefore correct about the treatment of nonrecourse debt. The final rule states that for the purpose of measuring compliance with the lending limits, a national bank records the investment in a lease net of any nonrecourse debt the bank has incurred to finance the acquisition of the leased asset. The OCC has revised § 23.7 to this effect, and renumbered it as § 23.6 in the final rule.

Applicability of Consumer Leasing Act (Removed)

The former rule stated that nothing in part 23 could be construed to be in conflict with the duties, liabilities, and standards imposed by the Consumer Leasing Act of 1976, 12 U.S.C. 1667 *et seq.* (CLA). The OCC proposed to remove this provision because other consumer protection laws and regulations may also apply to personal property lease financing activities, making the cross-reference potentially misleading and confusing. The OCC received no comments on this portion of the proposal and § 23.6 of the former rule is removed. This change does not affect the applicability of the CLA or any other consumer credit laws to national banks' lease financing activities, however. National banks still must know and comply with the full range of requirements that govern these activities.

Subpart B—CEBA Leases

Provisions Applicable to CEBA Leases (§§ 23.10, 23.11, and 23.12)

Proposed §§ 23.8, 23.9, and 23.10 contained the requirements applicable to CEBA Leases, including a statement of the general rule authorizing investment in personal property in connection with CEBA Leases, the limits placed on a national bank's exercise of its CEBA leasing authority, and a transition rule for CEBA Leases entered into after CEBA's enactment but before the effective date of the OCC's final implementing rule in 1991. The substance of these provisions as proposed was the same as the former rule.

The OCC received one comment on these provisions. The commenter who asked that the rule specifically address the exclusion of nonrecourse debt in connection with the computation of lending limits for leases also asked that nonrecourse debt be specifically excluded in measuring compliance with the 10 percent of assets limitation applicable to CEBA Leases. The OCC has permitted this treatment since it promulgated part 23 in 1991. Section 23.10 of the final rule states this position.

This commenter also asked whether the OCC intended any meaningful distinction between ''tangible personal property'' as used in proposed § 23.8 and ''personal property'' as used in proposed § 23.11. The reference to ''tangible personal property'' in proposed § 23.8 derives from the statutory language authorizing CEBA Leases. Section 24(Tenth) requires that CEBA Leases must be leases for tangible personal property. A national bank wishing to acquire and lease intangible personal property, such as patents, copyrights or other forms of intellectual property, must rely on its authority under section 24(Seventh). For these reasons, the final rule continues to use the phrase ''tangible personal property'' with respect to CEBA Leases. With respect to Section 24(Seventh) Leases, the final rule refers to tangible or intangible personal property. The OCC received no comments on proposed §§ 23.9 and 23.10, and adopts them as proposed, except to renumber them as §§ 23.11 and 23.12.

Subpart C—Section 24(Seventh) Leases

General rule (§ 23.20)

Proposed § 23.11 stated the general rule authorizing national banks to engage in lease financing pursuant to 12 U.S.C 24(Seventh). The OCC received no comments on this section, other than the request for clarification, noted in this discussion under ''Provisions applicable to CEBA Leases,'' with respect to the use of two different terms in proposed §§ 23.8 and 23.11. The OCC adopts this section with minor changes from the proposal, except that it removes as redundant the requirements in proposed § 23.11 that the lease must be a full-payout and net lease, and renumbered the section as § 23.20.

Estimated Residual Value (§ 23.21)

Proposed § 23.12 contained provisions that apply to a national bank's reliance on or estimate of residual value in Section 24(Seventh) leasing transactions. These provisions were substantively the same as the requirements of the former rule, including: (1) A provision that the amount of any estimated residual value guaranteed by a manufacturer, the lessee, or other third party that is not an affiliate of the bank may exceed 25 percent of the original cost of the property if the bank determines that the guarantor has the resources to meet the

[11] *See* 56 FR 28314, 28316 (June 20, 1991) (preamble to part 23 final rule).

guarantee and can document its determination; (2) a requirement that the estimated residual value amounts be reasonable given the type of property leased and other relevant circumstances, so that realization of the lessor bank's full investment and the cost of financing the property primarily depends on the creditworthiness of the lessee and any guarantor of the residual value, and not on the residual market value of the leased item; and (3) a provision that, when a bank leases personal property to a government entity, its estimates of residual value may be based on future transactions that it reasonably anticipates will occur.

The OCC received no comments on this section. The OCC made the following revisions in the final rule: Renumbered it as § 23.21, moved the 25% residual value limit that had appeared in proposed § 23.2(c) to this section for the reason discussed in this preamble under ''Definitions,'' and removed the last sentence of proposed § 23.12(a), which stated that the bank must depend primarily on the creditworthiness of the lessee (and any guarantor) and not on the residual value of the leased property. The OCC removed this sentence because it is redundant in light of the relocation of the 25 percent limit which appears in the final version of this section. The restrictions on Section 24(Seventh) leasing in subparts A and C are designed to ensure that the bank depends primarily on the credit of the lessee, and not on the residual value of the leased property at the end of the lease term.

Transition Rule (§ 23.22)

The former rule and proposed § 23.13 provide that leases executed before June 12, 1979, which was the effective date of the OCC's final rule amending 12 CFR 7.3400 to reflect the Ninth Circuit's decision in the *M&M Leasing* case, are not subject to part 23, and prescribe rules for renewing those leases. The OCC received no comments on this section and it remains unchanged, except for renumbering it as § 23.22.

DERIVATION TABLE

[This table directs readers to the provision(s) of the former regulation, if any, upon which the final rule is based.]

Revised provision	Original provision	Comments
§ 23.1	§ 23.1(a)	Modified.
§ 23.2(a), (b), (c), (d), (g), (h).		Added.
§ 23.2(e)	§ 23.1(b)	Modified.
§ 23.2(f)	§ 23.2(a)	Modified.
§ 23.3(a)		Added.
§ 23.3(b)	§ 23.2(b), (c), (d).	Modified.
§ 23.4(a)	§ 23.3(a)	Modified.
§ 23.4(b)		Added.
§ 23.4(c)	§ 23.3(b)	Modified.
§ 23.4(d)	§ 23.3(c)	Modified.
§ 23.5	§ 23.4	Modified.
§ 23.6	§ 23.5	Modified.
	§ 23.6	Removed.
§ 23.10	§ 23.7	Modified.
§ 23.11	§ 23.8	Modified.
§ 23.12	§ 23.9	Modified.
§ 23.20	§ 23.10	Modified.
§ 23.21	§ 23.11	Modified.
§ 23.22	§ 23.12	Modified.

Regulatory Flexibility Act

It is hereby certified that this final rule will not have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required. This final rule will reduce the regulatory burden on national banks, regardless of size, by simplifying and clarifying existing regulatory requirements.

Paperwork Reduction Act of 1995

The OCC invites comments on:

(1) Whether the collections of information contained in this notice of final rule are necessary for the proper performance of OCC functions, including whether the information has practical utility;

(2) The accuracy of the estimate of the burden of the information collections;

(3) Ways to enhance the quality, utility, and clarity of the information to be collected;

(4) Ways to minimize the burden of the information collections on respondents, including through the use of automated collection techniques or other forms of information technology; and

(5) Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

Respondents/recordkeepers are not required to respond to the foregoing collections of information unless this displays a currently valid OMB control number.

The collections of information contained in this final rule have been approved by the Office of Management and Budget (OMB) through June 30, 1997, in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)), under OMB Control No. 1557–0206. Comments on the collections of information should be sent to the Office of Management and Budget, Paperwork Reduction Project (1557–0206), Washington, DC 20503, with a copy to the Legislative and Regulatory Activities Division, Office of the Comptroller of the Currency, 250 E Street, SW., Washington, DC 20219. The OCC will submit the collections of information contained in this final rule for renewal of OMB approval following publication of this final rule.

The collections of information in this final rule are found in 12 CFR 23.4(c) and 23.5. These collections of information are necessary in order for a national bank to submit a request to the OCC for permission to extend the holding period of off-lease property, to maintain records according to generally accepted accounting principles and Federal law, and to ensure bank safety and soundness. The likely respondents/recordkeepers are national banks.

Estimated average annual burden hours per respondent/recordkeeper: 2.8.

Estimated number of respondents and/or recordkeepers: 660.

Estimated total annual reporting and recordkeeping burden: 1,820.

Start-up costs to respondents: None.

Executive Order 12866

OMB has concurred with the OCC's determination that this final rule is not a significant regulatory action under Executive Order 12866.

Unfunded Mandates Reform Act of 1995

The OCC has determined that the requirements of this final rule will not result in expenditures by State, local, and tribal governments, or by the private sector, of $100 million or more in any one year. Accordingly, a budgetary impact statement is not required under section 202 of the Unfunded Mandates Reform Act of 1995. As discussed in the preamble, this final rule has the effect of reducing burden and increasing the efficiency of lease financing transactions undertaken by national banks.

List of Subjects in 12 CFR Part 23

Banks, banking, Lease financing transactions, Leasing, National banks, Reporting and recordkeeping requirements.

Authority and Issuance

For the reasons set out in the preamble, part 23 of chapter I of title 12 of the Code of Federal Regulations is revised to read as follows:

PART 23—LEASING

Subpart A—General Provisions

Subpart B—CEBA Leases

Subpart C—Section 24(Seventh) Leases

Authority: 12 U.S.C. 1 *et seq.*, 24(Seventh), 24(Tenth), and 93a.

Subpart A—General Provisions

§ 23.1 Authority, purpose, and scope.

(a) *Authority.* A national bank may engage in personal property lease financing transactions pursuant to 12 U.S.C. 24(Seventh) or 12 U.S.C. 24(Tenth).

(b) *Purpose.* The purpose of this part is to set forth standards for personal property lease financing transactions authorized for national banks.

(c) *Scope.* This part applies to the acquisition of personal property by a national bank for the purpose of, or in connection with, the leasing of that property.

§ 23.2 Definitions.

(a) *Affiliate* means an affiliate as described in § 23.6.

(b) *Capital and surplus means:*

(1) A bank's Tier 1 and Tier 2 capital calculated under the OCC's risk-based capital standards set forth in appendix A to 12 CFR part 3 as reported in the bank's Consolidated Report of Condition and Income filed under 12 U.S.C. 161; plus

(2) The balance of a bank's allowance for loan and lease losses not included in the bank's Tier 2 capital, for purposes of the calculation of risk-based capital described in paragraph (b)(1) of this section, as reported in the bank's Consolidated Report of Condition and Income filed under 12 U.S.C. 161.

(c) *CEBA Lease* means a personal property lease authorized under 12 U.S.C. 24(Tenth).

(d) *Conforming lease* means:

(1) A CEBA Lease that conforms with the requirements of subparts A and B of this part; or

(2) A Section 24(Seventh) Lease that conforms with the requirements of subparts A and C of this part.

(e) *Full-payout lease* means a lease in which the national bank reasonably expects to realize the return of its full investment in the leased property, plus the estimated cost of financing the property over the term of the lease, from:

(1) Rentals;

(2) Estimated tax benefits; and

(3) The estimated residual value of the property at the expiration of the lease term.

(f) *Net lease* means a lease under which the national bank will not, directly or indirectly, provide or be obligated to provide for:

(1) Servicing, repair, or maintenance of the leased property during the lease term;

(2) Parts or accessories for the leased property;

(3) Loan of replacement or substitute property while the leased property is being serviced;

(4) Payment of insurance for the lessee, except where the lessee has failed in its contractual obligation to purchase or maintain required insurance; or

(5) Renewal of any license or registration for the property unless renewal by the bank is necessary to protect its interest as owner or financier of the property.

(g) *Off-lease property* means property that reverts to a national bank's possession or control upon the expiration of a lease or upon the default of the lessee.

(h) *Section 24(Seventh) Lease* means a personal property lease authorized under 12 U.S.C. 24(Seventh).

§ 23.3 Lease requirements.

(a) *General requirements.* A national bank may acquire personal property for the purpose of, or in connection with leasing that property, and may engage in activities incidental thereto, if the lease qualifies as a full-payout lease and a net lease.

(b) *Exceptions*—(1) *Change in condition.* If, in good faith, a national bank believes that there has been a change in condition that threatens its financial position by increasing its exposure to loss, then the bank may:

(i) Take reasonable and appropriate action, including the actions specified in § 23.2(f), to salvage or protect the value of the leased property or its interests arising under the lease; and

(ii) Acquire or perfect title to the leased property pursuant to any existing rights.

(2) *Provisions to protect the bank's interests.* A national bank may include any provision in a lease, or make any additional agreement, to protect its financial position or investment in the event of a change in conditions that would increase its exposure to loss.

(3) *Arranging for services by a third party.* A national bank may arrange for a third party to provide any of the services enumerated in § 23.2(f) to the lessee at the expense of the lessee.

§ 23.4 Investment in personal property.

(a) *General rule.* A national bank may acquire specific property to be leased only after the bank has entered into:

(1) A conforming lease;

(2) A legally binding written agreement that indemnifies the bank against loss in connection with its acquisition of the property; or

(3) A legally binding written commitment to enter into a conforming lease.

(b) *Exception.* A national bank may acquire property to be leased without complying with the requirements of paragraph (a) of this section, if:

(1) The acquisition of the property is consistent with the leasing business then conducted by the bank or is consistent with a business plan for expansion of the bank's existing leasing business or for entry into the leasing business; and

(2) The bank's aggregate investment in property held pursuant to this paragraph (b) does not exceed 15 percent of the bank's capital and surplus.

(c) *Holding period.* At the expiration of the lease (including any renewals or extensions with the same lessee), or in the event of a default on a lease agreement prior to the expiration of the lease term, a national bank shall either liquidate the off-lease property or re-lease it under a conforming lease as soon as practicable. Liquidation or re-lease must occur not later than five years from the date that the bank acquires the legal right to possession or control of the property, except the OCC may extend the period for up to an additional five years, if the bank provides a clearly convincing demonstration why any additional holding period is necessary. The bank must value off-lease property at the lower of current fair market value or book value promptly after the property becomes off-lease property.

(d) *Bridge or interim leases.* During the holding period allowed by paragraph (c) of this section, a national bank may enter into a short-term bridge or interim lease pending the liquidation of off-lease property or the re-lease of the property under a conforming lease. A short-term bridge or interim lease must be a net lease, but need not

comply with any requirement of subpart B or C of this part.

§ 23.5 Requirement for separate records.

If a national bank enters into both CEBA Leases and Section 24(Seventh) Leases, the bank's records must distinguish the CEBA Leases from the Section 24(Seventh) Leases.

§ 23.6 Application of lending limits; restrictions on transactions with affiliates.

A lease entered into pursuant to this part is subject to the lending limits prescribed by 12 U.S.C. 84 or, if the lessee is an affiliate of the bank, to the restrictions on transactions with affiliates prescribed by 12 U.S.C. 371c and 371c–1. The OCC may also determine that other limits or restrictions apply. The term affiliate means an affiliate as defined in 12 U.S.C. 371c or 371c–1, as applicable. For the purpose of measuring compliance with the lending limits prescribed by 12 U.S.C. 84, a national bank records the investment in a lease net of any nonrecourse debt the bank has incurred to finance the acquisition of the leased asset.

Subpart B—CEBA Leases

§ 23.10 General rule.

Pursuant to 12 U.S.C. 24(Tenth) a national bank may invest in tangible personal property, including vehicles, manufactured homes, machinery, equipment, or furniture, for the purpose of, or in connection with leasing that property, if the aggregate book value of the property does not exceed 10 percent of the bank's consolidated assets and the related lease is a conforming lease. For the purpose of measuring compliance with the 10 percent limit prescribed by this section, a national bank records the investment in a lease entered into pursuant to this subpart net of any nonrecourse debt the bank has incurred to finance the acquisition of the leased asset.

§ 23.11 Lease term.

A CEBA Lease must have an initial term of not less than 90 days. A national bank may acquire property subject to an existing lease with a remaining maturity of less than 90 days if, at its inception, the lease was a conforming lease.

§ 23.12 Transition rule.

(a) *General rule.* A CEBA Lease entered into prior to July 22, 1991, may continue to be administered in accordance with the lease terms in effect as of that date. For purposes of applying the lending limits and the restrictions on transactions with affiliates described in § 23.6, however, a national bank that enters into a new extension of credit to a customer, including a lease, on or after July 22, 1991, shall include all outstanding leases regardless of the date on which they were made.

(b) *Renewal of non-conforming leases.* A national bank may renew a CEBA Lease that was entered into prior to July 22, 1991, and that is not a conforming lease only if the following conditions are satisfied:

(1) The bank entered into the CEBA Lease in good faith;

(2) The expiring lease contains a binding agreement requiring that the bank renew the lease at the lessee's option, and the bank cannot reasonably avoid its commitment to do so; and

(3) The bank determines in good faith, and demonstrates by appropriate documentation, that renewal of the lease is necessary to avoid financial loss and to recover its investment in, and its cost of financing, the leased property.

Subpart C—Section 24(Seventh) Leases

§ 23.20 General rule.

Pursuant to 12 U.S.C. 24(Seventh) a national bank may invest in tangible or intangible personal property, including vehicles, manufactured homes, machinery, equipment, furniture, patents, copyrights, and other intellectual property, for the purpose of, or in connection with leasing that property, if the related lease is a conforming lease representing a noncancelable obligation of the lessee (notwithstanding the possible early termination of that lease).

§ 23.21 Estimated residual value.

(a) *Recovery of investment and costs.* A national bank's estimate of the residual value of the property that the bank relies upon to satisfy the requirements of a full-payout lease, for purposes of this subpart:

(1) Must be reasonable in light of the nature of the leased property and all circumstances relevant to the transaction; and

(2) Any unguaranteed amount must not exceed 25 percent of the original cost of the property to the bank.

(b) *Estimated residual value subject to guarantee.* The amount of any estimated residual value guaranteed by the manufacturer, the lessee, or other third party may exceed 25 percent of the original cost of the property if the bank determines, and demonstrates by appropriate documentation, that the guarantor has the resources to meet the guarantee and the guarantor is not an affiliate of the bank.

(c) *Leases to government entities.* A bank's calculations of estimated residual value in connection with leases of personal property to Federal, State, or local governmental entities may be based on future transactions or renewals that the bank reasonably anticipates will occur.

§ 23.22 Transition rule.

(a) *Exclusion.* A Section 24(Seventh) Lease entered into prior to June 12, 1979, may continue to be administered in accordance with the lease terms in effect as of that date. For purposes of applying the lending limits and the restrictions on transactions with affiliates described in § 23.6, however, a national bank that enters into a new extension of credit to a customer, including a lease, on or after June 12, 1979, shall include all outstanding leases regardless of the date on which they were made.

(b) *Renewal of non-conforming leases.* A national bank may renew a Section 24(Seventh) Lease that was entered into prior to June 12, 1979, and that is not a conforming lease only if the following conditions are satisfied:

(1) The bank entered into the Section 24(Seventh) Lease in good faith;

(2) The expiring lease contains a binding agreement requiring that the bank renew the lease at the lessee's option, and the bank cannot reasonably avoid its commitment to do so; and

(3) The bank determines in good faith, and demonstrates by appropriate documentation, that renewal of the lease is necessary to avoid financial loss and to recover its investment in, and its cost of financing, the leased property.

Dated: December 10, 1996.

Eugene A. Ludwig,

Comptroller of the Currency.

[FR Doc. 96–31967 Filed 12–17–96; 8:45 am]

BILLING CODE 4810–33–P

Office of Thrift Supervision

12 CFR Parts 545, 559, 560, 563, 567, 571

[No. 96–119]

RIN 1550–AA88

Subsidiaries and Equity Investments

AGENCY: Office of Thrift Supervision, Treasury.

ACTION: Final rule.

SUMMARY: The Office of Thrift Supervision (OTS or agency) is today issuing a final rule updating and substantially streamlining its regulations and policy statements concerning subsidiaries and other subordinate organizations in which