



**BOARD OF GOVERNORS**  
OF THE  
**FEDERAL RESERVE SYSTEM**  
WASHINGTON, D.C. 20551

DIVISION OF SUPERVISION  
AND REGULATION

**SR 17-9**  
**September 7, 2017**

**TO THE OFFICER IN CHARGE OF SUPERVISION  
AT EACH FEDERAL RESERVE BANK**

**SUBJECT: Supervisory Guidance for Examining Compliance with the Qualified Thrift  
Lender Test**

**Applicability:** This guidance applies to state savings banks and insured cooperative banks that are members of the Federal Reserve System and that have made an election pursuant to section 10(l) of the Home Owners' Loan Act for their parent holding companies to be treated as savings and loan holding companies.

The Federal Reserve is providing supervisory guidance regarding the Qualified Thrift Lender (QTL) test under section 10(m) of the Home Owners' Loan Act (HOLA).<sup>1</sup> Section 10(l) of HOLA permits a state savings bank or insured cooperative bank (referred to as an "electing bank") that meets the QTL test to be deemed a savings association solely for the purpose of determining the status of the electing bank's parent holding company as a savings and loan holding company (SLHC) under section 10 of HOLA.<sup>2</sup> Specifically, this letter provides an overview of the Federal Reserve's QTL requirements and the consequences of failing the QTL test for electing banks that are members of the Federal Reserve System and their parent holding companies. This letter also outlines procedures examiners should consider when assessing an institution's QTL compliance program.

**Eligibility**

A state-chartered savings bank is eligible to make an election under section 10(l) of HOLA if it transacts its ordinary banking business strictly as a savings bank under state laws imposing special requirements on such banks governing the manner of investing their funds and of conducting their business.<sup>3</sup> A bank that is not subject to such state laws is not eligible to make an election under section 10(l) of HOLA. A cooperative bank is eligible if its deposits are insured.<sup>4</sup>

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<sup>1</sup> 12 U.S.C. 1467a(m).

<sup>2</sup> 12 U.S.C. 1467a(l).

<sup>3</sup> 12 U.S.C. 1467a(l)(1) (cross referencing section 3(g) of the Federal Deposit Insurance Act (FDI Act), 12 U.S.C. 1813(g)).

<sup>4</sup> *Id.* (cross referencing section 3(h) of the FDI Act, 12 U.S.C. 1813(h), which defines insured banks).

## Qualified Thrift Lender Test

Upon application by an electing bank and a determination by the appropriate federal banking agency that the electing bank meets the QTL test, the electing bank's parent is treated as an SLHC subject to section 10 of HOLA and the Board's regulations concerning the operations and activities of SLHCs. In order to meet the QTL test, either (i) 65 percent or more of the electing bank's portfolio assets must be qualified thrift investments (QTIs), or (ii) the electing bank must qualify as a domestic building and loan association as defined in the Internal Revenue Code. For electing banks who meet the QTL test by holding the appropriate amount of QTIs, the electing bank's QTIs must continue to equal or exceed 65 percent of the electing bank's portfolio assets, on a monthly average basis, for nine out of any twelve month period.<sup>5</sup>

## Qualified Thrift Investments

Section 10(m) of HOLA provides instructions for calculating the proportion of an electing bank's portfolio assets that are QTIs. An electing bank's amount of QTIs equals the sum of (i) assets that are includable without limit and (ii) assets that are includable up to 20 percent of portfolio assets. Only the portion of a loan or investment that is used for purposes described below may be counted as a QTI.<sup>6</sup> Goodwill and other intangible assets are not QTIs.<sup>7</sup>

Section 10(m) defines portfolio assets as the sum of the electing bank's total assets *minus* (i) goodwill and other intangible assets, (ii) the value of property used by the electing bank to conduct its business, and (iii) liquid assets in an amount not to exceed 20 percent of the electing bank's total assets.<sup>8</sup>

### *Assets that are includable without limit:*

- Loans made to purchase, refinance, construct, improve, or repair domestic residential housing or manufactured housing.
- Home-equity loans.

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<sup>5</sup> 12 U.S.C. 1467a(m)(1)(B)(ii)

<sup>6</sup> See 12 U.S.C. 1467a(m)(4)(C)(v)(I).

<sup>7</sup> 12 U.S.C. 1467a(m)(4)(C)(v)(II).

<sup>8</sup> 12 U.S.C. 1467a(m)(4)(B)(i)-(iii). Liquid assets include: (1) cash; (2) balances maintained in a Federal Reserve bank, or passed through a Federal home loan bank or another depository institution to a Federal Reserve bank; (3) time and savings deposits in Federal home loan banks or commercial banks; (4) obligations of the United States and banker acceptances; (5) shares or certificates of any open-end management investment company registered with the U.S. Securities and Exchange Commission under the Investment Company Act of 1940 (the "SEC Act") and the portfolio of which is restricted by such investment company's investment policy, changeable only if authorized by shareholders vote, solely to any of the obligations or other investment enumerated in 12 U.S.C. 1465(A), (C)(i)-(ii), (iv)-(vii) (1999); (6) liquid, high-quality corporate debt obligations with three years or less remaining until maturity; (7) high-quality commercial paper with 270 days or less remaining until maturity; (8) mortgage-related securities that have one year or less remaining until maturity or are subject to an agreement to be purchased within one year by another insured depository institution that is in compliance with applicable capital standards, a primary dealer in U.S. government securities, or a broker or dealer registered under the SEC Act; and (9) mortgage loans on the security of a first lien on residential real property, if the mortgage loans qualify as backing for mortgage-backed securities issued by the Fannie Mae or Freddie Mac or guaranteed by the Ginnie Mae, and either the mortgage loans have one year or less remaining until maturity, or the mortgage loans are subject to an agreement of purchase (including a repurchase agreement, put option, right of redemption, or takeout commitment) that requires an insured depository institution that is in compliance with applicable capital standards to purchase the loans within one year. 12 U.S.C. 1467a(m)(4)(B)(iii).

- Securities backed by or representing an interest in mortgages on domestic residential housing or manufactured housing.
- Direct or indirect obligations of the Federal Deposit Insurance Corporation, Federal Savings and Loan Insurance Corporation (FSLIC), the FSLIC Resolution Fund, and the Resolution Trust Corporation issued pursuant to agreements entered into after July 1, 1989. These obligations are includable without limit only for five years from the date they were issued.
- Stock of Federal Home Loan Banks.
- Education loans, small business loans, and loans made through credit cards or credit card accounts.

*Assets that are includable up to 20 percent of portfolio assets:*

- 50 percent of the sum of residential mortgage loans originated by an electing bank and sold within 90 days of origination.
- Investments in a service corporation that derives at least 80 percent of its annual gross revenues from activities related to acquiring, refinancing, constructing, improving, or repairing domestic residential real estate or manufactured housing.
- 200 percent of the sum of loans and investments to acquire, develop, and construct one- to four-family residential real estate with a purchase price less than or equal to 60 percent of the area median value of similar newly-constructed residential real estate in the same community. A maximum of 25 percent of this amount may be attributed to loans and investments used for commercial property, but only if the commercial property serves the residents of the residential property related to the loan.
- 200 percent of the dollar amount of loans for the acquisition or improvement of residential real property, churches,<sup>9</sup> schools, and nursing homes, and loans for any other purpose to any small business, provided such loans are located within an area that has been identified in connection with a review or examination of community reinvestment practices by the Federal Reserve as a geographic area or neighborhood in which the credit needs of low- and moderate-income residents are not being met.
- Loans for purchasing, constructing, improving, or maintaining churches, schools, nursing homes, and hospitals (other than those reported as assets in the previous bullet).
- Loans for personal, family, or household purposes other than education loans, small business loans, and loans made through credit cards or credit card accounts.
- Shares of the Federal Home Loan Mortgage Corporation (Freddie Mac) or the Federal National Mortgage Association (Fannie Mae).

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<sup>9</sup> The term “churches” includes other places of worship.

Electing banks and examiners may refer to the Office of the Comptroller of the Currency (OCC) Qualified Thrift Lender Handbook for the following definitions: residential housing, manufacturing housing, and small business loans.<sup>10</sup>

### **Domestic Building and Loan Association**

An electing bank may also satisfy the QTL test if it qualifies as a domestic building and loan association, as defined in 26 U.S.C. 7701(a)(19).<sup>11</sup> The Internal Revenue Service has prescribed requirements for entities to qualify as domestic building and loan associations.<sup>12</sup>

### **Consolidation and Accounting Rules**

Section 10(m) of HOLA requires an electing bank to use the same consolidation and accounting rules when determining the bank's QTIs and portfolio assets.<sup>13</sup> An electing bank must consolidate the portfolio assets of its subsidiaries with the electing bank's portfolio assets if either (a) the electing bank also consolidates the assets of its subsidiaries to determine the electing bank's amount of QTIs, or (b) the electing bank also consolidates residential mortgage loans originated and sold by its subsidiaries within 90 days of origination to determine the electing bank's QTIs.

### **Consequence of Failing the QTL Test**

An electing bank that makes an effective election pursuant to section 10(l) of HOLA and later fails to meet the ongoing requirement of the QTL test is prohibited from being treated as a QTL and a savings association – and thus from having its parent holding company treated as an SLHC – for five years.<sup>14</sup> Consequently, the electing bank ceases to be treated as a savings association for purposes of HOLA, and its parent holding company must seek the Board's approval under section 3 of the Bank Holding Company Act of 1956, as amended, to be a bank holding company.<sup>15</sup>

### **Examination of QTL Compliance**

Electing banks and their primary federal bank supervisor are responsible for assessing compliance with the QTL test. In the case of electing banks that are state member banks, Federal Reserve examiners must confirm these institutions' QTL status during each full scope examination. Safety and soundness examiners should consider the attached examination procedures when assessing the QTL compliance of electing banks.

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<sup>10</sup> The *Comptroller's Handbook Qualified Thrift Lender (M-QTL)* is available at <https://occ.gov/publications/publications-by-type/comptrollers-handbook/m-ctl.pdf>

<sup>11</sup> 12 U.S.C. 1467a(m)(1)(A).

<sup>12</sup> See 26 CFR 301.7701-13A.

<sup>13</sup> 12 U.S.C. 1467a(m)(5)(A)-(B)

<sup>14</sup> 12 U.S.C. 1467a(l)(2).

<sup>15</sup> 12 U.S.C. 1842(a). Because the holding company would no longer enjoy treatment as an SLHC, it would meet the definition of "bank holding company" under the Bank Holding Company Act of 1956, as amended. 12 U.S.C. 1841(a).

Federal Reserve Banks are asked to distribute this letter to their supervised financial institutions and to appropriate supervisory and examination staff. Questions regarding this letter should be directed to the following individuals:

- Division of Supervision and Regulation: Karen Caplan, Manager SLHC Section, at (202) 452-2710; Elskin Butler, Supervisory Financial Analyst, at (202) 245-4226; or Josh Smolevitz, Financial Analyst, at (202) 912-7814.
- Legal Division: Michael Waldron, Special Counsel, at (202) 452-2798; Tate Wilson, Counsel, at (202) 452-3696; or Josh Strazanac, Attorney, at (202) 452-2457.

In addition, questions may be submitted via the Board's public website.<sup>16</sup>

Michael S. Gibson  
Director

**Attachment:**

- *Qualified Thrift Lender Examination Procedures*

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<sup>16</sup> See <http://www.federalreserve.gov/apps/contactus/feedback.aspx>.

## Qualified Thrift Lender Examination Procedures

September 7, 2017

### Examination Scope and Assessment

The purpose of these procedures is to help examiners determine whether a state savings bank or insured cooperative bank (referred to as an “electing bank”) meets the qualified thrift lender (QTL) test under section 10(m) of the Home Owners’ Loan Act (HOLA)<sup>1</sup> and has a satisfactory process to ensure ongoing compliance with the QTL test. These examination procedures are applicable only to electing banks in which the Federal Reserve has responsibility for assessing QTL compliance.

The scope of a QTL assessment should be commensurate with the electing bank’s risk of non-compliance with the QTL test. For example, if the electing bank is in danger of not meeting the QTL test, examiners should consider offsite monitoring by requesting reports from the institution in addition to the procedures discussed below. Examiners may consider a risk-focused review for an electing bank that has a history of compliance, qualified thrift investments (QTIs) that far exceed the minimum requirements, and satisfactory risk management practices.

### Examination Procedures

1. Review prior examination reports and/or examination work papers to identify any QTL related issues.
2. Verify that the electing bank is self-certifying its QTL status on the Call Report by completing:
  - RC-M line 15a, which asks for the electing bank to indicate whether it uses (1) the Home Owners' Loan Act (HOLA) QTL test or (2) the Internal Revenue Service Domestic Building and Loan Association (IRS DBLA) test to determine its QTL compliance.
  - RC-M line 15b, which asks the electing bank to indicate with a “yes” or “no” whether it has been in compliance with the HOLA test as of each month end during the quarter or qualified as a domestic building and loan association under the Internal Revenue Code for its most recent taxable year, as applicable.
3. Obtain the electing bank’s QTL work papers to determine the following:
  - The percentage of the electing bank’s portfolio assets that are QTIs.<sup>2</sup>
  - Whether the electing bank maintained QTIs of at least 65 percent of portfolio assets for nine of the preceding twelve months prior to the examination date. Examiners may consider sampling for a risk-based review.

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<sup>1</sup> 12 U.S.C. 1467a(m)(1).

<sup>2</sup> 12 U.S.C. 1467a(m)(4)(A).

- Verify that assets are categorized based on the applicable statutory definitions.<sup>3</sup>
  - Verify that the actual thrift investment percentage is accurate and consistent with HOLA.<sup>4</sup>
  - Determine the quality of the electing bank's work papers and whether they provide a reasonable audit trail.
4. Assess the electing bank's risk management practices and control systems.
- Determine whether QTL policies are satisfactory and periodically reviewed by the appropriate oversight committee.
  - Determine if risk management practices are sufficient to ensure ongoing compliance with QTL requirements, including whether the electing bank's staff and management have adequate training and knowledge of QTL compliance and procedures.
  - Determine if risk monitoring reports are timely, accurate, and provided periodically to senior management or the appropriate oversight committee.
  - Determine whether there are periodic audit and compliance reviews of proper scope and depth.
  - Determine if senior management considers QTL requirements for strategic planning, including acquisitions, new activities, or changes to the electing bank's balance sheet structure.
5. For an electing bank that fails to meet the QTL requirements, examiners should notify Board Legal and the SLHC Section of the Division of Supervision and Regulation. After consultation with Board staff, the Reserve Bank must notify the electing bank in writing of the QTL failure and the resulting consequence for the electing bank and its parent company.
6. Update the Supervisory Plan and Risk Assessment for the next exam cycle based on current exam findings.
- For an electing bank that is consistently in danger of failing the QTL test, examiners should consider whether additional quarterly monitoring is warranted.
  - Conversely, an electing bank that consistently exceeds the QTL requirement and has sufficient control systems may warrant a risk-focused review.

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<sup>3</sup> 12 U.S.C. 1467a(m)(4)(c)(ii), (iii). *See also* SR letter 17-9, "Supervisory Guidance for Examining Compliance with the Qualified Thrift Lender Test."

<sup>4</sup> 12 U.S.C. 1467a(m)(4)(A)