Office of Thrift Supervision

Department of the Treasury

Holding Companies

in the

Thrift Industry

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Index

RESPONSE TO RECENT QUESTIONS REGARDING THE APRIL 1997 BACKGROUND PAPER ON HOLDING COMPANIES IN THE THRIFT INDUSTRY

Executive Summary

In April 1997, the Office of Thrift Supervision ("OTS") published the Background Paper on Holding Companies in the Thrift Industry ("first holding company paper"). That paper reviewed the history of the major statutory, regulatory, and supervisory controls OTS maintains over thrift holding companies. It listed the types of holding companies supervised by OTS and their range of activities. Thrift holding companies' broader range of powers was also contrasted with bank holding companies' more limited powers. OTS's experience with commercial firms as thrift holding companies, as well as holding companies engaging in broader forms of "non-banking" activities[1], received particular attention in the first holding company paper.

OTS has received questions and requests for more detailed information concerning certain issues raised in the first holding company paper. This second holding company paper attempts to address these questions and requests. In addition, this paper updates the data for holding companies and thrifts through June 30, 1997. As with the first paper, the second holding company paper has a special focus on those holding companies engaged in non-banking activities. The questions OTS received regarding the first holding company paper can be summarized as follows:

- Provide more detail regarding the OTS's regulatory oversight of thrift holding companies, including enforcement actions against them;
- Quantify the significance of non-banking activities to those thrift holding companies engaged in such activities;
- Specify any differences in the safety and soundness of thrifts owned by holding companies engaged in non-banking activities versus other thrifts; and
- Provide additional data and possible explanations for the increase during the first half of 1997 in the number of applications from non-banking firms to obtain a thrift charter.

[1] Non-banking activities are those activities not authorized for bank holding companies under the Bank Holding Company Act. Examples of these commercial, industrial and other financial activities are listed in the Table on page 25 of this report. A more complete enumeration of non-banking activities currently pursued by thrift holding companies was contained in the Table on page 18 of the first holding company paper.

I. Regulatory Oversight of Thrift Holding Companies

Statutory Authority

- OTS has statutory authority to examine and supervise savings and loan holding companies and their subsidiaries under section 10(b) of the Home Owners' Loan Act (12 USC 1467a(b)). This authority is codified in the regulations at 12 CFR 584.1.

- Section 5(d) of the Home Owners' Loan Act (12 USC 1464(d)) authorizes OTS to enforce conditions of approval, written agreements entered into with OTS, directives, law, and regulation with respect to thrift holding companies.

    - OTS exercises this authority through examinations, off-site monitoring, and, when necessary, enforcement actions.

A. OTS Examinations of Thrift Holding Companies

Examination Focus, Timing, and Rating System

- The purpose of the holding company examination is to assess the degree of risk the holding company structure poses to the thrift. Key considerations in the holding company examination are: cash flow needs of the holding company; dependence of the holding company on the thrift for dividends; the quality of management; and inter-company transactions between the holding company, or its other subsidiaries, and the thrift.

- Examinations of holding companies are conducted concurrently with examinations of the thrift subsidiary on a 12-or 18-month cycle depending on the size and rating of the thrift.

- Separate examination reports and ratings are issued for the thrift and the holding company.

- OTS assigns one of the following ratings to the holding company structure based on the structure's overall effect on the thrift's operations and safety and soundness:

  "**Above Average**" – a clear and significant source of financial and managerial strength to the thrift.

  "**Satisfactory**" – a neutral effect on the thrift.

  "**Unsatisfactory**" – a detrimental or burdensome effect on the thrift's operations and safety and soundness.

Examination Statistics

- The OTS completed 483 holding company structure examinations in 1996. For the first six months of 1997, 202 holding company structure examinations have been completed.[1]

- The examination ratings for holding company structures as of June 30, 1997 were as follows:

Examination Ratings for Thrift Holding Company Structures Existing at June 30, 1997[2]

	All Holding Companies		Holding Co.'s Involved in Non-Bank Activities	
Rating	**Number**	**% of Total**	**Number**	**% of Total**
Above Average	65	13.4%	23	37.7%
Satisfactory	417	86.0%	38	62.3%
Unsatisfactory	3	0.6%	0	--
Total	**485**	**100.0%**	**61**	**100.0%**

[1] The Economic Growth and Regulatory Paperwork Reduction Act of October 1996 gave full examination and supervisory responsibility of holding companies owning both a commercial bank and a thrift to the Federal Reserve Board ("FRB"). Prior to October 1996, such holding companies were jointly regulated and examined by OTS and the FRB. This change lowered the rate of OTS holding company examinations for 1997 compared to 1996.

[2] 83 new holding company structures supervised by OTS have not yet been examined, or have examinations in progress.

B. Off-Site Monitoring of Thrift Holding Companies

- In addition to on-site examinations of thrift holding companies, OTS analysts and examiners monitor the financial condition and operations of thrift holding companies on a regular basis.

Focus of Off-Site Monitoring

- The focus of off-site monitoring is to analyze changes in the holding company's structure, management and financial condition and assess how such changes may affect the safe and sound operations of its thrift.

Sources of Data Used in Monitoring

- The primary data source used in these off-site monitoring efforts is the annual report thrift holding companies file with OTS. These reports provide information regarding changes in the corporate structure, management and activities of the holding company, as well as annual audited financial statements. Holding companies are also required to notify OTS of significant changes to their structure, management, or financial condition. [1]

- Other sources of information used to assist off-site monitoring of thrift holding companies include: SEC filings, public announcements and releases, newspapers and the Internet.

Outcome of Off-Site Monitoring

- Off-site monitoring may result in OTS contacting the holding company for explanations and more detailed information concerning certain transactions or changes in financial condition.

- Off-site monitoring may trigger a special examination of the holding company and/or result in changing the timing of the regular full scope examination.

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[1] Thrift holding companies can engage in a wide range of activities. The aggregate financial data filed by thrift holding companies in these annual reports is neither sufficiently detailed nor standardized to permit comparisons across types of activities. Thrift holding companies are monitored on a case-by-case basis. When peer information is needed to analyze a thrift holding company, OTS reviews data from other firms in similar lines of business that are <u>not</u> thrift holding companies. Hence, differing types of activities and data do not impede monitoring activities.

C. OTS Enforcement Actions Against Holding Companies

- Supervisory problems identified in examinations and off-site monitoring are typically corrected in a timely manner by thrifts and thrift holding companies.

- OTS takes formal enforcement measures for those problems not corrected to the satisfaction of OTS regulatory personnel. In addition, OTS will take formal enforcement actions when warranted by violations of statutes, regulations, or orders.

Types of Enforcement Actions

- The primary types of formal enforcement actions are:

  Supervisory Agreements; Cease and Desist Orders; Removal and/or Prohibition Orders; Civil Money Penalties; Capital Directives; and Injunctive Actions

Enforcement Statistics

- From January 1, 1993 through June 30, 1997, OTS initiated a total of 898 enforcement actions against thrifts and thrift holding companies supervised by OTS at the end of the second quarter of 1997.[1]

  - Of the 898 actions, 15 (1.7 percent), were initiated against thrift holding companies.

  - Another 25 actions cited a thrift or individual as the primary cause for the action, but also involved a holding company.

  - Of the 40 initiated enforcement actions involving holding companies, only 3 were against holding companies engaged in non-banking activities.

- The table on the following page summarizes the enforcement actions taken during this period, including the number of actions involving thrift holding companies.

[1] Includes enforcement actions taken against individuals associated with OTS-regulated thrifts and thrift holding companies.

Enforcement Actions Initiated from January 1993 through June 1997 Against OTS-Regulated Thrifts and Thrift Holding Companies Supervised by OTS June 30, 1997*

	Actions Initiated		Actions Involving HCs	
	Number	% of Total	Number	% of Total
Initiated Against:				
Thrifts	500	55.7%	24	2.7%
Thrift HCs	15	1.7%	15	1.7%
Others**	383	42.6%	1	0.1%
Total	**898**	**100.0%**	**40**	**4.5%**

*Excludes 530 actions against thrifts and holding companies no longer supervised by OTS. Of those actions, 19 (3.6 percent) were against thrift holding companies. Further breakout of those actions by holding companies engaged in non-banking activities is unavailable from the current OTS database.
**Primarily individuals associated with thrifts and thrift holding companies. Also includes subsidiaries of thrifts.

- Most actions taken against holding companies were due to: Conflicts of interest; failure to maintain thrift net worth; misrepresented applications; and failure of an existing thrift holding company to properly notify OTS of a change in the ownership structure of the thrift, such as creating an intermediate holding company.

- Thrift holding companies have not been a significant source of OTS enforcement actions over the past four-and-one-half years. Although holding companies own 50 percent of today's thrifts (see table on page 8), they are a contributing factor in only 4.5 percent of enforcement actions.

  - Thrift holding companies engaged in non-banking activities have been even less likely to be subject to an OTS enforcement action. While thrift holding companies with non-banking activities owned 5 percent of thrifts under OTS regulation at June 30, 1997, they accounted for only 0.3 percent of enforcement actions from January 1993 through the end of the second quarter of 1997.

  - Thrift holding companies have not been a direct cause of a thrift failure over the past four-and-one-half years either. There have only been 14 thrift failures since the end of 1992.

    - Five of the fourteen failed thrifts were owned by a holding company; three of those holding companies engaged in non-banking activities.

    - However, in none of these cases did the holding company contribute to the failure of the thrift.

II. Changes in the Number of Thrifts Owned by Holding Companies

Changes in Holding Company Ownership of Thrifts During the First Six Months of 1997

- As discussed in the first holding company paper, the number of holding companies changes frequently. Such changes are due to many factors, including individual business decisions by thrifts, mergers, and acquisitions. The table below shows the changes in the number of thrift holding companies, the number and assets of thrifts under a holding company structure between December 31, 1996 and June 30, 1997.

Changes in Thrift Holding Companies
(Dollars in Billions)

	As of December 1996			As of June 1997			Change From December 1996		
Holding Company Type	Number of HCs	Number of Thrifts Owned	Thrift Assets	Number of HCs	Number of Thrifts Owned	Thrift Assets	Number of HCs	Number of Thrifts Owned	Thrift Assets
OTS Regulated HCs									
Unitary	704	515	$467	714	519	$468	+10	+4	+$1
Multiple	40	39	$94	37	39	$90	-3	0	-$4
Sub-Total	744	554	$561	751	558	$558	+7	+4	-$3
Bank HCs Owning a Thrift	131	97	$71	119	94	$86	-12	-3	+$15
Total HCs & Thrifts in HCs	875	651	$632	870	652	$644	-5	1	+$12
Independent Thrifts		685	$137		620	$125		-65	-$12
Total Thrifts		**1,336**	**$769**		**1,272**	**$769**		**-64**	**$0**

- Over the first six months of 1997, the number of thrift holding companies declined by 5 (a 0.6 percent decrease) to 870 as of June 30, 1997. The decrease was principally due to a decline in bank holding companies owning OTS-regulated thrifts which dropped by 12 during this six month period to 119.
    - The slight decline in the total number of thrift holding companies masks higher exits and entries of holding companies. During the first six months of 1997, 66 new thrift holding companies were created[1] and 71 exited the industry.
- Despite the decrease in the total number of holding companies, the number of thrifts owned by holding companies increased to 652 at the end of the second quarter of 1997 from 651 six months earlier. This slight increase resulted primarily from a rise in the number of unitary thrift holding companies that own thrifts.
- The percent of all thrifts owned by holding companies increased slightly to 51.3 percent at June 1997 from 48.7 percent six months earlier. This increase reflects the continued trend in thrifts converting from mutual to stock form of ownership and, simultaneously, forming a thrift holding company. For thrifts under OTS regulation, approximately 95 percent of thrifts converting during the past three years also elected to form a holding company.[2]

[1] 49 of the 66 new holding companies were essentially shell corporations whose only business was holding the stock of the thrift.

[2] Thrifts typically form holding companies to provide greater flexibility in terms of operations, expansion, and diversification.

III. Thrifts Owned by Holding Companies Engaged in Non-Banking Activities

Number and Profile

- There were 64 thrifts owned by holding companies engaged in non-banking activities ("the NBA group") as of June 30, 1997, down from 73 thrifts six months ago.
    - This reduction resulted from both the sale of thrifts by holding companies engaged in non-banking activities and holding companies selling, or otherwise ceasing, their non-banking activities.
- The 64 thrifts in the NBA group held a disproportionately large amount of thrift industry assets -- 27.8 percent -- because of several very large thrifts in this group. The table below presents the distribution of thrifts owned by holding companies with non-banking activities by thrift asset size.

Thrifts in the NBA Group
As of June 30, 1997

Thrift Asset Size Groups	# Thrifts All	# Thrifts NBA Group	% of Total All	% of Total NBA Group
Small (<=$100M)	591	15	46.6	23.4
Medium (>$100M, <=$1B)	566	26	44.7	40.6
Large (>$1B, <=$10B)	94	18	7.4	28.1
Xlarge (>$10B)	16	5	1.3	7.8
Total*	**1,267**	**64**	**100.0**	**100.0**

* There were 1,272 OTS-regulated thrifts as of June 30, 1997. Five thrifts owned by other thrifts were excluded from this analysis to avoid double counting.

Asset Size

- The 64 thrifts in the NBA group range in asset size from $8 million to $47 billion.
  - Most of the thrifts in the NBA group are large -- 23 thrifts (36 percent of the group) have assets in excess of $1 billion. In contrast, the vast majority of the thrift industry is smaller -- 91 percent of all thrifts had assets less than $1 billion as of June 30, 1997.
  - Even though small thrifts are under-represented in the NBA group, they still account for almost a quarter of that group.

Financial Differences Between Thrifts in the NBA Group and Other Thrifts[1]

- Economic conditions during the first six months of 1997 have been very favorable to the thrift industry, including thrifts in the NBA group. Their economic performance and financial condition during this period are generally comparable to the overall industry.
- Thrifts in the NBA group employed various business strategies. Several were "specialists," i.e. focused on one or just several lending and/or deposit products.
  - A few notable differences in the asset structure between the NBA group, and the thrift industry, as a whole, are attributable to several large thrifts in the NBA group that specialize in activities such as loan servicing or credit card loans.
- Because the number of thrifts in the NBA group is small, group averages can be easily skewed by "outliers," especially if the outlier is a large thrift.
  - Consequently, the following review of selected financial indicators for the 64 thrifts in the NBA group occasionally presents data excluding outliers when comparisons to industry average are skewed by these outliers.

[1] Thrifts in the NBA group are compared to averages for all thrifts (mutual and stock held thrifts) in this paper. Thrifts owned by holding companies are, by definition, stock institutions. Excluding mutual thrifts from the industry averages would generally have produced comparative data more favorable to the NBA group. See Appendix 1 for a comparison of selected financial indicators for mutual and stock held thrifts.

Asset Composition

- In general, the NBA group holds more of their assets in mortgage loans and related securities – 73.7 percent – than the thrift industry average – 70.6 percent. The types of loans held by this group are compared to the industry averages in the table on the following page.
    - As shown in the table, the NBA group held a lower percentage of assets in single-family mortgages (47.5 percent) than the industry average (50.1 percent). This difference is primarily due to two large credit card specialist thrifts in the NBA group.
        - There are five credit card specialist thrifts in the industry. Absent these thrifts, the industry's average single-family mortgage-to-asset ratio would increase to 50.7 percent. This is only slightly higher than the NBA group average of 50.2 percent excluding the two credit card specialist thrifts in the NBA group.
    - The NBA group held a higher than average proportion of their assets in mortgage-backed securities and multi-family mortgages. Mortgage-backed securities and multi-family mortgages represented 17.3 percent and 8.9 percent, respectively, of the NBA group's assets versus the industry averages of 14.3 percent and 6.2 percent, respectively. The NBA group holds a smaller than average proportion of their assets in commercial loans and, with the exception of the two credit card specialists, holds a lower portion of consumer loans.
        - Consumer loans comprised 5.9 percent of the NBA group's assets versus 5.2 percent for the industry. However, when the credit card specialists are excluded, these ratios drop to 1.9 percent and 4.2 percent, respectively.
        - The NBA group held 0.8 percent of their assets in commercial business loans, slightly less than the industry average of 1.3 percent. This difference is primarily due to the limited amount of commercial lending by the very large thrifts in the NBA group. Small and medium sized thrifts in the NBA group hold higher proportions of commercial loans than the industry averages for comparably sized thrifts.

Asset Composition Comparison

As of June 30, 1997

All OTS Thrifts

Asset Size Group	Mtg-Bk Securities	1-4 Fam. Mtg. Lns.	5 + Fam Mtg. Lns.	Nonres. Mtg. Lns.	Other Mtg. Lns.	Consumer Loans	Commercial Loans
	Percent of Total Assets						
Small	8.4	51.6	2.3	5.2	3.2	5.2	1.7
Medium	10.8	48.2	4.2	5.7	3.6	5.6	1.5
Large	16.0	44.4	5.5	4.5	1.9	8.4	1.5
Xlarge	15.3	55.2	8.1	2.8	0.9	2.7	1.1
Total	**14.3**	**50.1***	**6.2**	**4.1**	**1.9**	**5.2***	**1.3**

Thrifts in the NBA Group

Asset Size Group	Mtg-Bk Securities	1-4 Fam. Mtg. Lns.	5 + Fam Mtg. Lns.	Nonres. Mtg. Lns.	Other Mtg. Lns.	Consumer Loans	Commercial Loans
	Percent of Total Assets						
Small	5.2	39.5	2.1	5.6	6.1	4.5	3.6
Medium	6.8	40.7	5.3	10.7	8.0	3.4	2.6
Large	12.7	34.1	5.6	4.3	1.7	22.6	1.5
Xlarge	19.4	52.2	10.2	3.4	1.0	0.8	0.4
Total	**17.3**	**47.5****	**8.9**	**3.9**	**1.5**	**5.9****	**0.8**

*Excluding credit card specialists, the industry averages for single-family loans and consumer loans would rise to 50.7 percent and fall to 4.2 percent, respectively.
**Excluding two credit card specialists, the NBA group averages for single-family loans and consumer loans would rise to 50.2 percent and fall to 1.9 percent, respectively.

Liability Composition

- Thrifts in the NBA group tend to rely less on deposits as a funding source than the industry average. The deposit-to-asset ratio for the NBA group was 63.1 percent versus 66.7 percent for the industry, although this result is not consistent for all asset size groups.

    - However, the NBA group had a slightly higher proportion of non-interest bearing deposits (4.0 percent of assets) and deposit accounts greater than $100,000 (9.9 percent) than did the industry, whose averages were 3.2 percent and 9.7 percent, respectively.

Comparison of Funding Sources

As of June 30, 1997

All OTS Thrifts		
Asset Size Group	Total Deposits	Total Borrowings
	Percent of Total Assets	
Small	81.2	5.8
Medium	76.3	11.9
Large	66.8	23.3
Xlarge	60.4	29.8
Total	**66.7**	**22.9**

Thrifts in the NBA Group		
Asset Size Group	Total Deposits	Total Borrowings
	Percent of Total Assets	
Small	80.8	6.3
Medium	77.2	11.9
Large	63.1	25.6
Xlarge	62.3	28.1
Total	**63.1**	**26.8**

- Borrowings were used as a funding source more extensively by the NBA group (26.8 percent of assets) than by the industry as a whole (22.9 percent).

Capital Levels

- Industrywide, larger thrifts tend to hold lower levels of capital than smaller thrifts. (Larger banks also hold lower levels of capital than smaller banks.) This tendency holds true for the NBA group.

- The NBA group's average capital level of 7.0 percent was lower than the industry average capital level of 8.1 percent. This was attributable to the overrepresentation of large thrifts in the NBA group.

  - Both capital levels would meet the highest regulatory standard of "well-capitalized."

Comparison of Equity Capital Levels*

As of June 30, 1997

All OTS Thrifts	
Asset Size Group	Equity Capital
	% TA
Small	11.7
Medium	9.8
Large	8.0
Xlarge	7.1
Total	**8.1**

Thrifts in the NBA Group	
Asset Size Group	Equity Capital
	% TA
Small	11.1
Medium	8.0
Large	8.6
Xlarge	6.4
Total	**7.0**

*An equity capital ratio of 5 percent or greater meets well-capitalized standards.

Earnings

- The NBA group's annualized return on average assets ("ROA") for the first six months of 1997 was 101 basis points, compared to the industry 's ROA of 89 basis points. Higher fee income for the NBA group accounted for much of this difference.

Comparison of Primary Sources of Profitability
For the Six Months Ended June 30, 1997

All OTS Thrifts			
Asset Size Group	Net Income	Net Int. Margin	Fee Income
	Percent of Average Assets		
Small	1.00	3.34	0.48
Medium	0.93	3.23	0.44
Large	1.01	3.00	0.67
Xlarge	0.78	2.58	0.50
Total	**0.89**	**2.88**	**0.54**

Thrifts in the NBA Group			
Asset Size Group	Net Income	Net Int. Margin	Fee Income
	Percent of Average Assets		
Small*	0.45	3.99	1.97
Medium	0.83	3.35	0.53
Large**	1.39	3.62	1.60
Xlarge	0.90	2.59	0.55
Total	**1.01**	**2.87**	**0.80**

*Two small de novo thrifts in the small NBA group were chartered in 1997 and experienced significant startup costs. Absent these two thrifts, ROA would increase to 102 basis points for the 15-member small group.
**Absent the two credit card specialists and one large thrift specializing in "working out" delinquent loans, the ROA for the 18-member large group would be 120 basis points.

- Even when the NBA and industry group averages are adjusted for outliers, all NBA group thrifts, except the medium sized thrifts, were more profitable than their peers.

Operating Efficiency

- Operating efficiency is the ratio of overhead expense to net interest income and fee income. A lower ratio indicates more efficient operations. Operating efficiency measures the percentage of gross "core" earnings consumed by overhead expense.

- The NBA group's operating efficiency ratio of 59.14 percent for the first half of 1997 was equivalent to the industry average of 59.07 percent.

Comparison of Operating Efficiency

For the Six Months Ended June 30, 1997

All OTS Thrifts		
Asset Size Group	G&A Expense % AA	Operating Efficiency Ratio
Small	2.93	76.80
Medium	2.32	63.31
Large	2.21	60.44
Xlarge	1.64	53.17
Total	**2.02**	**59.07**

Thrifts in the NBA Group		
Asset Size Group	G&A Expense % AA	Operating Efficiency Ratio
Small*	5.91	99.14
Medium	2.58	66.45
Large	3.74	71.62
Xlarge	1.61	51.13
Total	**2.16**	**59.14**

*Absent the two de novo thrifts in this group, the G&A expense ratio would drop to 5.24 percent and the operating efficiency ratio would improve to 87.94 percent.

- The large thrift group includes 12 loan servicing specialist thrifts with very large loan servicing portfolios. Seven of these thrifts are in the NBA group. Loan servicing is labor intensive and tends to increase overhead costs. Absent the loan servicing specialists, the operating efficiency ratio drops to 56.2 for all large thrifts and to 64.3 for large thrifts in the NBA group.

Asset Quality

- The NBA group's ratio of troubled assets[1] to total assets as of June 30, 1997 was 1.61 percent, 52 percent higher than the industry aggregate ratio of 1.06 percent. This large difference in the troubled assets ratio stems primarily from a single large "work out" specialist thrift in the NBA group. A work out specialist thrift purchases already delinquent loans that are, by definition, "troubled."
    - Excluding the one large work out specialist thrift, the troubled assets ratio for the NBA group drops to 1.18 percent, a level more comparable to the industry average, albeit still 10 percent higher than the industry average.

Comparison of Asset Quality

As of June 30, 1997

All OTS Thrifts		
	Credit Risk	
Asset Size Group	30-89 PD Loans	Troubled Assets
	Percent of Total Assets	
Small	1.36	0.95
Medium	0.86	1.00
Large	0.75	1.30
Xlarge	0.70	0.92
Total	**0.78**	**1.06**

Thrifts in the NBA Group		
	Credit Risk	
Asset Size Group	30-89 PD Loans	Troubled Assets
	Percent of Total Assets	
Small	1.74	1.55
Medium	0.85	0.99
Large*	1.16	3.40
Xlarge	0.73	1.08
Total	**0.84**	**1.61**

*Excluding the work out specialist thrift, the troubled assets ratio for the large group declines to 1.53 percent.

[1] Troubled assets include loans 90 days or more delinquent, loans in non-accrual status, and repossessed assets.

- For all but the small thrift groups[1], asset quality for the NBA group did not differ significantly from industry averages (excluding the large work out specialist outlier).

[1] One thrift in the small NBA group had a very high troubled assets-to-total assets ratio (11.10 percent). (This thrift is profitable and, after an infusion of capital from its holding company in September 1996, is currently well-capitalized.) Excluding this thrift, the small NBA group's ratio of troubled assets to total assets declines to 0.65 percent from 1.55 percent and the ratio of loans 30-89 days delinquent declines to 1.48 percent from 1.74 percent. (The exclusion of this one thrift did not change the asset quality ratios of the entire small thrift group.)

IV. Significance of Non-Banking Activities to Thrift Holding Companies

Survey of Examiners and Analysts

- Since OTS does not regularly obtain detailed information regarding the significance of non-banking activities to thrift holding companies, the agency conducted a special survey of OTS examiners and analysts in August 1997 to get this information. Comparable financial data were not obtainable for all holding companies with non-banking activities. The following table presents the number of thrifts owned by holding companies[1] engaged in non-banking activities that were included in this survey.

Survey of Holding Companies with Non-Banking Activities

Thrift Asset Size Group	All		Thrift Asset Size Group	Survey Results		Survey Results % of Total	
	Numbers	Thrift Assets $ Millions		Numbers	Thrift Assets $ Millions	Numbers %	Assets %
Small	15	$786	Small	8	$361	53.3%	47.0%
Medium	26	8,560	Medium	18	6,683	69.2%	78.1%
Large	18	49,385	Large	11	29,224	61.1%	59.2%
Xlarge	5	154,671	Xlarge	5	154,671	100.0%	100.0%
Total	**64**	**$213,402**	**Total ***	**42**	**$190,939**	**65.6%**	**89.5%**

*One holding company structure in the survey owned two thrifts.

[1] Financial holding company data used in the survey were consolidated. Consequently, the number of holding companies reported in this section refers to holding company structures. The holding company structures may own a number of other subsidiaries. The range of complex holding company structures was discussed more fully in the first holding company paper.

- Detailed non-banking activity data were obtainable for the holding company structures of 42 of the 64 thrifts in the NBA group. (One holding company structure in the survey owned two thrifts.) However, the survey results appear to be fairly representative. Every size group has at least 50 percent of the group represented in the survey.

- OTS examiners and analysts reviewed the individual holding company consolidated financial reports to determine the significance of non-banking activities to the holding companies engaged in such activities. The examiners and analysts also relied on information from the OTS holding company examinations. In addition, the holding companies were contacted directly to update any data.

    - Since the information needed to fully address this issue was gathered from both public and confidential sources, the information will not be released for individual holding companies.

    - Data for certain holding companies, primarily holding companies that are family trusts, were not available in sufficient detail for this analysis.

    - The data collected from the August 1997 survey reflected the latest data available, generally 1996 year-end data.

- Revenues were used to analyze the significance of non-banking activities to thrift holding company structures. Revenues appear to provide more meaningful results than assets or net income for such analyses. Net income can be skewed by differing depreciation and tax rates between industries. Moreover, net income can be significantly affected by the timing of one-time losses or gains. Assets vary substantially by industry, e.g. manufacturing firms are asset intensive while service oriented firms have relatively few assets for the revenues generated.

    - In contrast, revenues are more directly comparable between differing industries and less influenced by one-time events.

        - However, the revenues, like net income and assets, of holding companies' subsidiaries may not consistently sum to consolidated holding company data due to the elimination of inter-company transactions.

Range of Significance of Non-Banking Activities by Percentage of Revenue

- The significance of non-banking activities to holding companies engaged in such activities was wide-ranging. Measured as a percent of the holding companies' total revenue, non-banking activities contributed, on average, 71 percent of these holding companies' total revenue. The following table presents the range of percentages of non-banking revenues to their holding companies' total revenue.

Survey of Holding Companies with Non-Banking Activities
By Percent of Revenue from NBA Activities

Survey Results				
			Revenues from NBA	
Dependence on NBA Activities	Numbers	Total Revenues $ Millions	$ Millions	% Total Revenues
Minimal (Less Than 10%)	17	$18,758	$369	2.0%
Moderate (10% - 50%)	1	11	5	45.5%
Significant (51% - 80%)	4	12,778	8,942	70.0%
Predominant (Over 80%)	19	55,832	52,764	94.5%
Total	**41**	**$87,379**	**$62,080**	**71.0%**

- For 17 holding company structures – 41 percent of those included in the survey – non-banking activities contributed less than 10 percent of their total revenue.

- For 23 holding company structures – 56 percent of the survey group – non-banking activities accounted for more than half of their total revenues.

  - Among this latter group, non-banking activity was the predominant source (80 percent or more) of total revenue for 19 holding company structures (46 percent of the total survey group).

Significance of Non-Banking Activities by Size of Thrift

- For the holding companies in the survey, those owning larger thrifts generated a lower percentage of their revenue from non-banking activities than those owning smaller thrifts.

- Larger thrifts tended to be the primary asset of their holding companies. Hence, revenues from these thrifts typically accounted for the majority of their holding companies' total revenues. However, even for the five extra-large thrifts, non-banking activity revenues accounted for an average 19 percent of their holding company structures' total revenue.

- Non-banking revenue to thrift holding companies is presented in the following table by thrift asset size group.

Survey of Holding Companies
By Thrift Asset Size

Survey Results			
Thrift Asset Size Group	Numbers	Thrift Assets $ Millions	NBA Revenues % Total Revenues
Small	8	$361	88.1%
Medium	18	6,683	97.0%
Large	11	29,224	40.0%
Xlarge	5	154,671	19.0%
Total *	**42**	**$190,939**	**71.0%**

*One holding company structure in the survey owned two thrifts.

- The group averages mask substantial variance in the relative importance of the non-banking activities for individual entities. For all groups except small thrifts, there are at least two holding companies for whom non-banking activities contribute a minimal amount (less than 10%) of total holding company revenues. All groups, however, have at least two holding companies that are very dependent (over 75% of revenue) on non-banking activity revenues.

Significance of Non-Banking Activities by Size of Holding Company

- The significance of non-banking revenue to thrift holding companies is presented in the table below by holding company asset size. As shown in the table, non-banking revenue was least significant for the largest holding company group (holding company assets over $10 billion). Holding companies of other size groups had similar percentages of revenues from non-banking activities.

- The nine largest holding companies fall into two groups – those owning larger thrifts (six) and those holding smaller thrifts (three). The six with larger thrifts tended to generate a lower proportion of revenues from non-banking activities. In contrast, the three owning smaller thrifts generated a significant portion of their revenue from non-banking activities. The ratios of non-banking revenue-to-total holding company structure revenue for these two divergent groups, when combined, resulted in a lower than average ratio.

- Again, group averages mask wide variations in the relative importance of non-banking activity revenue to total holding company revenue. Within each holding company group there are at least four holding companies that are minimally dependent (less than 10%) upon non-banking activity revenues. However, there also are at least three holding companies in each group whose revenues are predominantly (larger than 80%) from non-banking activities.

Survey of Holding Companies with Non-Banking Activities
By Top Tier Holding Company Asset Size

Survey Results					
HC Asset Size Group	Numbers	Total HC Assets $ Millions	Total HC Revenues $ Millions	Revenues from NBA $ Millions	% Total Revenues
<= $500M	11	$1,824	$559	$489	87.5%
> $500M, <= $1B	8	6,118	3,870	3,493	90.3%
> $1B, <= $10B	13	34,583	10,348	9,110	88.0%
> $10B	9	527,025	72,603	48,989	67.5%
Total	**41**	**$569,550**	**$87,380**	**$62,081**	**71.0%**

Significance of Non-Banking Activities by Type of Activity

- The table on the following page presents the significance of non-banking activities by type of activity. Revenues generated from non-banking activities are shown as a percent of total consolidated holding company structure revenue.[1]

- Although non-banking activity revenue, on average, accounted for 71 percent of total consolidated holding company revenue, the revenue contribution from individual non-banking activities ranged widely from about three percent to 85 percent.

- The most prominent types of non-bank activities conducted by thrift holding companies were: real estate development; insurance; investments; broker dealer; hotel management and development; and wood products. Among the most prominent group, investment activities generated the highest percentage of revenues (85 percent) for their holding companies.

- Investment activities and insurance and related services generated the largest dollar amounts of revenue for the holding companies in the survey – $30 billion and $18 billion, respectively.

- The relative importance of non-banking activity revenue to total revenue also varies substantially among individual holding companies providing the same type of activity. For example, among holding companies providing insurance and related services, the contribution of non-banking activity revenue to total revenue varied between less than 1% percent and 120% percent. (The percentage exceeded 100 percent due primarily to the elimination of inter-company transactions upon consolidation.)

[1] As discussed in the first holding company paper, a holding company structure can contain numerous subsidiary holding companies engaged in various activities. In many cases, a subsidiary holding company is established to hold companies engaged in a specific activity. For this reason, the number of holding companies engaged in individual activities exceeds the number of holding company structures.

SIGNIFICANCE OF NON-BANKING ACTIVITIES TO THRIFT HOLDING COMPANIES

Non-Banking Activity*	HCs Engaged in Activity (#)	HCs in Survey (#)	Total NBA Revenue ($ Millions)	NBA Revenue / HC Revenue** (%)
Real Estate & Related Services	47	23	$2,262	14%
Insurance & Related Services	25	12	$17,669	48%
Investments	9	5	$29,786	85%
Fund Mgmt. & Other Invest. Serv.	9	4	$193	11%
Broker / Dealer	7	4	$1,670	30%
Management Services	5	3	$22	3%
Hotel Owner, Operator, Developer	6	3	$14	3%
Wood Products	5	4	$2,756	72%
All Other Activities***	24	15	$7,709	74%

*A holding company can be engaged in more than one activity.
**NBA revenues divided by consolidated holding company revenues for holding companies engaged in that activity.
***Includes a wide range of activities discussed in the first holding company paper.

V. Recent Increase in Thrift Chartering Activity

Chartering Activity: From 1993 through 1996

- There were 66 new thrifts chartered by OTS in the four-year period from 1993 through 1996 – an average of 17 per year. Most of these new entrants (35) were state-chartered thrifts, commercial banks, and credit unions converting to an OTS-regulated thrift. The remaining new OTS-regulated thrifts (31) entered the industry as start-up institutions or de novos.
    - Among the 66 new entrants were 7 thrifts (11 percent) owned by holding companies engaged in non-banking activities.

Chartering Activity For the First Eleven Months of 1997 and Applications "In the Pipeline"

- There has been an increase in chartering activity and applications received to establish thrifts during the first eleven months of 1997. The rise in applications received from commercial firms to establish thrifts has been especially sharp.
    - For the first eleven months of 1997, 20 new OTS-regulated thrifts were established.
    - As of November 30, 1997, there were 28 applications for thrift charters pending review and decision by OTS.
        - Of the 20 new entrants through November 30, 1997, 3 (15 percent) are owned by holding companies engaged in non-banking activities.
        - Of the 28 applications for a thrift charter, 9 (32 percent) are from holding companies engaged in non-banking activities.
            - The number of thrifts established through November 30, 1997, and applications for thrift charters, by firms engaged in non-bank activities exceeds the combined number that entered the industry in the four-year period, 1993 - 1996.

Possible Explanations for the Recent Increase in Chartering Activity and Applications

- This increased interest in establishing a thrift may reflect several recent legislative changes enacted during 1996 that leveled the competitive playing field for thrifts. These legislative changes included:

    - **The Economic Growth and Regulatory Paperwork Reduction Act of 1996** ("EGRPRA") -- EGRPRA reforms expanded the amounts of consumer loans, especially education loans and credit card loans, as well as loans to small businesses and farms, that thrifts can make.

    - **The Deposit Insurance Funds Act of 1996** (part of EGRPRA) -- assessed thrifts a one-time special assessment to fully capitalize the Savings Association Insurance Fund ("SAIF"). Since the SAIF is now fully capitalized, federal deposit insurance premiums for thrifts are minimal and do not exceed premiums charged banks with comparable examination ratings and capital levels.

    - **The Small Business Job Protection Act of 1996** -- relieved thrifts of having to meet restrictive qualifications as "domestic building and loan associations" for tax purposes. This legislation augmented thrifts' lending flexibility. This act also reduced the costs of acquiring a thrift and changing charters from a thrift to a commercial bank.

- The recent increase in thrift charter applications, especially among holding companies with non-banking activities, may also reflect some concern over the future availability of a federal thrift charter and the unitary holding company structure. Both are fundamental issues included in the congressional debate on HR10, the financial modernization proposal introduced in the 105th Congress.

Common Business Plan Elements from Recent Commercial Firms' Applications to Start or Acquire a Thrift

- The business plans filed by the commercial firms recently applying to establish a thrift were reviewed to help determine further possible reasons for the recent increased interest in thrift chartering activity.

    - Most of these applicants plan on starting de novo thrifts rather than purchasing an existing thrift.

- In general, all of the recent applicants project utilizing some already existing business strength or competitive advantage to assist their thrift operations.
- In addition, these firms all have experience in regulated environments and most have senior managers with experience in the thrift/banking industries.
- Other major common elements of the applicants' business plans are as follows:

Product Expansion – Most of the applicants would use the thrift to make available a wider range of products to consumers. Most applicants anticipate offering various deposit and loan products to customers in an effort to more fully respond to increasing demand for financial services.

Initial Focus on Current Customers – All of the applicants would market thrift products to their current customers.

Utilize Established Product Distribution Channels -- The applicants plan on using their existing channels of distribution for making thrift products available to consumers. Some of the applicants indicated that having established channels in place will reduce start up costs and will shorten the time to break even operations for the thrift.

Technology is Key -- The majority of the applicants would have no additional or separate thrift branches. Instead, they will use ATMs, debit cards, phone banking, home PC banking, and existing office networks.

Outsourcing of Back Room Operations -- Almost all of the applicants project outsourcing the back room activities associated with the processing and servicing of loans and deposits. This will reduce the capital investment in equipment and minimize overhead costs.

Major Difference Among the Plans -- Specialization versus Full-Line Services

- There was one major difference among the applications reviewed. Most of the applicants planned on offering a full-line of thrift products and services, while some would offer one, or few, products.
- Expertise in certain products and the "fit" of thrift products with existing products offered appeared to be the primary factors in determining the breadth of the product lines to be offered.

MUTUAL AND STOCK THRIFTS
Selected Financial Indicators
As of and For the Six Months Ended June 30, 1997

	Mutual	Stock	All
Total Number	509	758	1,267
% by Asset Size Group			
Small	61.7%	36.5%	46.6%
Medium	36.9%	49.9%	44.7%
Large	1.4%	11.5%	7.4%
XLarge	0.0%	2.1%	1.3%
Total Assets ($ Millions)	$72,837	$696,152	$768,989
% by Asset Size Group			
Small	20.7%	2.3%	4.0%
Medium	61.6%	17.4%	21.6%
Large	17.7%	33.5%	32.0%
XLarge	NA	46.8%	42.4%
1-4 Mortgage Loans/Assets			
Small	56.4%	47.0%	51.6%
Medium	52.9%	46.5%	48.2%
Large	51.1%	44.0%	44.4%
XLarge	NA	55.2%	55.2%
All	53.3%	49.8%	50.1%
Equity Capital/Assets			
Small	11.4%	12.0%	11.7%
Medium	10.9%	9.4%	9.8%
Large	10.2%	7.8%	8.0%
XLarge	NA	7.1%	7.1%
All	10.9%	7.8%	8.1%
Profitability - ROA			
Small	0.84%	1.16%	1.00%
Medium	0.98%	0.90%	0.93%
Large	0.95%	1.02%	1.01%
XLarge	NA	0.78%	0.78%
All	0.94%	0.89%	0.89%
Operating Efficiency Ratio			
Small	64.30%	86.66%	76.80%
Medium	57.35%	65.31%	63.31%
Large	56.66%	60.63%	60.44%
XLarge	NA	53.17%	53.17%
All	58.68%	59.12%	59.07%
Troubled Assets/Assets			
Small	0.78%	1.10%	0.95%
Medium	0.65%	1.14%	1.00%
Large	0.33%	1.35%	1.30%
XLarge	NA	0.92%	0.92%
All	0.62%	1.11%	1.06%

Small = assets under $100 million
Medium = assets between $100 million and $1 billion
Large = assets between $1 billion and $10 billion
XLarge = assets greater than $10 billion

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