Department of the Treasury

Regulatory Bulletin

RB 32-9 was rescinded 6/19/02 by RB 32-24. Click HERE to link to RB 32-24

RB 32-9

Handbook: **Thrift Activities**
Subject: **Qualified Thrift Lender Test** **Section: 270**

RESCINDED

Thrift Activities Regulatory Handbook Update

Summary: This bulletin provides an update to Thrift Activities Regulatory Handbook Section 270, Qualified Thrift Lender Test. Please replace the existing handbook section with the enclosed revised section. A summary of changes is provided below.

For Further Information Contact: Your Office of Thrift Supervision (OTS) Regional Office or the Supervision Policy Division of the OTS, Washington, DC. You may access this bulletin at our web site: www.ots.treas.gov. If you wish to purchase a handbook and a subscription to the updates, please contact the OTS Order Department at (301) 645-6264.

Regulatory Bulletin 32-9

SUMMARY OF CHANGES

Changes to Section 270 are summarized below. Change bars in the margins of the handbook section indicate revisions.

270 Qualified Thrift Lender Test

Introduction: Explains that savings associations may switch from one QTL test (HOLA or IRS) to the other.

Exceptions: Explains two exceptions to the QTL test requirements.

Definitions of QTL Terms: Adds definitions for "community service facilities," "manufactured housing," and "residential housing," based on definitions included in OTS's former QTL regulations, §§ 563.50, 563.51 and 563.52, removed in November 1996. Adds the definition of "small business loans" to be in accord with OTS's § 560.3 regulatory definition of the term, adopted in April 1997. Also revises the definitions of “credit-needy area” and “starter home loans” to comport with the new CRA regulations.

References: Updates references.

Appendix C: Clarifies various instructions for preparing the QTL worksheet.

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Introduction

To be a Qualified Thrift Lender (QTL), an institution must either meet the Home Owners' Loan Act (HOLA) QTL test or the Internal Revenue Service (IRS) tax code Domestic Building and Loan Association (DBLA) test.

Savings associations may use either test to qualify and may switch from one test to the other. OTS has placed no limitations on the election except to require that the association must meet the time requirements of the respective test, that is, nine out of the last twelve months or the taxable year. According to the IRS, a taxable year may be either a calendar or fiscal year.

Qualified Thrift Lender Test

Under the QTL test, an institution must hold Qualified Thrift Investments (QTI) equal to at least 65 percent of its portfolio assets. The ratio of an institution's QTI divided by its portfolio assets is the institution's actual thrift investment percentage (ATIP). QTI must fall into one of the two following categories:

- Assets that are includable in QTI without limit.
- Assets limited to 20 percent of portfolio assets.

Portfolio assets are total assets minus goodwill and other intangible assets, office property, and liquid assets not exceeding 20 percent of total assets. An institution ceases to be a QTL when its ratio of QTI (numerator) divided by its portfolio assets (denominator) falls, at month end, below 65 percent for four months within any 12 month period.

<u>Assets that are includable as QTI without limit:</u>

- Loans (including qualifying real estate owned as a result of such loans) to purchase, refinance, construct, improve, or repair domestic residential or manufactured housing.
- Home equity loans.
- Educational loans.
- Small business loans.
- Loans made through credit cards or credit card accounts.
- Securities backed by or representing an interest in mortgages on domestic residential or manufactured housing.
- FHLB stock.
- Obligations of the FDIC, FSLIC, RTC, and the FSLIC Resolution Fund (depending on the date of the issue of such obligations).

<u>Assets that are includable as QTI up to 20 percent of portfolio assets:</u>

- Fifty percent of the amount of domestic residential housing mortgage loans originated and sold within 90 days. An institution may, on a consistent basis, include as QTI either the sales amounts from a previous quarter or the previous rolling 90 days or three-month period.
- Investments in a service corporation that derives at least 80 percent of its gross revenues from activities related to domestic or manufactured residential housing.
- Two hundred percent of the amount of loans and investments in "starter homes."
- Two hundred percent of the amount of certain loans in "credit-needy areas."
- Loans for the purchase, construction, development, or improvements of "community service facilities" not in credit-needy areas.
- Loans for personal, family, or household purposes (other than those reported in the assets includable without limit category).
- FNMA and FHLMC stock.

Domestic Building and Loan Association Test

To be a QTL under the DBLA test (IRS regulation 26 CFR § 301.7701-13A), an institution must meet a "business operations test" and a "60 percent of assets test."

The business operations test requires the business of a DBLA to consist primarily of acquiring the savings of the public and investing in loans. An institution meets the public savings requirement when it meets one of two conditions:

- The institution acquires its savings in conformity with OTS rules and regulations.
- The general public holds more than 75 percent of its deposits, withdrawable shares, and other obligations. The general public may not include family or related business groups or persons who are officers or directors of the institution.

An institution meets the investing in loans requirement when more than 75 percent of its gross income consists of interest on loans and government obligations, and various other specified types of operating income that financial institutions ordinarily earn.

The 60 percent of assets test requires that at least 60 percent of a DBLA's assets must consist of assets that thrifts normally hold, except for consumer loans that are not educational loans. The DBLA test does not include, as the QTL test does to a limited or optional extent, mortgage loans originated and sold into the secondary market and subsidiary investments.

See Appendix A for the Internal Revenue Code statutory definition of domestic building and loan association (26 USCA § 7701(a)(19)). See Appendix B for the IRS's implementing regulation defining domestic building and loan association (26 CFR § 301.7701-13A).

Background

Congress first established the QTL test as part of the Competitive Equality Banking Act of 1987 (CEBA). Effective January 1, 1988, the Federal Home Loan Bank Board implemented the CEBA provisions. This required all thrift institutions to invest at least 60 percent of their tangible assets in certain housing and related investments to maintain QTL status.

Congress amended the QTL test as part of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) and raised the required ATIP to 70 percent. The statute phased in the changes over a two-year period. On August 9, 1990, new penalty provisions for failing the QTL test became effective and on July 1, 1991, the remainder of the FIRREA changes became effective.

The Federal Deposit Insurance Corporation Improvement Act of 1991 lowered the required ATIP to 65 percent and changed the computation period from a required weekly average to a required maintenance period of 9 out of 12 immediately preceding months.

The Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA) amended the QTL requirements to give thrifts a choice of tests. A thrift must qualify either by meeting the HOLA QTL test, as amended by the EGRPRA, or by meeting the IRS's DBLA tax code test. The EGRPRA amended the QTL test to allow:

- Educational loans, small business loans, and credit card loans to count as QTIs without limit.
- Loans for personal, family, or household purposes (other than those included in the without limit category) to count as QTI in the category limited to 20 percent of portfolio assets.

Exceptions

Pursuant to 12 USC § 1467a(m)(2), OTS may grant temporary and limited exceptions from compliance with the QTL test. OTS may grant exceptions when extraordinary circumstances exist, or to significantly facilitate an acquisition under §13(c) or §13(k) of the Federal Deposit Insurance Act (FDIA).

Section 1467a(m)(2)(A) presents an example of an extraordinary circumstance: when the effects of high interest rates reduce mortgage demand to such a degree that an insufficient opportunity ex-

ists for a savings association to meet the QTL requirement. Also, Thrift Bulletin 71, "Serving Communities Affected by Natural Disasters," explains that within the constraints of safety and soundness and statutory requirements, the OTS will facilitate savings association efforts to assist communities affected by a natural disaster. In doing so, the OTS may temporarily waive the QTL requirement to allow capital compliant institutions to help rebuild non-QTL businesses.

Section 13(c) of the FDIA authorizes the FDIC to provide financial assistance to facilitate a merger or consolidation of a troubled insured depository institution. Section 13(k) of the FDIA sets forth criteria for such emergency acquisitions of troubled institutions. When granting an exception to significantly facilitate a § 13(c) or §13(k) acquisition, the OTS must determine the following:

- The acquired association will comply with a 51-month incremental phase-in transaction period (see 12 USC §§ 1467a(m)(2)(B)(ii) and (m)(7)(B)).
- The exception will not have an undue adverse effect on competing savings associations in the relevant market and will further the purposes of the QTL test.

Definitions of QTL Terms

An institution must be able to demonstrate that items being counted as QTI meet the specific definitions set forth below:

Acquisition, Development, and Construction (ADC) Loans

Associations may include ADC loans in QTI without limit provided the association is reasonably certain the property will become domestic residential housing. Moreover, to count as QTI, an ADC loan must meet at least one of the following criteria:

- The loan is for property zoned exclusively for residential use.
- The loan is for property zoned to permit residential use and there are restrictions in the deed to the property that limit its use to primarily residential dwellings.
- The borrower will construct dwellings immediately on nearly all the residentially zoned property.

Community Service Facilities

Community service facility means churches or other places of worship, schools, nursing homes, hospitals, and facilities serving similar functions within a community.

Domestic Housing

This term refers to housing located within the 50 states, the District of Columbia, Puerto Rico, the Virgin Islands, Guam, and the Pacific Islands.

Loans To Credit-Needy Areas

A credit-needy area is a geographic area or neighborhood in which the credit needs of the low- and moderate income residents are not being adequately met. This includes any census tract or block numbering area delineated by the United States Bureau of the Census where median income is less than 80 percent of the area median income. Area median income means the median family income for a Metropolitan Statistical Area (MSA), or the statewide non-metropolitan area if located outside an MSA.

A credit-needy area may also be an area that meets either of the following criteria:

- An area targeted for redevelopment by a federal, state, tribal or local government that also receives some form of financial assistance from the federal, state, tribal or local government.
- Identified as credit-needy through consultations with local government and community representatives. These determinations will be subject to review for reasonableness during examinations.
  - In addition, if the loan is for a small business or a "community service facility" the association may classify it as a loan to a credit-needy area if it meets one of the following criteria:

— The loan is to a community service facility or a small business within the credit-needy area.

— The loan is to a small business owned by an individual whose home address is within the credit-needy area.

— The loan is to a community service facility that primarily serves individuals whose homes are within the credit-needy area.

For example, under the first criteria, a loan to a community center, school, or small business in a credit-needy area would qualify. Under the second, a small business loan to a person living in a credit-needy area but whose business is not within such an area would qualify. Finally, under the third criteria, loans to hospitals, churches or school dormitories that have clientele, the majority of who live in credit-needy areas, would qualify.

Manufactured Housing

Manufactured housing has the same meaning as defined by the National Manufactured Home Construction and Safety Standards Act in 42 USC Section 5402(6):

> A structure, transportable in one or more sections, that in traveling mode measures at least eight feet by forty feet, or when erected is at least 320 square feet, and that is built on a permanent chassis and designed to be used as a dwelling with or without a permanent foundation when connected to the required utilities, and includes the plumbing, heating, air-conditioning, and electrical systems contained therein.

Mutual Funds

An institution may count mutual fund investments as QTI on a pro rata basis to the same extent that the underlying investments are eligible as QTI if the institution invested directly in the underlying investments. The mutual funds must also meet the other standards set forth in HOLA § 5(c)(1)(Q).

Residential Housing

For QTL purposes, residential housing includes OTS's regulatory 12 CFR Part 541 definitions of "residential real estate" and "dwelling unit." Section 541.23 also defines residential real estate (or residential real property):

- Homes (including condominiums and cooperatives).
- Combinations of homes and business property.
- Other real estate used for primarily residential purposes other than a home (but which may include homes).
- Combinations of such real estate and business property involving only minor business use.
- Farm residences and combinations of farm residences and commercial farm real estate.
- Property to be improved by the construction of such structures.
- Leasehold interests in the above real estate.

Section 541.10 defines dwelling unit to mean, "The unified combination of rooms designed for residential use by one family, other than a single-family dwelling."

Small Business Loans

<u>OTS definition</u>

OTS adopted the definition of a small business loan in the Thrift Financial Report Instructions to enhance small business lending without adding unnecessary complexity. Schedule SB defines a small business loan as a business loan with an original amount of $1 million or less. The following guidelines also apply:

- Generally, the original amount of a loan is the total amount of the loan at origination or the amount of the loan balance outstanding, whichever is larger.
- For loan participations and syndications, the original amount of the loan participation or syndication is the entire amount of the credit the lead lender originated.
- For loans drawn down under lines of credit or loan commitments, the original amount of the loan is the amount when the lender most recently approved, extended, or renewed the line of credit or loan commitment before the report

date. However, if the amount currently outstanding as of the report date exceeds this size, the original amount is the amount currently outstanding.

- Institutions should combine multiple loans to one borrower and report them on an aggregated basis.

Small Business Administration (SBA) Definition

OTS regulation 12 CFR § 560.3 also cites the SBA definition of small business loans. Savings associations familiar with the SBA standards may prefer to use the eligibility criteria established by the SBA. See section 3(a) of the Small Business Act (Act), 15 USC 632(a), as implemented by SBA's regulations at 13 CFR Part 121.

Section 3(a) of the Act states that a small business concern must be independently owned and operated and not dominant in its field of operation. The Act provides that the definition shall vary from industry to industry in determining what a small business is to the extent necessary to properly reflect industry differences. In addition, the SBA is to make a detailed definition of the term based on, among other criteria, a business's number of employees and dollar amount of business.

The SBA size standards at 13 CFR Part 121 define the maximum sizes to be eligible as a small business concern. Two principal maximum size standards are 500 employees for most manufacturing and mining industries, and $5 million in average annual receipts for most manufacturing industries. However, many exceptions exist and the SBA periodically changes size standards for different industries. Reference to the regulations is necessary to determine size eligibility requirements for a specific business concern.

Starter Home Loans

To be defined as a starter home loan for QTL purposes, a loan must meet certain criteria:

- Be secured by a one-to-four family home or multifamily residential dwelling; or by a development where 75 percent or more of the value of the development consists of such homes. In developments, up to 25 percent of the loan amount may be for facilities serving the community such as community centers or shopping malls.
- Be appraised at the time of loan origination at 60 percent less than the median value of newly constructed one- to four-family houses in the community where the starter home is located.

If no median figures are available for the local community, there are three permissible methods for estimating the median housing price in the community.

- Federal Housing Finance Board (FHFB) Method. An institution may rely on the most recent annual statewide housing value data generated by the FHFB. OTS regional offices will make the FHFB data available.
- National Association of Home Builders (NAHB) Method. NAHB publishes median housing prices monthly for 190 metropolitan areas as part of its Housing Opportunity Index. Associations may use the most recent NAHB data if it includes the local community in which the starter home is located.
- Private Method. An institution may rely on figures generated by a private company that has substantial experience conducting market surveys. The association may use the data on newly constructed housing values for one year after the date of the survey. The survey methodology will be subject to review during examinations.

Consolidation of Subsidiaries

In determining an institution's portfolio assets in the calculation of its ATIP, the institution must consolidate its assets with a subsidiary's assets in the following situations:

- The institution consolidates the subsidiary's assets with the institution's assets in determining its QTI.
- The association includes the subsidiary's residential mortgage loans originated and sold within 90 days of origination to determine the institution's QTI.

Except for these circumstances, an institution has the option to consolidate or not, and may make such a decision as frequently as monthly.

Penalties

Statutory penalty provisions require an institution that fails to remain a QTL to either become a national bank or be prohibited from the following:

- Making any new investments or engaging in any activity not allowed for both a national bank and a savings association.
- Establishing any new branch office unless allowable for a national bank.
- Obtaining new FHLBank advances.
- Paying dividends unless allowable for a national bank.

Any company that controls a savings association that fails to regain its QTL status within one year must register as and be deemed to be a bank holding company.

Three years from the date a savings association ceases to be a QTL, by failing either to meet the QTL test or the DBLA test, the institution must comply with the following restrictions:

- Not retain any investment or engage in any activity not allowed for both a national bank and a savings association.
- Promptly and prudently repay any FHLBank advances.

Requalification

A savings association may requalify as a QTL only once. Failure to maintain QTL status after requalification permanently subjects a savings association to the penalties described above.

Monitoring QTL Compliance

You are responsible for reviewing an institution's policies and procedures for maintaining QTL or DBLA status. You must also review documentation with the primary focus on the following:

- Evaluate the eligibility of qualifying investments and to reconcile the amounts recorded.
- Ensure that calculations reported on Schedule SI of an institution's Thrift Financial Report are correct.
- Confirm that the institution's QTL or DBLA status is correct.

References

United States Code (12 USC)

§ 1430(e)	Reduced Eligibility for Advances
§ 1467a(m)	Qualified Thrift Lender Test

United States Code (15 USC)

§ 632(a)	Small Business Act

United States Code (26 USC)

§ 7701(a)(19)	Domestic Building and Loan Association Test

United States Code (42 USC)

§ 5402(6)	National Manufactured Home Construction and Safety Standards Act

Code of Federal Regulations (12 CFR)

§ 566.1	Liquidity Definitions

Code of Federal Regulations (13 CFR)

Part 121	Small Business Regulations

Code of Federal Regulations (26 CFR)

§ 301.7701-13A	Post-1969 Domestic Building and Loan Association

Office of Thrift Supervision Bulletins

TB 71	Serving Communities Affected by Natural Disasters

Internal Revenue Code Definition of "Domestic Building and Loan Association"

26 U.S.C.A. § 7701(a)(19)

(19) *Domestic building and loan association*.--The term "domestic building and loan association" means a domestic building and loan association, a domestic savings and loan association, and a Federal savings and loan association--

(A) which either (i) is an insured institution within the meaning of section 401(a) of the National Housing Act (12 U.S.C., sec. 1724(a)), or (ii) is subject by law to supervision and examination by State or Federal authority having supervision over such associations;

(B) the business of which consists principally of acquiring the savings of the public and investing in loans; and

(C) at least 60 percent of the amount of the total assets of which (at the close of the taxable year) consists of--

(i) cash,

(ii) obligations of the United States or of a State or political subdivision thereof, and stock or obligations of a corporation which is an instrumentality of the United States or of a State or political subdivision thereof, but not including obligations the interest on which is excludable from gross income under section 103,

(iii) certificates of deposit in, or obligations of, a corporation organized under a State law which specifically authorizes such corporation to insure the deposits or share accounts of member associations,

(iv) loans secured by a deposit or share of a member,

(v) loans (including redeemable ground rents, as defined in section 1055) secured by an interest in real property which is (or, from the proceeds of the loan, will become) residential real property or real property used primarily for church purposes, loans made for the improvement of residential real property or real property used primarily for church purposes, provided that for purposes of this clause, residential real property shall include single or multifamily dwellings, facilities in residential developments dedicated to public use or property used on a nonprofit basis for residents, and mobile homes not used on a transient basis,

(vi) loans secured by an interest in real property located within an urban renewal area to be developed for predominantly residential use under an urban renewal plan approved by the Secretary of Housing and Urban Development under part A or part B of title I of the Housing Act of 1949, as amended, or located within any area covered by a program eligible for assistance under section 103 of the Demonstration Cities and Metropolitan Development Act of 1966, as amended, and loans made for the improvement of any such real property,

(vii) loans secured by an interest in educational, health, or welfare institutions or facilities, including structures designed or used primarily for residential purposes for students, residents, and persons under care, employees, or members of the staff of such institutions or facilities,

(viii) property acquired through the liquidation of defaulted loans described in clause (v), (vi), or (vii),

(ix) loans made for the payment of expenses of college or university education or vocational training, in accordance with such regulations as may be prescribed by the Secretary,

(x) property used by the association in the conduct of the business described in subparagraph (B), and

(xi) any regular or residual interest in a REMIC, but only in the proportion which the assets of such REMIC consist of property described in any of the preceding clauses of this subparagraph; except that if 95 percent or more of the assets of such REMIC are assets described in clauses (i) through (x), the entire interest in the REMIC shall qualify.

At the election of the taxpayer, the percentage specified in this subparagraph shall be applied on the basis of the average assets outstanding during the taxable year, in lieu of the close of the taxable year, computed under regulations prescribed by the Secretary. For purposes of clause (v), if a multifamily structure securing a loan is used in part of nonresidential purposes, the entire loan is deemed a residential real property loan if the planned residential use exceeds 80 percent of the property's planned use (determined as of the time the loan is made). For purposes of clause (v), loans made to finance the acquisition or development of land shall be deemed to be loans secured by an interest in residential real property if, under regulations prescribed by the Secretary, there is reasonable assurance that the property will become residential real property within a period of three years from the date of acquisition of such land; but this sentence shall not apply for any taxable year unless, within such three-year period, such land becomes residential real property. For purposes of determining whether any interest in a REMIC qualifies under clause (xi), any regular interest in another REMIC held by such REMIC shall be treated as a loan described in a preceding clause under principles similar to the principles of clause (xi); except that, if such REMIC's are part of a tiered structure, they shall be treated as one REMIC for purposes of clause (xi).

Internal Revenue Service's Regulatory Definition of "Domestic Building and Loan Association"

26 CFR Ch. 1 (4-1-96 Edition)

§ 301.7701-13A. Post-1969 domestic building and loan association.

(a) In general. For taxable years beginning after July 11, 1969, the term "domestic building and loan association" means a domestic building and loan association, a domestic savings and loan association, a Federal savings and loan association, and any other savings institution chartered and supervised as a savings and loan or similar association under Federal or State law which meets the supervisory test (described in paragraph (b) of this section), the business operations test (described in paragraph (c) of this section), and the assets test (described in Paragraph (d) of this section). For the definition of the term "domestic building and loan association" for taxable years beginning after October 16, 1962, and before July 12, 1969, see § 301.7701-13.

(b) Supervisory test. A domestic building and loan association must be either (1) an insured institution within the meaning of section 401(a) of the National Housing Act (12 U.S.C. 1724(a)) or (2) subject by law to supervision and examination by State or Federal authority having supervision over such associations. An "insured institution" is one the accounts of which are insured by the Federal Savings and Loan Insurance Corporation.

(c) Business operations test--(1) In general. An association must utilize its assets so that its business consists principally of acquiring the savings of the public and investing in loans. The requirement of this paragraph is referred to in this section as the business operations test. The business of acquiring the savings of the public and investing in loans includes ancillary or incidental activities which are directly and primarily related to such acquisition and investment, such as advertising for savings, appraising property on which loans are to be made by the association, and inspecting the progress of construction in connection with construction loans. Even though an association meets the supervisory test described in paragraph (b) of this section and the assets test described in paragraph (d) of this section, it will nevertheless not qualify as a domestic building and loan association if it does not meet the requirements of both paragraphs (2) and (3) of this paragraph (c), relating, respectively, to acquiring the savings of the public and investing in loans.

(2) Acquiring the savings of the public. The requirement that an association's business (other then investing in loans) must consist principally of acquiring the savings of the public ordinarily will be considered to be met if savings are acquired in all material respects in conformity with the rules and regulations of the Federal Home Loan Bank Board or substantially equivalent rules of a State law or supervisory authority. Alternatively, such requirement will be considered to be met if more than 75 percent of the dollar amount of the total deposits, withdrawable shares, and other obligations of the association are held during the taxable year by the general public, as opposed to amounts deposited or held by family or related business groups or persons who are officers or directors of the association. However, the preceding sentence shall not apply if the dollar amount of other obligations of the association outstanding during the taxable year exceeds 25 percent of the dollar amount of the total deposits, withdrawable shares, and other obligations of the association outstanding during such year. For purposes of this paragraph, the term "other obligation" means notes, bonds, debentures, or other obligations, or other securities (except capital stock), issued by an association in conformity with the rules and regulations of the Federal Home Loan Bank Board or substantially equivalent rules of a State law or supervisory author-

ity. The term "other obligations" does not include an advance made by a Federal Home Loan Bank under the authority of section 10 or 10b of the Federal Home Loan Bank Act (12 U.S.C. 1430, 1430b) as amended and supplemented. Both percentages specified in this paragraph shall be computed either as of the close of the taxable year or, at the option of the taxpayer, on the basis of the average of the dollar amounts of the total deposits, withdrawable shares, and other obligations of the association held during the taxable year. Such averages shall be determined by computing each percentage specified either as of the close of each month, as of the close of each quarter, or semiannually during the taxable year and by using the yearly average of the monthly, quarterly, or semiannual percentages obtained. The method selected must be applied uniformly for the taxable year to both percentages, but the method may be changed from year to year.

(3) Investing in loans--(i) In general. The requirement that an association's business (other than acquiring the savings of the public) must consist principally of investing in loans will be considered to be met for a taxable year only if more than 75 percent of the gross income of the association consists of--

(a) Interest or dividends on assets defined in paragraphs (1), (2), and (3) of paragraph (e) of this section,

(b) Interest on loans,

(c) Income attributable to the portion of property used in the association's business, as defined in paragraph (e)(11) of this section,

(d) So much of the amount of premiums, discounts, commissions, or fees (including late charges and penalties) on loans which have at some time been held by the association, or for which firm commitments have been issued, as is not in excess of 20 percent of the gross income of the association,

(e) Net gain from sales and exchanges of governmental obligations, as defined in paragraph (e)(2) of this section, or

(f) Income, gain or loss attributable to foreclosed property, as defined in paragraph (e)(9) of this section, but not including such income, gain or loss which, pursuant to section 595 and the regulations thereunder, is not included in gross income. Examples of types of income which would cause an association to fail to meet the requirements of this paragraph if, in the aggregate, they equal or exceed 25 percent of gross income, are: The excess of gains over losses from sales of real property (other than foreclosed property); rental income (other than on foreclosed property and the portion of property used in the association's business); premiums, commission, and fees (other than commitment fees) on loans which have never been held by the association; and insurance brokerage fees.

(ii) Computation of gross income. For purposes of this paragraph, gross income is computed without regard to--

(a) Gain or loss on the sale or exchange of the portion of property used in the association's business as defined in paragraph (e)(11) of this section.

(b) Gain or loss on the sales or exchange of the rented portion of property used as the principal or branch office of the association, as defined in paragraph (e)(11) of this section, and

(c) Gains or losses on sales of participations, and loans, other than governmental obligations defined in paragraph (e)(2) of this section.

For purposes of this paragraph, gross income is also computed without regard to items of income which an association establishes arise out of transactions which are necessitated by

exceptional circumstances and which are not undertaken as recurring business activities for profit. Thus, for example, an association would meet the investing in loans requirement if it can establish that it would otherwise fail to meet that requirement solely because of the receipt of a nonrecurring item of income due to exceptional circumstances. For this purpose, transactions necessitated by an excess of demand for loans over savings capital in the association's area are not to be deemed to be necessitated by exceptional circumstances. For purposes of paragraph (c)(3)(ii)(c) of this section, the term "sales of participations" means sales by an association of interest in loans, which sales meet the requirements of the regulations of the Federal Home Loan Bank Board relating to sales of participations, or which meet substantially equivalent requirements of State law or regulations relating to sales of participations.

(iii) Reporting requirement. In the case of income tax returns for taxable years beginning after July 11, 1969, there is required to be led with the return a statement showing the amount of gross income for the taxable year in each of the categories described in paragraph (c)(3)(i) of this section.

(d) 60 Percent of assets test. At least 60 percent of the amount of the total assets of a domestic building and loan association must consist of the assets defined in paragraph (e) of this section. The percentage specified in this paragraph is computed as of the close of the taxable year or, at the option of the taxpayer, may be computed on the basis of the average assets outstanding during the taxable year. Such average is determined by making the appropriate computation described in this section either as of the close of each month, as of the close of each quarter, or semiannually during the taxable year and by using the yearly average of the monthly, quarterly, or semiannual percentage obtained for each category of assets defined in paragraph (e) of this section. The method selected must be applied uniformly for the taxable year to all categories of assets, but the method may be changed form year to year. For purposes of this paragraph, it is immaterial whether the association originated the loans defined in paragraphs (4) through (8) and (10) of paragraph (e) of this section or purchased or otherwise acquired them in whole or in part from another. See paragraph (f) of this section for definition of certain terms used in this paragraph and in paragraph (e) of this section, and for the determination of amount and character of loans.

(e) Assets defined. The assets defined in this paragraph are--

(1) Cash. The term "cash" means cash on hand, and time or demand deposits with, or withdrawable accounts in, other financial institutions.

(2) Governmental obligations. The term "governmental obligations" means--

(i) Obligations of United States,

(ii) Obligations of a State or political subdivision of a State, and

(iii) Stock or obligations of a corporation which is an instrumentality of the United States, a State, or a political subdivision of a State, other than obligations the interest on which is excludable from gross income under section 103 and the regulations thereunder.

(3) Deposit insurance company securities. The term "deposit insurance company securities" means certificates of deposit in, or obligations of, a corporation organized under a State law which specifically authorizes such corporation to insure the deposits or share accounts of member associations.

(4) Passbook loan. The term "passbook loan" means a loan to the extent secured by a deposit, withdrawable share, or savings account in the association, or share of a member of the association, with respect to which a distribution is allowable as a deduction under section 591.

(5) Residential real property loan. [Reserved]

(6) Church loan. [Reserved]

(7) Urban renewal loan. [Reserved]

(8) Institutional loan. [Reserved]

(9) Foreclosed property. [Reserved]

(10) Educational loan. [Reserved]

(11) Property used in the association's business--(i) In general. The term "property used in the association's business" means land, buildings, furniture, fixtures, equipment, leasehold interests, leasehold improvements, and other assets used by the association in the conduct of its business of acquiring the savings of the public and investing in loans. Real property held for the purpose of being used primarily as the principal or branch office of the association constitutes property used in the association's business so long as it is reasonably anticipated that such property will be occupied for such use by the association, or that construction work preparatory to such occupancy will be commenced thereon, within 2 years after acquisition of the property. Stock of a wholly owned subsidiary corporation which has as its exclusive activity the ownership and management of property more than 50 percent of the fair rental value of which is used as the principal or branch office of the association constitutes property used in such business. Real property held by an association for investment or sale, even for the purpose of obtaining mortgage loans thereon, does not constitute property used in the association's business.

(ii) Property rented to others. Except as provided in the second sentence of paragraph (11)(i) of this paragraph (e), property or a portion thereof rented by the association to others does not constitute property used in the association's business. However, if the fair rental value of the rented portion of a single piece of real property (including appurtenant parcels) used as the principal or branch office of the association constitutes less than 50 percent of the fair rental value of such piece of property, or if such property has an adjusted basis of not more than $150,000, the entire property shall be considered used in such business. If such rented portion constitutes 50 percent or more of the fair rental value of such piece of property, and such property has an adjusted basis of more than $150,000, an allocation of its adjusted basis is required. The portion of the total adjusted basis of such piece of property which is deemed to be property used in the association's business shall be equal to an amount which bears the same ratio to such total adjusted basis as the amount of the fair rental value of the portion used as the principal or branch office of the association bears to the total fair rental value of such property. In the case of all property other than real property used or to be used as the principal or branch office of the association, if the fair rental value of the rented portion thereof constitutes less than 15 percent of the fair rental value of such property, the entire property shall be considered used in the association's business. If such rented portion constitutes 15 percent or more of the fair rental value of such property, an allocation of its adjusted basis (in the same manner as required for real property used as the principal or branch office) is required.

(12) Regular or residual interest in a REMIC--(i) In general. If for any calendar quarter at least 95 percent of a REMIC's assets (as determined in accordance with § 1.860F-4(e)(1)(ii) or § 1.6049-7(f)(3) of this chapter) are assets defined in paragraph (e)(1) through (e)(11) of this section, then for that calendar quarter all the regular and residual interests in that REMIC are treated as assets defined in this paragraph (e). If less than 95 percent of a REMIC's assets are assets defined in paragraph (e)(1) through (e)(11) of this section, the percentage of each REMIC regular or residual interest treated as an asset defined

in this paragraph (e) is equal to the percentage of the REMIC's assets that are assets defined in paragraph (e)(1) through (e)(11) of this section. See §§ 1.860F-4(e)(1)(ii)(B) and 1.6049-7(f)(3) of this chapter for information required to be provided to regular and residual interest holders if the 95 percent test is not met.

(ii) Loans secured by manufactured housing. For purposes of paragraph (e)(12)(i) of this section, a loan secured by manufactured housing treated as a single family residence under section 25(e)(10) is an asset defined in paragraph (e)(1) through (e)(11) of this section.

(f) Special rules. [Reserved]

QTL Worksheet for the Month of _____

	Line	Amount *(in thousands)*
PORTFOLIO ASSETS		
Total Assets	**1**	
20% of Total Assets *(Line 1 X .20)*	**2**	
Office Building	**3**	
Regulatory Liquidity	**4**	
Goodwill and Other Intangibles	**5**	
Deductions from Total Assets *(Sum of Lines 3, 4, and 5)*	**6**	
PORTFOLIO ASSETS *(Lines1 Minus Line 6)*	**7**	
20% OF PORTFOLIO ASSETS *(Line 7 X .20)*	**8**	
QUALIFIED THRIFT INVESTMENTS (QTI)		
ASSETS INCLUDABLE WITHOUT LIMIT		
Mortgage Loans	**9**	
Real Estate Owned (Residential)	**10**	
Home Equity Loans	**11**	
Mortgage-Backed Securities	**12**	
Educational Loans	**13**	
Small Business Loans	**14**	
Credit Card Loans	**15**	
Obligations of Deposit Insurance Agencies (Prior to 7/1/89)	**16**	
Obligations of Deposit Insurance Agencies (On or After 7/1/89)	**17**	
Federal Home Loan Bank Stock	**18**	
TOTAL QTI INCLUDABLE WITHOUT LIMIT *(Sum of Lines 9 through 18)*	**19**	
ASSETS INCLUDABLE UP TO 20% OF PORTFOLIO ASSETS		
50% Of Residential Mortgage Loans Originated and Sold Within 90 Days	**20**	
80% Service Corporations	**21**	
200% of 1-4 Family Residence Loans (Starter Homes <60% Median)	**22**	
200% of Certain Loans in Credit-Needy Areas	**23**	
Community Service Facility Loans (Purchase, Construction, Improvement)	**24**	
Loans for Personal, Family, or Household Purposes	**25**	
FNMA or FHLMC Stock	**26**	
FOR PUERTO RICAN AND VIRGIN ISLAND INSTITUTIONS ONLY		
Loans for Personal Family or Household Purposes	**27**	
Community Service Facility Loans (Purchase, Construction, Improvement)	**28**	
200% of 1-4 Family Residence Loans (Starter Homes<Median)	**29**	
Total QTI Includable Up to 20% of Portfolio Assets *(The Lesser of the Sum of Lines 20-26 or Line 8)*	**30**	
TOTAL QUALIFIED THRIFT INVESTMENTS *(Sum of Lines 19 and 30)*	**31**	
ACTUAL THRIFT INVESTMENT PERCENTAGE *(Line 31 Divided by Line 7)*	**32**	%

OTS Form 1427

Instructions for QTL Worksheet

To calculate the actual thrift investment percentage (ATIP), follow the instructions below and refer to the QTL worksheet. Each institution that elects to comply with the QTL test must perform these calculations on a monthly basis.

Part 1 – Portfolio Assets

Line 1 – Total Assets

Enter total assets. Consolidate a subsidiary if the association counts as a qualified thrift investment any of the subsidiary's assets, or mortgages originated and sold within 90 days of origination. Also, if the institution counts its investment in an 80% mortgage-related revenue subsidiary as qualified thrift investment on Line 21, it must include that investment in total assets.

Line 2 – 20% of Total Assets

Multiply Line 1 by 0.20.

Line 3 – Office Building

Enter the depreciated carrying value of the property, furniture, fixtures, and equipment that the institution uses to conduct its business.

Line 4 – Regulatory Liquidity

Enter the lesser of the institution's assets that qualify as regulatory liquidity (regardless of the percentage required in Part 566) or the amount on Line 2. Do not include as liquidity any securities entered on Line 12.

Line 5 – Goodwill and Other Intangibles

Enter the current unamortized balance of goodwill and other intangibles (including mortgage loan servicing rights).

Line 6 – Deductions from Total Assets

Enter the sum of Lines 3, 4, and 5.

Line 7 – Portfolio Assets

Subtract Line 6 from Line 1.

Line 8 – 20% of Portfolio Assets

Multiply Line 7 by 0.20.

Part 2 – Qualified Thrift Investments

Note: For all calculations use the outstanding principal balance and add accrued interest and premiums; deduct specific valuation allowances, charge-offs, deferred loan fees, loans in process and unearned discounts.

A. Assets Includable Without Limit

Line 9 – Mortgage Loans

Enter loans held that were made to purchase, refinance, construct, improve, or repair domestic residential housing or manufactured housing. *Note*: The term "domestic" refers to units within the 50 states, the District of Columbia, Puerto Rico, the Virgin Islands, Guam, and the Pacific Islands.

Line 10 – REO (Residential)

Enter property acquired through foreclosure, deed in lieu of foreclosure, or in-substance foreclosure that if it had remained as a loan would have been a qualified thrift investment reported on Lines 9, 11, or 14. Include real estate in judgment.

Line 11 – Home Equity Loans

Enter home equity loans. *Note*: Include here any consumer receivables secured in part by lien on domestic residential housing. If entered here do not include on Line 25.

Line 12 – Mortgage-Backed Securities

Enter securities backed by or representing an interest in domestic residential housing or manufactured housing. Institutions should include securities purchased and exclude securities sold from qualified thrift investments on their trade dates. *Note:* This item encompasses mortgage-pool securities, mortgage-pool pass-through secu-

rities, mortgage-backed bonds, and mortgage-backed pay-through bonds. This item also encompasses any derivative mortgage-related security created by disaggregating and repackaging the cash flows received as payments on mortgages and traditional mortgage-pool securities. The underlying assets of such securities must be domestic residential housing. Bonds, including FHLB, FHLMC, FNMA and GNMA bonds, count only if they are backed by mortgages. Do not include as a qualified thrift investment Resolution Funding Corporation (REFCO) bonds.

Line 13 – Educational Loans

Enter education loans.

Line 14 – Small Business Loans

Enter small business loans. Generally, small business loans are $1 million or less at origination. See further guidance in the Thrift Financial Report Instructions, Section SB.

Line 15 – Credit Card Loans

Enter loans made in conjunction with the issuance or extension of credit through a credit card. This includes loans made to consolidate credit card debt (including credit card debt that other lenders previously held), participation certificates, securities and similar instruments secured by credit card receivables.

Line 16 – Obligations of Deposit Insurance Agencies Issued Prior to July 1, 1989

Enter obligations of the FDIC or FSLIC issued before July 1, 1989, for a period not to exceed ten years past the issue date.

Line 17 – Obligations of Deposit Insurance Agencies Issued On or After July 1, 1989

Enter obligations of the FDIC, the FSLIC, the FSLIC Resolution Fund, or the RTC issued on or after July 1, 1989, for a period not to exceed five years past the issue date.

Line 18 – Federal Home Loan Bank Stock

Enter Federal Home Loan Bank stock.

Line 19 – Total Qualified Thrift Investments Includable Without Limit

Enter the sum of Lines 9 through 18.

B. Assets Includable up to 20% of Portfolio Assets

Line 20 – 50% of Residential Mortgage Loans Originated and Sold Within 90 Days

Enter 50% of loans on domestic residential housing that the association originated and sold within 90 days of origination, provided that the association sold these mortgage loans during the quarter for which this calculation is being made. Associations may use either the previous quarter's figures or a rolling 90-day period.

Line 21 – 80% Service Corporations

Enter the investment (capital stock, loans, advances, and securities) in service corporations that derive 80% of their gross revenues from dealing in domestic residential housing or manufactured housing. *Note*: Institutions that consolidate such subsidiaries in Line 1 (Total Assets) and count any service corporation assets as qualified thrift investments may not report the institution's investment on this line.

Line 22 – 200% of One- to Four-Family Residence Loans (Starter Homes Less than 60% Median)

Enter 200% of loans and investments in domestic residential housing (if not entered on Line 9), the price of which is, or is guaranteed to be, less than 60% of the median price of comparable housing in the community where the housing is located. *Note*: To use this line item, institutions must maintain records demonstrating that the housing meets the 60% of median value test. See definition of starter home loans.

Line 23 – 200% of Certain Loans In Credit-Needy Areas

Enter 200% of loans on domestic residential housing, community service facilities, and to small businesses in credit-needy areas. Do not include any small business loans here if entered on Line 14.

Line 24 – Community Service Facility Loans (Purchase, Construction, Improvement)

Enter loans for community service facilities except those included on Line 23.

Line 25 – Loans for Personal, Family, or Household Purposes

Enter personal, family, household, or share loans, except those included on Lines 11, 13 and 15.

Line 26 – Stock of the FNMA or the FHLMC

Enter FNMA and FHLMC stock that the institution holds.

Puerto Rican and Virgin Island Institutions Only -- All Other Thrifts Go to Line 30.

Note: For Lines 27 and 29, the amounts that Puerto Rican thrifts enter may only be for investments in Puerto Rico. Similarly, the amounts that Virgin Islands thrifts enter may only be for investments in the Virgin Islands.

Line 27 – Loan for Personal, Family or Household Purposes

Enter personal, family, household, or share loans made to persons residing or domiciled in Puerto Rico or the Virgin Islands. Do not include loans entered on Lines 11 or 25.

Line 28 – Community Service Facility Loans (Purchases, Construction, Improvement)

Enter loans for community service facilities and loans to small businesses in Puerto Rico or the Virgin Islands, except those included on Lines 23 and 24.

Line 29 – 200% of One- to Four-Family Residence Loans (Starter Homes Less than Median)

Enter 200% of loans and investments in domestic residential housing in Puerto Rico and the Virgin Islands, the price of which is, or is guaranteed to be, less than the median price of comparable housing in the community where the housing in located. Do not include loans entered on Line 22. *Note:* To use this line item, institutions must maintain records demonstrating that the housing meets the median value test.

Line 30 – Total Qualified Thrift Investments Includable Up to 20% of Portfolio Assets

Enter the lesser of the sum of Lines 20 through 26 or Line 8.

Part 3 – Total Qualified Thrift Investments and Actual Thrift Investment Percentage

Line 31 – Total Qualified Thrift Investments

Enter the sum of Lines 19 and 30. This is a savings association's total qualified thrift investment figure. If you are a Puerto Rican or Virgin Island savings association, also add Lines 27 through 29.

Line 32 – Actual Thrift Investment Percentage (ATIP)

Divide Line 31 by Line 7.

Qualified Thrift Lender Status Program

Examination Objectives

To evaluate the institution's policies, procedures, and controls for maintaining QTL or DBLA status.

To confirm the institution's QTL or DBLA status.

To ensure that the institution observes any consequent limitations or penalties for QTL or DBLA failure.

Examination Procedures

Wkp.Ref.

Level I

1. Determine if the institution observes the QTL or DBLA test. If it is the DBLA test, determine if the institution meets applicable DBLA criteria.

_____ _____

2. Review and assess the accuracy of the Qualified Thrift Lender Worksheet or records of compliance with the DBLA test.

_____ _____

3. Determine whether the institution met the requirements of the QTL or DBLA test since the last examination.

_____ _____

4. Review the previous examination report to determine the presence of any QTL-related issues.

_____ _____

5. Assess the institution's policies, procedures, and controls relating to maintenance of QTL or DBLA status.

_____ _____

6. Determine whether any exceptions to the QTL requirement exist, such as extraordinary circumstances.

_____ _____

7. Determine if the institution records all investments correctly.

_____ _____

Exam Date: _____
Prepared By: _____
Reviewed By: _____
Docket #: _____

Wkp.Ref.

8. Determine if all investments counted as QTI meet the applicable standards.

_____ _____

9. Review documentation supporting the inclusion of any investments that are not clearly eligible.

_____ _____

10. Ensure that the review meets the Examination Objectives of this Handbook Section. State your findings, conclusions, and appropriate recommendations for any necessary corrective measures on the appropriate work papers and report pages.

_____ _____

11. If the institution failed the QTL or DBLA test, perform Level II procedures.

_____ _____

Level II

12. When the institution has failed the QTL or DBLA test, determine if the failure is the first one.

_____ _____

13. Determine how long the failure has lasted and if the institution has complied with the appropriate penalties.

_____ _____

14. Interview management to determine if the institution intends to change the composition of its balance sheet to re-qualify as a QTL or DBLA.

_____ _____

15. Determine management's plan for maintaining QTL or DBLA status once regained, stressing the consequences of a second failure.

_____ _____

Exam Date: _____
Prepared By: _____
Reviewed By: _____
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Wkp.Ref.

16. State in the examination report if the institution has not complied with QTL penalties since failure, or if the review uncovers a second failure. Outline the actions the institution needs to take to comply with the applicable penalty provisions.

_____ _____

Exam Date: _____
Prepared By: _____
Reviewed By: _____
Docket #: _____