

IN THE HOUSE OF REPRESENTATIVES

HOUSE BILL NO. 9

BY BUSINESS COMMITTEE

AN ACT

1 RELATING TO LIMITATIONS ON LOANS, INVESTMENTS, AND PRACTICES; AMENDING SEC-
2 TION 26-705, IDAHO CODE, TO DEFINE TERMS, TO REVISE A DEFINITION, TO
3 PROVIDE AN ADDITIONAL ITEM THAT DOES NOT CONSTITUTE A LOAN OR EXTENSION
4 OF CREDIT, TO PROVIDE REQUIREMENTS FOR A BANK ENGAGED IN A DERIVATIVE
5 TRANSACTION, TO REVISE HEADINGS, TO ESTABLISH PROVISIONS RELATING TO
6 EXTENSIONS OF CREDIT AND CREDIT EXPOSURE IN A DERIVATIVE TRANSACTION
7 AND TO MAKE TECHNICAL CORRECTIONS; DECLARING AN EMERGENCY AND PROVIDING
8 RETROACTIVE APPLICATION.
9

10 Be It Enacted by the Legislature of the State of Idaho:

11 SECTION 1. That Section 26-705, Idaho Code, be, and the same is hereby
12 amended to read as follows:

13 26-705. LOANS TO ONE PERSON. (1) The total loans and extensions of
14 credit by a bank to a person outstanding at one (1) time, shall at no time
15 exceed twenty percent (20%) of the capital structure of such bank.

16 (2) "Borrower" means a person who is named as a borrower or debtor in a
17 loan or extension of credit, a counterparty to whom a bank has credit expo-
18 sure in a derivative transaction entered into by the bank, or any other per-
19 son including a drawer, endorser or guarantor, who is deemed to be a borrower
20 under the direct benefit and common enterprise tests set forth in this sec-
21 tion.

22 (3) "Derivative transaction" includes any transaction that is a con-
23 tract, agreement, swap, warrant, note or option that is based, in whole or in
24 part, on the value of, any interest in or any quantitative measure or the oc-
25 currence of any event relating to, one (1) or more commodities, securities,
26 currencies, interest or other rates, indices or other assets.

27 (4) "Loans and extensions of credit" means a bank's direct or indirect
28 advance of funds to or on behalf of a borrower based upon an obligation of the
29 borrower to repay the funds, or repayable from specific property pledged by
30 or on behalf of the borrower, and includes, for the purposes of this section:

31 (a) A contractual commitment to advance funds;

32 (b) A maker or endorser's obligation arising from a bank's discount of
33 commercial paper;

34 (c) A bank's purchase of securities subject to an agreement that the
35 seller shall repurchase the securities at the end of a stated period,
36 but not including a bank's purchase of type I securities, as defined in
37 12 CFR part 1, subject to a repurchase agreement, where the purchasing
38 bank has assured control over or has established its rights to the type I
39 securities as collateral;

40 (d) A bank's purchase of third-party paper subject to an agreement that
41 the seller shall repurchase the paper upon default or at the end of a
42 stated period. The amount of the bank's loan is the total unpaid bal-

1 ance of the paper owned by the bank less any applicable dealer reserves
 2 retained by the bank and held by the bank as collateral security. Where
 3 the seller's obligation to repurchase is limited, the bank's loan is
 4 measured by the total amount of the paper the seller may ultimately be
 5 obligated to repurchase. A bank's purchase of third party paper without
 6 direct or indirect recourse to the seller is not a loan or extension of
 7 credit to the seller;

8 (e) An overdraft, whether or not prearranged, but not an ~~intra-day~~
 9 intraday overdraft for which payment is received before the close of
 10 business of the bank that makes the funds available;

11 (f) The sale of federal funds with a maturity of more than one (1) busi-
 12 ness day, but not federal funds with a maturity of one (1) day or less or
 13 federal funds sold under a continuing contract; and

14 (g) Loans or extensions of credit that have been charged off on the
 15 books of the bank in whole or in part, unless the loan or extension of
 16 credit:

17 (i) Is unenforceable by reason of discharge in bankruptcy;

18 (ii) Is no longer legally enforceable because of expiration of the
 19 statute of limitations or a judicial decision; or

20 (iii) Is no longer legally enforceable for other reasons, provided
 21 that the bank maintains sufficient records to demonstrate that the
 22 loan is unenforceable; and

23 (h) Any credit exposure in a derivative transaction.

24 (35) The following items do not constitute loans or extensions of
 25 credit for purposes of this section:

26 (a) Additional funds advanced for the benefit of a borrower by a bank
 27 for payment of taxes, insurance, utilities, security, and maintenance
 28 and operating expenses necessary to preserve the value of real property
 29 securing the loan, consistent with safe and sound banking practices,
 30 but only if the advance is for the protection of the bank's interest in
 31 the collateral, and provided that such amounts must be treated as an ex-
 32 tension of credit if a new loan or extension of credit is made to the bor-
 33 rower;

34 (b) Accrued and discounted interest on an existing loan or extension of
 35 credit, including interest that has been capitalized from prior notes
 36 and interest that has been advanced under terms and conditions of a loan
 37 agreement;

38 (c) Financed sales of a bank's own assets, including other real estate
 39 owned, if the financing does not put the bank in a worse position than
 40 when the bank held title to the assets;

41 (d) A renewal or restructuring of a loan as a new loan or extension of
 42 credit, following the exercise by a bank of reasonable efforts, consis-
 43 tent with safe and sound banking practices, to bring the loan into con-
 44 formance with the lending limit, unless new funds are advanced by the
 45 bank to the borrower (except as permitted by this section), or a new bor-
 46 rower replaces the original borrower, or unless the director determines
 47 that a renewal or restructuring was undertaken as a means to evade the
 48 bank's lending limit;

49 (e) Amounts paid against uncollected funds in the normal process of
 50 collection; and

1 (f) (i) That portion of a loan or extension of credit sold as a partic-
 2 ipation by a bank on a nonrecourse basis, provided that the partic-
 3 ipation results in a pro rata sharing of credit risk proportion-
 4 ate to the respective interests of the originating and participat-
 5 ing lenders. Where a participation agreement provides that repay-
 6 ment must be applied first to the portions sold, a pro rata shar-
 7 ing shall be deemed to exist only if the agreement also provides
 8 that, in the event of a default or comparable event defined in the
 9 agreement, participants must share in all subsequent repayments
 10 and collections in proportion to their percentage participation
 11 at the time of the occurrence of the event.

12 (ii) When an originating bank funds the entire loan, it must re-
 13 ceive funding from the participants before the close of business
 14 of its next business day. If the participating portions are not
 15 received within that period, then the portions funded shall be
 16 treated as a loan by the originating bank to the borrower. If the
 17 portions so attributed to the borrower exceed the originating
 18 bank's lending limit, the loan may be treated as nonconforming,
 19 rather than a violation, if:

20 1. The originating bank had a valid and unconditional par-
 21 ticipation agreement with a participating bank or banks that
 22 was sufficient to reduce the loan to within the originating
 23 bank's lending limit;

24 2. The participating bank reconfirmed its participation
 25 and the originating bank had no knowledge of any information
 26 that would permit the participant to withhold its participa-
 27 tion; and

28 3. The participation was to be funded by close of business of
 29 the originating bank's next business day; and

30 (g) Intraday credit exposure in a derivative transaction.

31 (46) The following loans or extensions of credit are not subject to the
 32 lending limits of this section:

33 (a) The discount of bills of exchange drawn in good faith against actual
 34 existing values;

35 (b) The discount of bankers' acceptances of other banks;

36 (c) The discount of commercial or business paper actually owned by the
 37 person negotiating the same;

38 (d) The obligations of the United States or general obligations of any
 39 state or of any political subdivision thereof, or obligation issued un-
 40 der authority of the federal farm loan act;

41 (e) Loans made on warehouse receipts and bills of lading, when such
 42 warehouse receipts and bills of lading cover nonperishable commodities
 43 of the marketable value of at least one hundred twenty percent (120%) of
 44 the amount loaned thereon;

45 (f) Loans and extensions of credit to the extent secured or covered by
 46 guaranties, or by commitments or agreements to take over or to purchase,
 47 made by any ~~F~~federal ~~R~~eserve ~~B~~ank or by the United States or any de-
 48 partment, bureau, board, commission, or establishment of the United
 49 States, including any corporation wholly owned directly or indirectly
 50 by the United States; or

1 (g) Loans, including portions thereof, secured by a segregated deposit
2 account in the lending bank, provided a security interest in the deposit
3 has been perfected under applicable law.

4 (~~5~~7) Combination. Loans or extensions of credit to one (1) borrower
5 shall be attributed to another person and each person shall be deemed a bor-
6 rower when proceeds of a loan or extension of credit are to be used for the
7 direct benefit of the other person, to the extent of the proceeds so used, or
8 when a common enterprise is deemed to exist between the persons.

9 (a) Direct benefit. The proceeds of a loan or extension of credit to
10 a borrower shall be deemed to be used for the direct benefit of another
11 person and shall be attributed to the other person when the proceeds, or
12 assets purchased with the proceeds, are transferred to another person,
13 other than in a bona fide arm's length transaction where the proceeds
14 are used to acquire property, goods or services.

15 (b) Common enterprise. A common enterprise shall be deemed to exist and
16 loans to separate borrowers shall be aggregated:

17 (i) When the expected source of repayment for each loan or exten-
18 sion of credit is the same for each borrower and neither borrower
19 has another source of income from which the loan (together with the
20 borrower's other obligations) may be fully repaid. An employer
21 shall not be treated as a source of repayment under this paragraph
22 because of wages and salaries paid to an employee unless the stan-
23 dards of paragraph (b) (ii) of this subsection are met;

24 (ii) When loans or extensions of credit are made:

25 1. To borrowers who are related directly or indirectly
26 through common control, including where one (1) borrower is
27 directly or indirectly controlled by another borrower; and

28 2. Substantial financial interdependence exists between or
29 among the borrowers. Substantial financial interdependence
30 is deemed to exist when fifty percent (50%) or more of one
31 (1) borrower's gross receipts or gross expenditures (on an
32 annual basis) are derived from transactions with the other
33 borrower. Gross receipts and expenditures include gross
34 revenues/expenses, intercompany loans, dividends, capital
35 contributions, and similar receipts or payments;

36 (iii) When separate persons borrow from a bank to acquire a busi-
37 ness enterprise of which those borrowers will own more than fifty
38 percent (50%) of the voting securities or voting interests, in
39 which case a common enterprise is deemed to exist between the bor-
40 rowers for purposes of combining the acquisition loans; or

41 (iv) When the director determines, based upon an evaluation of the
42 facts and circumstances of particular transactions, that a common
43 enterprise exists.

44 (c) Loans to a corporate group.

45 (i) Loans or extensions of credit by a bank to a corporate group
46 may not exceed fifty percent (50%) of the bank's capital and
47 surplus. A corporate group includes a person and all of its sub-
48 sidiaries. For purposes of this paragraph, a corporation or a
49 limited liability company is a subsidiary of a person if the person
50 owns or beneficially owns directly or indirectly more than fifty

1 percent (50%) of the voting securities or voting interests of the
2 corporation or company.

3 (ii) Except as provided in paragraph (c) (i) of this subsection,
4 loans or extensions of credit to a person and its subsidiary, or to
5 different subsidiaries of a person, are not combined unless either
6 the direct benefit or the common enterprise test is met.

7 (d) Loans to partnerships, joint ventures, and associations.

8 (i) Partnership loans. Loans or extensions of credit to a part-
9 nership, joint venture or association are deemed to be loans or ex-
10 tensions of credit to each member of the partnership, joint ven-
11 ture or association. This rule does not apply to limited partners
12 in limited partnerships or to members of joint ventures or asso-
13 ciations if the partners or members, by the terms of the partner-
14 ship or membership agreement, are not held generally liable for
15 the debts or actions of the partnership, joint venture or associa-
16 tion, and those provisions are valid under applicable law.

17 (ii) Loans to partners.

18 1. Loans or extensions of credit to members of a partner-
19 ship, joint venture or association are not attributed to
20 the partnership, joint venture or association unless either
21 the direct benefit or the common enterprise test is met.
22 Both the direct benefit and common enterprise tests are met
23 between a member of a partnership, joint venture or associ-
24 ation and such partnership, joint venture or association,
25 when loans or extensions of credit are made to the member to
26 purchase an interest in the partnership, joint venture or
27 association.

28 2. Loans or extensions of credit to members of a partner-
29 ship, joint venture or association are not attributed to
30 other members of the partnership, joint venture or associa-
31 tion unless either the direct benefit or common enterprise
32 test is met.

33 (e) Loans to foreign governments and their agencies and instrumentali-
34 ties.

35 (i) Aggregation. Loans and extensions of credit to foreign gov-
36 ernments and their agencies and instrumentalities shall be aggre-
37 gated with one another only if the loans or extensions of credit
38 fail to meet either the means test or the purpose test at the time
39 the loan or extension of credit is made.

40 1. The means test is satisfied if the borrower has resources
41 or revenue of its own sufficient to service its debt obli-
42 gations. If the government's support (excluding guarantees
43 by a central government of the borrower's debt) exceeds the
44 borrower's annual revenues from other sources, it shall be
45 presumed that the means test has not been satisfied.

46 2. The purpose test is satisfied if the purpose of the loan
47 or extension of credit is consistent with the purposes of the
48 borrower's general business.

1 (ii) Documentation. In order to show that the means and purpose
 2 tests have been satisfied, a bank must, at a minimum, retain in its
 3 files the following items:

- 4 1. A statement (accompanied by supporting documentation)
 5 describing the legal status and the degree of financial and
 6 operational autonomy of the borrowing entity;
- 7 2. Financial statements for the borrowing entity for a mini-
 8 mum of three (3) years prior to the date the loan or extension
 9 of credit was made or for each year that the borrowing entity
 10 has been in existence, if less than three (3) years;
- 11 3. Financial statements for each year the loan or extension
 12 of credit is outstanding;
- 13 4. The bank's assessment of the borrower's means of ser-
 14 vicing the loan or extension of credit, including specific
 15 reasons in support of that assessment. The assessment shall
 16 include an analysis of the borrower's financial history, its
 17 present and projected economic and financial performance,
 18 and the significance of any financial support provided to
 19 the borrower by third parties, including the borrower's cen-
 20 tral government; and
- 21 5. A loan agreement or other written statement from the
 22 borrower that clearly describes the purpose of the loan or
 23 extension of credit. The written representation will ordi-
 24 narily constitute sufficient evidence that the purpose test
 25 has been satisfied. However, when, at the time the funds are
 26 disbursed, the bank knows or has reason to know of other in-
 27 formation suggesting that the borrower will use the proceeds
 28 in a manner inconsistent with the written representation,
 29 it may not, without further inquiry, accept the representa-
 30 tion.

31 (8) A bank shall evaluate the credit exposure in a derivative transac-
 32 tion in accordance with a methodology approved by any federal bank supervi-
 33 sory agency. In each type of derivative transaction a bank engages in, a bank
 34 shall use the same credit exposure methodology in all derivative transac-
 35 tions of that type.

36 (69) Lending limit cCalculation. For purposes of determining compli-
 37 ance with this section, a bank shall determine its lending limit as of the
 38 last day of the preceding calendar quarter. A bank's lending limit calcu-
 39 lated in accordance with this section shall be effective on the date that the
 40 limit is to be calculated. If the director determines for safety and sound-
 41 ness reasons that a bank should calculate its lending limit more frequently
 42 than required by this subsection, the director may provide written notice to
 43 the bank directing the bank to calculate its lending limit at a more frequent
 44 interval, and the bank shall thereafter calculate its lending limit at that
 45 interval until further notice from the director.

46 (710) Nonconforming loans and extensions of credit. A loan or extension
 47 of credit, within a bank's legal lending limit when made, shall not be deemed
 48 a violation but shall be treated as nonconforming if the loan or extension of
 49 credit is no longer in conformity with the bank's lending limit because:

1 (a) The bank's capital has declined, borrowers have subsequently
2 merged or formed a common enterprise, lenders have merged, or the lend-
3 ing limit or capital rules have changed. A bank must use reasonable ef-
4 forts to bring a loan or extension of credit that is nonconforming under
5 this subsection into conformity with the bank's lending limit unless to
6 do so would be inconsistent with safe and sound banking practices.

7 (b) Collateral securing the loan or extension of credit to satisfy the
8 requirements of a lending limit exception has declined in value. A bank
9 must bring a loan or extension of credit that is nonconforming under
10 this subsection into conformity with the bank's lending limit within
11 thirty (30) calendar days, except when judicial proceedings, regula-
12 tory actions or other extraordinary circumstances beyond the bank's
13 control prevent the bank from taking action.

14 (c) In the case of credit exposure in a derivative transaction, the
15 credit exposure increases after execution of the transaction. A bank
16 must use reasonable efforts to bring a derivative transaction that is
17 nonconforming under this subsection into conformity with the bank's
18 lending limit unless to do so would be inconsistent with safe and sound
19 banking practices.

20 (§11) When in the judgment of the director the loans and extensions of
21 credit to any person, or the combined loans and extensions of credit to any
22 corporation and one (1) or more of its stockholders are excessive, he shall
23 require the reduction thereof to such limits and within such time as he shall
24 prescribe.

25 Provided, further, that the director may compel the reduction of any
26 loan or extension of credit which shall in his judgment appear excessive or
27 dangerous.

28 SECTION 2. An emergency existing therefor, which emergency is hereby
29 declared to exist, this act shall be in full force and effect on and after its
30 passage and approval, and retroactively to January 21, 2013.