



Office of Thrift Supervision
Department of the Treasury

Director

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April 3, 1997

MEMORANDUM FOR: Chief Executive Officers

FROM: Nicolas P. Retsinas *Nicolas P. Retsinas*
Director

SUBJECT: Thrift Holding Company Background Paper

We have received a number of recent inquiries about thrift holding companies — their evolution, various forms and authorized activities, prevalence within the thrift industry, and the major statutory, regulatory and supervisory controls under which they operate.

Because of the holding company issues that have been raised in connection with the financial modernization legislation now being considered by Congress, we are attempting to compile background information to assist in the understanding of these issues. Attached is a summary, entitled *Holding Companies in the Thrift Industry*, which represents initial efforts. We believe that this background paper will be useful in the continuing deliberations on the relationship of banking and commerce.

We recognize, of course, that the paper will not answer every question. Indeed we expect that it will inspire further questions. Our staff is presently gathering additional information from examination reports and other sources, which we will be happy to share as it becomes available. Meanwhile, I am forwarding a copy of our summary for your information.

Enclosure

Office of Thrift Supervision

Department of the Treasury



Holding Companies

in the

Thrift Industry

Background Paper

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BACKGROUND PAPER HOLDING COMPANIES IN THE THRIFT INDUSTRY

Executive Summary

As discussions evolve on the relationship between banking and commerce, it may be helpful to consider the experience of thrift holding companies which, unlike bank holding companies, have historically been given broad powers.

The range of permissible activities of thrift holding companies is governed by the Savings and Loan Holding Company Act of 1967. Under this act, holding companies that own a single thrift are generally permitted to engage in any activities that do not threaten the safety and soundness of their subsidiary thrift.

Today, the Office of Thrift Supervision regulates over 1300 thrifts; 651 of those thrifts are controlled by holding companies. These 651 thrifts hold \$632 billion in assets, representing 82% of all thrift assets.

The roster of thrift holding companies includes many small holding companies engaged exclusively in activities closely related to owning and managing a subsidiary thrift. It also includes multi-billion dollar companies engaged in diverse financial, commercial and industrial activities. In between are numerous medium-size companies that engage in a few select diversified activities.

Regardless of the scope of their activities, all thrift holding companies must comply with a variety of strict statutory and regulatory requirements and restrictions. They must also undergo regular examinations by the Office of Thrift Supervision. These safeguards are intended to address the concerns that motivated passage of the Bank Holding Company Act and the Glass-Steagall Act.

In the attached paper, the Office of Thrift Supervision attempts to share its experience as the regulator of thrift holding companies. The paper:

- provides some historical context to the evolution of thrift holding company powers;
- identifies the major statutory, regulatory and supervisory controls over thrift holding companies;
- describes the various forms of thrift holding companies and their authorized activities;
- quantifies the extent of holding company involvement in the thrift industry; and
- offers some representative examples of diverse thrift holding companies.

The Office of Thrift Supervision, as the primary federal regulator of the thrift industry, remains mindful of the problems that plagued the industry during the 1980s. There certainly have been occasions when thrift holding companies have violated laws or regulations or otherwise engaged in unsafe and unsound practices that required enforcement action. We have not, however, detected any systemic problems that arise from the scope of permissible activities of thrift holding companies and their affiliates.

I. Introduction

- The thrift industry regulated by the Office of Thrift Supervision (“OTS”) is comprised of over 1300 institutions with assets of \$769 billion.
 - 536 are mutual institutions, which have neither stockholders nor holding companies.
 - 800 are stock institutions.
 - The vast majority of the thrift industry’s assets is held by stock institutions, which control \$689 billion or 90% of the industry’s assets.
- Within the universe of stock institutions, 651 thrifts are controlled by holding companies.
- Thrift holding companies may be either stock or mutual, may control a single thrift (a unitary thrift holding company) or several thrifts (a multiple thrift holding company).
- The range of permissible activities for a thrift holding company generally depends on the number of thrifts that the company controls and the company’s form of ownership.
 - Generally, stock holding companies controlling only one thrift (unitary thrift holding companies) are permitted to engage in a much broader range of activities than mutual thrift holding companies or those controlling multiple thrifts.
- All thrift holding companies are governed by the same restrictions on interactions between the thrift and its holding company.
 - Restrictions are designed to protect the thrift from being exploited by its holding company or its holding company affiliates.

II. Background/Historical Perspective

- **Affiliations with Securities Firms**

- 1933—Glass-Steagall Act—imposed stringent restrictions on affiliations (and other relationships) between banks and securities or investment banking firms.
 - Most of those restrictions were not applicable to thrifts.

- **Bank Holding Companies**

- 1956—Bank Holding Company Act—restricted the scope of permissible activities of multiple bank holding companies and their subsidiaries to those that are “closely related” to banking.
- 1970—Bank Holding Company Act Amendments—extended to unitary bank holding companies the same activities restrictions that are imposed on multiple bank holding companies.

- **Thrift Holding Companies**

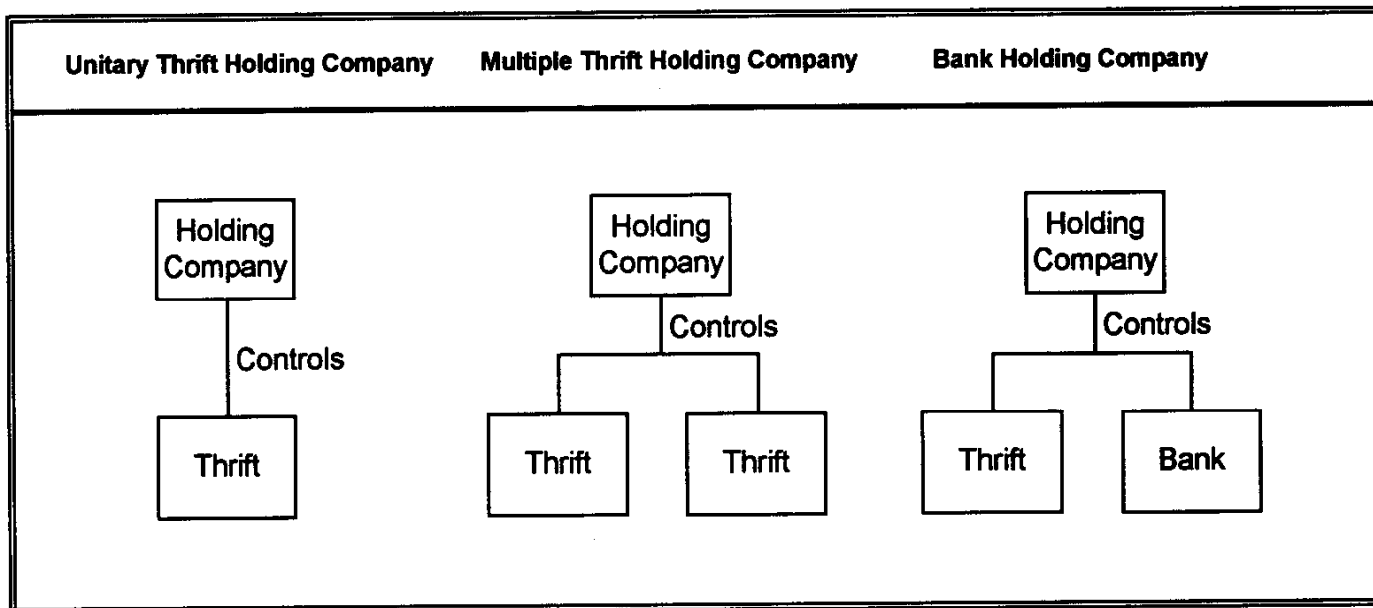
- 1959—Spence Act—halted the growth of multiple thrift holding companies until Congress had the opportunity to determine whether additional regulation was needed.
 - Imposed moratorium on further acquisitions of thrifts by existing thrift holding companies.
 - Prohibited newly-formed thrift holding companies from acquiring more than one thrift.

- **1967—Savings and Loan Holding Company Act Amendments—terminated moratorium on creation/expansion of multiple thrift holding companies.**
 - **Prohibited multiple thrift holding companies from engaging in commercial and industrial enterprises, as well as certain financial activities such as underwriting insurance or securities.**
 - **Continued to permit unitary thrift holding companies to engage in any activities that were not detrimental to the safety and soundness of the thrift.**
- **1987—Competitive Equality Banking Act—permitted mutual thrifts to create mutual holding companies and sell minority interest in newly created stock thrifts.**
 - **Added specific requirement that thrift subsidiaries of unitary thrift holding companies must meet the Qualified Thrift Lender test for such companies to retain their broad powers.**

III. Range of Activities

- The Savings and Loan Holding Company Act stipulates the permissible range of activities for thrift holding companies, generally depending on the number of thrifts they control.
- In order to be a qualified thrift lender (QTL), a thrift must maintain a specific amount of assets in defined qualified thrift investments, primarily housing and consumer related. Provided that its thrift meets the QTL test, a unitary thrift holding company (one that controls only one thrift) may engage in any commercial or industrial activity as long as the activity does not:
 - threaten the safety and soundness of its subsidiary thrift; or
 - enable the thrift to evade applicable laws and regulations.
- A multiple thrift holding company (one that controls more than one thrift), or a mutual thrift holding company, may generally engage in those activities authorized for bank holding companies by the Bank Holding Company Act. Limited additional activities are permitted, the most significant being:
 - real estate acquisition, development, management, sale and rental; and
 - for multiple thrift holding companies, insurance agency without geographic restriction.
- A bank holding company (one that controls both a bank(s) and a thrift(s)) may engage only in those activities authorized for bank holding companies by the Bank Holding Company Act.

BASIC TYPES OF HOLDING COMPANIES OWNING THRIFTS



IV. Restrictions on Interactions

- **All thrift holding companies and their subsidiary thrifts must comply with strict statutory and regulatory restrictions on the scope and manner of their interactions. These restrictions, which are designed to protect the thrift from being exploited by the holding company or its affiliates, include:**
 - **Except for existing bank holding companies, companies must obtain OTS approval before acquiring a thrift.**
 - **Thrifts are generally prohibited from:**
 - **Purchasing securities issued or being underwritten by its holding company or affiliates;**
 - **Making loans to affiliates engaged in activities that are impermissible for bank holding companies;**
 - **Requiring that a customer that obtains a loan or other service from the thrift must also obtain some other service from the holding company or other affiliate (subject to certain narrow exceptions); and**
 - **Agreeing, stating or suggesting that the thrift is in any way responsible for the obligations of its holding company or affiliates.**
 - **Certain transactions with affiliates:**
 - **Are limited to 10 percent of the thrift's capital with any one affiliate;**
 - **Are limited to 20 percent of the thrift's capital with all affiliates in the aggregate; and**
 - **Must be conducted on arm's length terms.**
 - **Thrifts are required to notify the OTS in advance of paying any dividend to their holding companies. Thrifts that fail to maintain adequate capital are prohibited from making such payments. Dividend restrictions may be placed on other thrifts for safety and soundness reasons.**

V. Advantages to Thrifts

- **Affiliations between thrifts and companies engaged in financial, commercial and industrial activities have had three primary benefits:**
 - **Financial advantages - thrift holding companies that engage in diverse lines of business often have substantially greater financial resources than non-diversified companies:**
 - **Enhanced access to capital markets.**
 - **Diversification of liquidity sources.**
 - **Lowered costs of borrowing.**
 - **Managerial advantages - thrift holding companies can contribute business and managerial talent and expertise to the thrift:**
 - **Particularly true when thrift holding companies have significant experience in a broad array of financial services activities.**
 - **Promotes operating efficiencies through economies of scale.**
 - **Customer service advantages - customers benefit when they are able to do business with an integrated financial services company.**

VI. Supervision of Thrift Holding Companies

- Thrift holding companies (controlling only thrifts) are regulated by the Office of Thrift Supervision.
- Bank holding companies (controlling both banks and thrifts) are now regulated by the Federal Reserve Board ("FRB"). (Prior to October 1996, they were jointly regulated by OTS and the FRB).
- Thrift holding companies must undergo regular OTS examinations, which are usually concurrent with the examination of their subsidiary thrift.
 - OTS examinations of holding companies focus on:
 - Transactions between the thrift, its holding company, and the company's other affiliates;
 - Funds flowing from the thrift to its holding company and affiliates (e.g. dividends and tax payments);
 - The quality of holding company management and the extent of management's participation in and oversight of thrift decisions; and
 - The present or potential financial impact or other risks, if any, of the holding company's and its affiliates' operations on the thrift.
 - The complexity of the holding company's corporate structure, and the level of its interaction with the thrift, dictate the scope of OTS examinations.
- Thrift holding companies are also required to submit periodic reports on their activities to the OTS.
- Certain activities of multiple thrift holding companies require prior notification to, or approval by, the OTS.
- Unitary thrift holding companies are not required to obtain OTS approval to undertake new non-banking activities.

VII. Current Holding Company Ownership of Thrifts

- As of December 31, 1996, there were 875 holding companies that owned 651 OTS-regulated thrifts, or 49 percent of all OTS-regulated thrifts.
 - The number of holding companies exceeds the number of thrifts owned by holding companies because a thrift may be owned by several companies. For example, thrifts may be owned by family trusts where separate trusts, and hence, holding companies, are formed for each member of the family.
 - The chart on Page 11 illustrates the basic ownership structures for thrift holding companies.
- Thrifts owned by holding companies held aggregate assets of approximately \$632 billion as of December 31, 1996 - 82 percent of total industry assets.
 - Within this universe, there are:
 - 515 thrifts, with \$467 billion in assets, controlled by unitary thrift holding companies;
 - 39 thrifts, with \$94 billion in assets, controlled by multiple thrift holding companies;
 - 97 thrifts, with \$71 billion in assets, controlled by bank holding companies.

- The involvement of holding companies in the thrift industry is a dynamic process, as companies move into and out of the industry regularly.

- As the data below indicate, a substantial number of holding companies enter or leave the thrift industry each year:

	Entries	Exits
• 1996	168	162
• 1995	201	157
• 1994	192	131

- As illustrated, the total number of holding companies entering or leaving the thrift industry in 1996 accounted for over 38% of the total number of holding companies at the end of the year.
- Thus, the characteristics of today's holding companies, the activities in which they engage, and the statistics presented in this paper, are subject to change over time.

BASIC THRIFT HOLDING COMPANY STRUCTURES

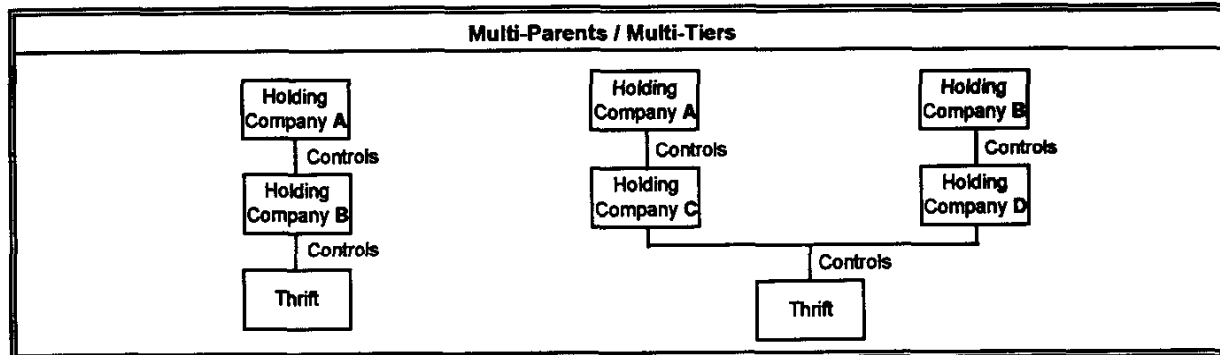
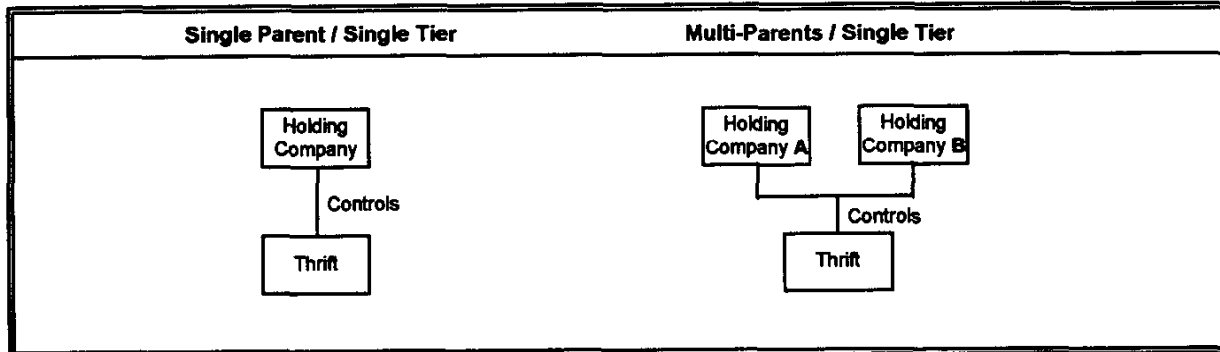


TABLE 1**Holding Companies Owning OTS Regulated Thrifts**
(Dollars in Billions)

<u>Holding Company Type</u>	<u>Number</u>	<u>%</u>	<u>Number of Thrifts Owned</u>	<u>Thrift Assets</u>
OTS-Regulated HCs:				
Unitary	704	80%	515	\$467
Multiple	<u>40</u>	<u>5</u>	<u>39</u>	<u>94</u>
	<u>744</u>	<u>85%</u>	<u>554</u>	<u>\$561</u>
Bank HCs Owning a Thrift	<u>131</u>	<u>15%</u>	<u>97</u>	<u>\$ 71</u>
Total HCs & Thrifts in HCs	875	100%	651	\$632
Independent Thrifts			685	\$137
Total Thrifts			1,336	\$769

VIII. OTS Experience with Large Commercial Firms Owning Thrifts

- Most large commercial firms purchased thrifts in the early 1980s, or the late 1980s/early 1990s.
 - During those periods, many thrifts were suffering losses. Some thrifts may have been purchased by commercial firms in order to capture the thrifts' net operating loss carryforwards or other tax credits.
 - Some thrifts may have been purchased by large commercial firms because thrifts were "cheap". Commercial firms were able to enter the thrift industry inexpensively since high interest rates, asset quality problems, and losses, depressed some thrifts' stock.
 - Some commercial firms purchased failed thrifts from the FSLIC.
- More recent thrift purchases by commercial firms have involved healthy thrifts.
 - It appears these thrifts were purchased because they offer some "synergy" between the thrifts' customers and the customers of the commercial firm. Examples include offering the firm's financial products to the thrift's customers; or allowing thrift customers to conduct financial transactions through the firm's existing distribution systems, such as grocery stores.
- Most large commercial firms held their thrifts for a period of between two and five years.
- The majority of large commercial firms purchased smaller thrifts – few had over \$1 billion in assets.
- Nearly all thrifts owned by large commercial firms either shrank in asset size or remained approximately the same size.
 - A notable exception is Temple-Inland, Inc. which has purchased several thrifts over the past ten years. Total assets of thrifts held by Temple-Inland, Inc. have increased from \$92 million in 1987, to \$9 billion as of the end of 1996.

IX. Examples of Large Commercial Firms Owning Thrifts

- Over the past ten years, several very large commercial firms have owned OTS-regulated thrifts. Examples of such firms that previously owned thrifts are:
 - Ford Motor Company - the second largest auto manufacturer in the U.S. Also engages in vehicle leasing and rental, and manufacturing electronic equipment.
 - Sears Roebuck and Company - the world's second largest retailer. Operates full-line department and specialty stores.
 - ITT Corporation - one of the world's leading hotel, gaming, entertainment and information services companies.
 - Weyerhaeuser Company - the world's largest private owner of softwood timber, producing wood products (lumber, plywood, particle board) and paper products (pulp, newsprint, containers).
- Examples of large commercial firms that currently own thrifts are:
 - Temple Inland, Inc. - has major interests in paper, packaging, building products, and financial services. Owns and leases 1.9 million acres of timberland in TX, LA, AL and GA. Financial services include thrift activities, mortgage banking, real estate development, and insurance.
 - Pulte Corporation - One of the nation's largest builders of single-family homes and developers of residential subdivisions. Operates in 24 states and 39 markets nationwide. Also engages in thrift ownership and mortgage banking.
 - Dean Witter, Discover & Company - a diversified financial services firm with two main businesses: credit services (Discover card), and securities (Dean Witter brokerage). Recently announced a merger with Morgan Stanley which would create the largest securities firm in the world.

X. Examples of Small Commercial Firms Owning Thrifts

- Most thrift holding companies are smaller, less well-known firms.
- Some examples include:
 - *Hy-Vee, Inc* - an integrated food company with over 200 food, drug and convenience stores located in seven states.
 - *Club Corporation International* - operates country clubs, athletic clubs, resorts and golf facilities.
 - *Ohio Savings Financial Corporation* - owns an equity interest in an automobile rental company.

XI. Non-Banking Activities of Thrift Holding Companies

- In total, about 29 percent of OTS-regulated thrift assets are held by thrifts in holding companies with some non-banking related activities.
- 39 thrifts, with assets of \$94 billion, are controlled by multiple thrift holding companies. In addition to activities permitted under the Bank Holding Company Act, these companies may engage in specified activities, including:
 - Acquisition, development, management, sale and rental of real estate.
 - 2 multiple thrift holding companies are actively engaged in one or more of the real estate-related activities described above. The 4 thrifts in these multiple thrift holding companies hold \$24 billion in assets – about 3 percent of total industry assets.
- There are 515 thrifts, with assets of \$467 billion, controlled by unitary thrift holding companies. These companies may engage in unrestricted non-banking, commercial or industrial activities.
 - Currently, there are approximately 102 unitary thrift holding companies, owning 73 thrifts, that actively engage in non-banking activities.
 - The 73 thrifts in these unitary thrift holding companies hold approximately \$196 billion in assets – about 26 percent of the total industry.
 - The major types of non-banking activities that these unitary thrift holding companies currently pursue include:
 - Real estate development, investment and management activities (51 holding companies);
 - Insurance sales and underwriting (27 holding companies).
 - Most other non-banking activities are consumer oriented but there are a few exceptions (e.g., manufacturing, wholesale goods, energy and exploration.)

TABLE 2

Thrift Holding Companies With Non-Banking Related Activities
(Dollars in Billions)

<u>Holding Company Type</u>	<u>Number</u>	<u>Number of Thrifts Owned</u>	<u>Thrift Assets</u>
Unitary	102	73 ¹	\$196
Multiple	2	4	24
Total	104	77	\$220

¹ includes three thrifts that are not regulated by the OTS; their holding companies are regulated by the OTS.

NON-BANKING ACTIVITIES OF UNITARY THRIFT HOLDING COMPANIES

Real Estate Development/Investment/Management/Sales	51	Car Rental	1
Insurance Sales & Underwriting/Life/Casualty/Property	27	Dairy Farming	1
Equity and Fixed Income Investment	12	Data Processing	1
Broker/Dealer	8	Electric Utility	1
Hotel Owner/Operator	4	Energy Exploration and Production	1
Mutual Fund Management	4	Entertainment and Leisure	1
Pension Fund Management	4	Fast Food Operations	1
Financial Asset Management	3	Food Bulk Sales	1
Manufacturing	3	Fuel Hauling	1
Telecommunications	3	Grocery Stores	1
Travel Agency	3	Management Services	1
Auto Sales	2	Movie Theaters	1
Canadian Credit Union Leagues	2	Pharmaceuticals	1
Consumer Goods	2	Software	1
Convenience Stores	2	Title Abstract Company	1
Broker Servicer	1	Transportation	1
Country Club Development & Management	1	Waste Collection and Processing	1

There are 102 unitary thrift holding companies included in the above count.
The same holding company may be counted for more than one activity.

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