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covered transaction for a member bank for as long as the member bank holds the asset.

(2) *Asset purchases by a member bank from a nonaffiliate in contemplation of the nonaffiliate becoming an affiliate of the member bank.* If a member bank purchases an asset from a nonaffiliate in contemplation of the nonaffiliate becoming an affiliate of the member bank, the asset purchase becomes a covered transaction at the time that the nonaffiliate becomes an affiliate of the member bank. In addition, the member bank must ensure that the aggregate amount of the member bank's covered transactions (including any such transaction with the nonaffiliate) would not exceed the quantitative limits of § 223.11 or 223.12 at the time the nonaffiliate becomes an affiliate.

(c) *Examples.* The following are examples of how to value a member bank's purchase of an asset from an affiliate.

(1) *Cash purchase of assets.* A member bank purchases a pool of loans from an affiliate for \$10 million. The member bank initially must value the covered transaction at \$10 million. Going forward, if the borrowers repay \$6 million of the principal amount of the loans, the member bank may value the covered transaction at \$4 million.

(2) *Purchase of assets through an assumption of liabilities.* An affiliate of a member bank contributes real property with a fair market value of \$200,000 to the member bank. The member bank pays the affiliate no cash for the property, but assumes a \$50,000 mortgage on the property. The member bank has engaged in a covered transaction with the affiliate and initially must value the transaction at \$50,000. Going forward, if the member bank retains the real property but pays off the mortgage, the member bank must continue to value the covered transaction at \$50,000. If the member bank, however, sells the real property, the transaction ceases to be a covered transaction at the time of the sale (regardless of the status of the mortgage).

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§ 223.23 What valuation and timing principles apply to purchases of and investments in securities issued by an affiliate?

(a) *Valuation.* (1) *In general.* Except as provided in paragraph (b) of § 223.32 with respect to financial subsidiaries, a member bank's purchase of or investment in a security issued by an affiliate must be valued at the greater of:

(i) The total amount of consideration given (including liabilities assumed) by the member bank in exchange for the security, reduced to reflect amortization of the security to the extent consistent with GAAP; or

(ii) The carrying value of the security.

(2) *Examples.* The following are examples of how to value a member bank's purchase of or investment in securities issued by an affiliate (other than a financial subsidiary of the member bank).

(i) *Purchase of the debt securities of an affiliate.* The parent holding company of a member bank owns 100 percent of the shares of a mortgage company. The member bank purchases debt securities issued by the mortgage company for \$600. The initial carrying value of the securities is \$600. The member bank initially must value the investment at \$600.

(ii) *Purchase of the shares of an affiliate.* The parent holding company of a member bank owns 51 percent of the shares of a mortgage company. The member bank purchases an additional 30 percent of the shares of the mortgage company from a third party for \$100. The initial carrying value of the shares is \$100. The member bank initially must value the investment at \$100. Going forward, if the member bank's carrying value of the shares declines to \$40, the member bank must continue to value the investment at \$100.

(iii) *Contribution of the shares of an affiliate.* The parent holding company of a member bank owns 100 percent of the shares of a mortgage company and contributes 30 percent of the shares to the member bank. The member bank gives no consideration in exchange for the shares. If the initial carrying value of the shares is \$300, then the member

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bank initially must value the investment at \$300. Going forward, if the member bank's carrying value of the shares increases to \$500, the member bank must value the investment at \$500.

(b) *Timing.* (1) *In general.* A purchase of or investment in a security issued by an affiliate remains a covered transaction for a member bank for as long as the member bank holds the security.

(2) *A member bank's purchase of or investment in a security issued by a nonaffiliate that becomes an affiliate of the member bank.* A member bank's purchase of or investment in a security issued by a nonaffiliate that becomes an affiliate of the member bank must be treated according to the same transition rules that apply to credit transactions described in paragraph (b)(2) of § 223.21.

§ 223.24 What valuation principles apply to extensions of credit secured by affiliate securities?

(a) *Valuation of extensions of credit secured exclusively by affiliate securities.* An extension of credit by a member bank to a nonaffiliate secured exclusively by securities issued by an affiliate of the member bank must be valued at the lesser of:

(1) The total value of the extension of credit; or

(2) The fair market value of the securities issued by an affiliate that are pledged as collateral, if the member bank verifies that such securities meet the market quotation standard contained in paragraph (e) of § 223.42 or the standards set forth in paragraphs (f)(1) and (5) of § 223.42.

(b) *Valuation of extensions of credit secured by affiliate securities and other collateral.* An extension of credit by a member bank to a nonaffiliate secured in part by securities issued by an affiliate of the member bank and in part by nonaffiliate collateral must be valued at the lesser of:

(1) The total value of the extension of credit less the fair market value of the nonaffiliate collateral; or

(2) The fair market value of the securities issued by an affiliate that are pledged as collateral, if the member bank verifies that such securities meet the market quotation standard con-

tained in paragraph (e) of § 223.42 or the standards set forth in paragraphs (f)(1) and (5) of § 223.42.

(c) *Exclusion of eligible affiliated mutual fund securities.* (1) *The exclusion.* Eligible affiliated mutual fund securities are not considered to be securities issued by an affiliate, and are instead considered to be nonaffiliate collateral, for purposes of paragraphs (a) and (b) of this section, unless the member bank knows or has reason to know that the proceeds of the extension of credit will be used to purchase the eligible affiliated mutual fund securities collateral or will otherwise be used for the benefit of or transferred to an affiliate of the member bank.

(2) *Definition.* "Eligible affiliated mutual fund securities" with respect to a member bank are securities issued by an affiliate of the member bank that is an open-end investment company registered with the Securities and Exchange Commission under the Investment Company Act of 1940 (15 U.S.C. 80a-1 *et seq.*), if:

(i) The securities issued by the investment company:

(A) Meet the market quotation standard contained in paragraph (e) of § 223.42;

(B) Meet the standards set forth in paragraphs (f)(1) and (5) of § 223.42; or

(C) Have closing prices that are made public through a mutual fund "supermarket" website maintained by an unaffiliated securities broker-dealer or mutual fund distributor; and

(ii) The member bank and its affiliates do not own or control in the aggregate more than 5 percent of any class of voting securities or of the equity capital of the investment company (excluding securities held by the member bank or an affiliate in good faith in a fiduciary capacity, unless the member bank or affiliate holds the securities for the benefit of the member bank or affiliate, or the shareholders, employees, or subsidiaries of the member bank or affiliate).

(3) *Example.* A member bank proposes to lend \$100 to a nonaffiliate secured exclusively by eligible affiliated mutual fund securities. The member bank knows that the nonaffiliate intends to use all the loan proceeds to purchase