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Flagstar Bank, FSB

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General Comment

See attached file.

Attachments

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November 19, 2018

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street SE, Suite 3E-218
Washington, DC 20219

RE: Docket ID OCC-2018-0020, Covered Savings Associations

To Whom It May Concern:

Flagstar Bank, FSB (the "Bank") welcomes the opportunity to comment on this notice of proposed rulemaking ("NPR")[1] intended to provide federal savings associations ("FSAs") with much-needed flexibility to adapt to new economic conditions and business environments without changing their charters. We appreciate the efforts of the Office of the Comptroller of the Currency ("OCC") and its staff in developing the proposal, and we generally support the approach taken in the NPR. We do believe, however, that the NPR could be further refined to ease the implementation burden and reduce uncertainty regarding certain aspects of the proposed regulatory framework for covered savings associations ("CSAs"), including with respect to the potential impact of CSA status under other banking laws and regulations.

I. Background

Chartered in 1987, the Bank is a full-service, federally-chartered savings bank headquartered in Troy, Michigan. The Bank is the primary operating unit of Flagstar Bancorp, Inc. (combined, "Flagstar"), a savings and loan holding company ("SLHC") with total assets of approximately $$18.7 billion. The Bank conducts business primarily in Michigan and California through its 108 branch footprint and is a leading national originator of residential mortgage loans. Flagstar is a top 5 national bank mortgage originator and top 10 GNMA/FHA/VA lender, providing home loans through a wholesale network of brokers and correspondents in all 50 states as well as 81 retail locations in 27 states. Flagstar is also a leading servicer of mortgage loans, handling payments and record keeping for $136 billion of home loans representing nearly 620,000 borrowers.

II. Summary

In May 2018, Congress passed the Economic Growth, Regulatory Relief, and Consumer Protection Act (the "Act") to "promote economic growth, provide tailored regulatory relief, and enhance consumer protections." Section 206 of the Act amended the Home Owners' Loan Act to create an option for certain FSAs to elect to be CSAs subject to the same rights, privileges, duties, restrictions, conditions, and limitations as apply to national banks. Section 206 instructed the OCC to establish "streamlined standards and procedures that clearly identify required documentation and timelines" for FSAs to make the election and "clarify requirements for the treatment of [CSAs], including provisions of law that apply to [CSAs]."[2] The Bank acknowledges that in drafting the NPR, the OCC has broadly adhered to Congress' intent and instructions.

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[1] *Covered Savings Associations*, 83 Fed. Reg. 47,101 (proposed Sept. 18, 2018).

[2] *Economic Growth, Regulatory Relief, and Consumer Protection Act*, Pub. L. No. 115-174 § 206, 132 Stat. 1,296, 1,310-11 (2018).

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Part III of this comment letter addresses three aspects of the NPR that we believe should be revised to reduce the regulatory burden on electing FSAs and CSAs without undermining any policy objective or supervisory interest reflected in the Act or the NPR.[3] These items are: (i) the proposed treatment of existing service corporation investments; (ii) the proposed framework options for applying national bank rules to CSAs; and (iii) the proposed branch and agency identification requirement in the election procedures.

Part IV of this comment letter addresses three issues that were not raised in the NPR, but which we believe the OCC should address contemporaneously with the promulgation of a final CSA rule, because these issues involve significant uncertainties regarding the interaction between the CSA regulatory framework and other banking laws and regulations. Specifically, we address: (i) the potential impact of CSA status on SLHCs; (ii) the potential applicability of interstate merger restrictions to CSAs; and (iii) the need for clarification regarding CSA membership in the Federal Reserve System.

III. Recommendations Regarding the Proposed CSA Regulation

A. Proposed Treatment of Service Corporation Investments

The NPR could require CSAs to expend unnecessary resources re-characterizing investments in certain "service corporations" that engage solely in activities that are permissible for national banks. Specifically, section 101.5(a) of the NPR would require a CSA to divest, conform, or discontinue a nonconforming subsidiary, asset, or activity at the earliest time that prudent judgment dictates but not later than two years after the effective date of the election to be a CSA. Among other things, this would require CSAs to terminate, restructure, or re-characterize investments held under service corporation authority, because national banks (unlike FSAs) do not have the legal authority to own interests in service corporations.[4]

As the OCC is aware, while service corporations are permitted to engage in certain activities that national banks are not authorized to engage in directly (or not authorized to engage in to the same extent as service corporations), many FSAs, including the Bank, operate service corporations that engage solely in activities that are permissible for national banks. Such FSAs could be required under the NPR to make filings with the OCC to re-characterize their existing service corporation investments under analogous national bank investment authorities (e.g., as operating subsidiaries or other equity investments). Further, FSAs may need to review, and potentially revise, organizational and investment documentation associated with service corporation investments to reflect reliance on national bank investment authorities. In situations where the activities of a service corporation are plainly permissible for both FSAs and national banks to conduct, either through a subsidiary or through some other form of non-controlled equity investments, these kinds of procedural burdens would, in our view, be unwarranted and inconsistent with the statutory requirement to adopt "streamlined standards and procedures to govern the CSA election process." The OCC appears to have recognized this in its commentary to the NPR, noting that a potential alternative approach to this re-characterization process would be for the OCC to authorize CSAs to continue to operate service corporations that are engaged solely in activities that would be permissible for a national bank.[5] We urge the OCC to adopt this alternative

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[3] The NPR would condition eligibility to elect CSA status on whether a FSA is an "eligible savings association", but also requests comment on potential alternatives. The Bank supports the OCC's proposed approach of relying on the existing regulatory definition of "eligible savings association" to determine an FSA's eligibility to make an election to be a CSA, and does not see a need to replace it with an alternative approach. Accordingly, the Bank does not address this item in the body of this comment letter.

[4] 83 Fed. Reg. at 47,103 ("a [FSA] can invest in a service corporation, but a national bank cannot.").

[5] 83 Fed. Reg. at 47,108-09.

approach, which should result in material burden reduction for FSAs electing CSA status and in that regard would be more consistent with the intent of the Act.

B. Proposed Framework Options for Applying National Bank Rules to CSAs

The NPR identifies and requests comment on two potential options ("Option A" and "Option B") regarding the general framework for determining which laws, regulations, and guidance applicable to national banks would apply to CSAs. Both options are similar in that a CSA would be treated like a national bank, but differ in the way a CSA would identify applicable legal requirements. Option A "would provide a framework for a [CSA] to understand the provisions of law that apply to it: That is, national bank provisions will apply, except where specifically set out in the proposed rule, and [FSA] laws will not apply, except where specifically set out in the proposed rule."[6] Option B "would provide that a covered savings association may engage in any activity that is permissible for a national bank to engage in as part of, or incidental to, the business of banking, or explicitly authorized by statute for a national bank, subject to the same authorization, terms, and conditions that would apply to a similarly located national bank, as determined by the OCC for purposes of the proposed rule."[7]

If the OCC adopts Option A, then CSAs may have greater legal certainty regarding which specific national bank statutory and regulatory provisions apply to their activities, at the cost of less flexibility for the OCC to tailor those legal requirements where a particular national bank law or regulation may be inappropriate for CSAs. If the OCC adopts Option B, on the other hand, CSAs may ultimately have more flexibility with respect to their businesses, but may need to engage with the OCC more often (and rely on OCC discretion) to determine exactly how national bank legal requirements should be tailored and applied to their activities.

While selecting Option B may result in less certainty on some interpretive questions for CSAs, and therefore necessitate more frequent informal consultation with the OCC (at least initially, as the CSA framework and precedent are established over time), it avoids the risk that a particular investment or activity could be unnecessarily undermined by a national bank law or regulation that may apply to CSAs in an unforeseen way. Therefore, the Bank believes that Option B is preferable because it preserves and provides for greater OCC flexibility to tailor its approach as needed to accommodate a CSA's unique and unforeseen business needs.

C. Proposed Branch and Agency Identification Requirement

The NPR would establish a "cataloging" requirement for existing branches and agencies that in our view is unduly burdensome, and the purpose of which is not evident from the NPR. Specifically, section 101.3(a)(2)(iii) of the NPR would require an electing FSA to include in its submission to the OCC a list identifying each branch or agency that the FSA operates or will operate on the effective date of the election that has not been the subject of an application or notice under 12 C.F.R. part 5.

The NPR indicates that the cataloging requirement is intended to identify those branches and agencies that are newly-established at the time a FSA is making an election to be a CSA (and thus may not yet have been covered by an application or notice).[8] However, the proposed rule text in the NPR does not contain such a limitation. In fact, many FSA branches were established before the Dodd-Frank Act transferred authority for FSAs from the Office of Thrift Supervision ("OTS") to the OCC and the OCC integrated the OTS's rules into its own, and thus, would not have been

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[6] 83 Fed. Reg. at 47,105.

[7] *Id.*

[8] 83 Fed. Reg. at 47,104 ("These are likely to be branches or agencies that are newly established at the time of an election under the proposed rule.").

subject to 12 C.F.R. part 5.[9] With respect to agencies, the OTS generally did not, and the OCC generally does not, require FSAs to submit an application or notice in connection with establishing an agency.[10] Therefore, the intended scope of this listing requirement is unclear. The purpose of this historical cataloging requirement is also not evident in the NPR, as information regarding existing branches is readily available to the OCC in the National Information Center Database maintained by the Board of Governors of the Federal Reserve System ("Federal Reserve") and the Institution Directory maintained by the Federal Deposit Insurance Corporation.

Based on the foregoing, the Bank believes this branch and agency identification requirement is an unnecessary burden to impose on electing FSAs. The time and cost associated with reviewing historical regulatory filings to identify branches and agencies to be included on the list would not appear to serve any compelling regulatory or supervisory purpose and, with respect to agencies, would actually require CSAs to disclose more information to the OCC than is required from FSAs or national banks.[11] Accordingly, the Bank recommends that the NPR be revised either to eliminate the branch and agency identification requirement altogether, or the OCC should further clarify the intended scope.

IV. Recommendations Regarding the Interaction of the CSA Option with Other Banking Laws and Regulations

A. Potential Impact on SLHCs

The NPR could have unintended negative consequences for holding companies that control FSAs electing CSA status. In keeping with the statutory purpose to provide CSAs with greater flexibility related to asset composition, the NPR states that a CSA would no longer be subject to the qualified thrift lender ("QTL") restrictions of the Savings and Loan Holding Company Act ("SLHCA").[12] However, under the SLHCA, if a SLHC controls a FSA that fails to satisfy the QTL test, the SLHC must register as and will be deemed to be a bank holding company ("BHC") under the Bank Holding Company Act.[13] This would result in greater restrictions on holding company activities and investments, particularly in the case of "grandfathered unitary" SLHCs. The Federal Reserve is the regulator of SLHCs, and there does not appear to have been any confirmation regarding whether the Federal Reserve will interpret Section 206 of the Act and the SLHCA in a manner that would allow a CSA's parent company to retain SLHC status (including grandfathered unitary status) and avoid becoming a bank holding company if its CSA subsidiary falls out of compliance with the QTL test (e.g., by virtue of growing non-mortgage assets).

While we do not believe that such a result was intended, absent clarification, a CSA's holding company could be at risk of losing its status as a grandfathered unitary SLHC and could even be required to register as a BHC. If holding companies of CSAs were to become BHCs, (i) future investments and acquisitions by the holding company would

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[9] *See* 12 C.F.R. § 545.93 (2011) (former OTS regulation governing branch application and notice requirements); 12 C.F.R. § 145.93 (2015) (former OCC regulation governing branch application and notice requirements for FSAs).

[10] *See* 12 C.F.R. § 5.31(k)(2)(ii) (requiring an application only if the agency office will engage in activities not listed in 12 C.F.R. § 5.31(k)(1)); 12 C.F.R. § 545.96 (similar former OTS regulation governing agency offices).

[11] The OCC does not require national banks to submit an application or notice in connection with establishing a loan or deposit production office, the national bank equivalents of an agency. *See* 12 C.F.R. §§ 7.1004, 7.1005, 7.4004 (OCC regulations governing loan and deposit production offices of national banks).

[12] 83 Fed. Reg. at 47,106 ("a [CSA] under section 5A is not subject to, among other things, the QTL test and the restrictions in 12 U.S.C. 1467a(m)(3)(B) for failing to meet the QTL test.").

[13] 12 U.S.C. § 1467a(m)(3)(C) ("Any company that controls a savings association that is subject to any provision of subparagraph (B) shall, within one year after the date on which the savings association should have become or ceases to be a qualified thrift lender, register as and be deemed to be a bank holding company").

become more burdensome, and (ii) the types of activities and investments the holding company could make would be more limited. The Bank believes that this outcome cannot have been intended by Congress in enacting Section 206 and would greatly diminish the appeal of the CSA option. Accordingly, the Bank believes that the OCC should coordinate with the Federal Reserve (as regulator of SLHCs) to issue a clarification, either as part of the final CSA rule or in a separate process undertaken by the Federal Reserve, to confirm that SLHCs that control CSAs will retain their status under the SLHCA and will not be treated as BHCs.

B. Potential Application of Interstate Merger Restrictions

Notwithstanding that Section 206 of the Act and the NPR state generally that a CSA will be treated as an FSA for purposes of consolidation and mergers, the NPR could be interpreted as limiting a CSA's ability to engage in certain interstate merger transactions, if CSAs are treated as national banks for purposes of the interstate merger laws.

As the OCC is aware, the Riegle-Neal Act imposes certain limitations on (i) interstate branching, and (ii) interstate mergers involving national banks, but does not apply to interstate branching or interstate mergers by FSAs.[14] For example, state age laws (i.e., state laws prohibiting the acquisition of recently-chartered banks) may apply to interstate mergers by national banks under the Riegle-Neal Act, but not to interstate mergers by FSAs.[15]

The NPR seems to indicate that the branching-related provisions of the Riegle-Neal Act will apply to a CSA, meaning that restrictions on interstate branching currently applicable only to national banks will also apply to CSAs.[16] However, the NPR is silent regarding the interstate merger provisions of the Riegle-Neal Act. Congress directed that interstate mergers (as opposed to branching), are expressly within scope of those matters with respect to which a CSA should continue to be subject to rules applicable to FSAs rather than the rules applicable to national banks. Accordingly, we believe the OCC should at a minimum confirm that CSAs will not be subject to the interstate merger provisions of Riegle-Neal.

Absent such clarification, uncertainty regarding the applicability of the Riegle-Neal Act could discourage and impede certain kinds of future merger activity, for example, by preventing a CSA from acquiring a recently-chartered bank in a state that has a minimum "age to be acquired" law. Congress was clear in enacting the CSA legislation that CSAs remain subject to the merger requirements applicable to FSAs, not national banks.[17] Accordingly, the Bank believes that the OCC should confirm in the final CSA rule that CSAs are only subject to the merger provisions of the Home Owners' Loan Act and other laws that apply to FSAs, and are not subject to the merger provisions applicable only to national banks, such as those in the Riegle-Neal Act.

C. Clarification of CSA Membership in the Federal Reserve System

The NPR does not address whether a CSA would be authorized or required to become a member of the Federal Reserve System. Under the Federal Reserve Act, national banks are required to become members of the Federal Reserve System.[18] Among other things, becoming a member of the Federal Reserve System requires a national bank

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[14] *See* 12 U.S.C. § 1831u.

[15] 12 U.S.C. § 1831u(a)(5) ("The responsible agency may not approve an application pursuant to paragraph (1) that would have the effect of permitting **an out-of-State bank** or out-of-State bank holding company to acquire a bank in a host State that has not been in existence for the minimum period of time, if any, specified in the statutory law of the host State." (emphasis added)).

[16] 83 Fed. Reg. at 47,108 ("For example, a [CSA] seeking to establish a de novo branch or close an existing branch would be subject to the statutes and regulations that govern the establishment or closing of a national bank branch.").

[17] *See* 12 U.S.C. § 1464a(d)(2).

[18] 12 U.S.C. § 222 ("Every national bank in any State shall, upon commencing business … become a member bank of the Federal Reserve System").

to purchase a certain amount of stock in a regional Federal Reserve Bank.[19] FSAs on the other hand, are ineligible to become members of the Federal Reserve System.[20]

Section 206 and the NPR do not address whether a CSA may or must become a member of the Federal Reserve System. Membership in the Federal Reserve System comes with certain costs (e.g., financial cost of acquiring Reserve Bank stock), as well as benefits (e.g., guaranteed dividends on Reserve Bank stock), that could make it attractive to some, but not all, CSAs. The Bank believes that to fulfill Congress' intent of providing electing FSAs with a tailored and more flexible operating environment, the OCC should coordinate with the Federal Reserve to issue a clarifying statement that CSAs may, but are not required to, become members of the Federal Reserve System.

V. Conclusion

We believe that the changes suggested above are consistent with Congress' intent to provide FSAs electing CSA status with "streamlined standards and procedures" for making an election. We also believe it is important that the OCC coordinate with other regulators to the extent necessary to ensure that effective implementation of the CSA regulatory framework is not undermined by potential impacts on electing FSAs under other bodies of law.

We appreciate the opportunity to comment on the proposed rule and would be happy to address any questions or provide any additional information the OCC may find helpful as it works to finalize this important rule.

Respectfully,

Alessandro P. DiNello
President and Chief Executive Officer

cc: Stephen V. Figliuolo, Chief Risk Officer
Patrick M. McGuirk, General Counsel

[19] 12 U.S.C. § 222; 12 C.F.R. § 209.2 ("The bank shall pay for the stock (or deposit) in accordance with § 209.4 of this part.").

[20] OCC, *Conversions to Federal Charter*, 17, n.29 (August 2018).