



Office of Thrift Supervision
Department of the Treasury

Regional Director, Northeast

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OTS No.: [REDACTED]

[REDACTED]
[REDACTED]
Dear Mr. [REDACTED]

This letter serves as a reminder of prior observations made by this agency regarding purchases of Bank Owned Life Insurance (BOLI) and highlights OTS guidance in this area. On July 31, 2002, the Office of Thrift Supervision issued Regulatory Bulletin 32-26, which amended OTS's regulatory guidance in several respects. Specifically, Section 250 of the Thrift Activities Handbook was amended as follows:

- Revised the appendix to track more closely the Office of the Comptroller of the Currency's (OCC) bulletin on BOLI, BC 2000-23.
- Stated explicitly that purchasing BOLI that is not incidental to banking is not permitted.
- Revised the concentration guidance to make it clear that thrifts' investment in BOLI should not exceed 25 percent of capital.
- Added guidance on separate account BOLI.
- Discussed loans to one borrower limitations in more detail and identified the conditions and controls necessary to allow lending limits to apply to the underlying assets in separate account BOLI.
- Added a discussion on insurable interest and stated that holding insurance in excess of the institution's risk of loss is considered unsafe and unsound.

Purchases of BOLI, even when less than 25 percent of capital, can be a cause for supervisory concern because of various operational, credit, liquidity, and market risks attendant to such holdings. One such risk is the potential loss of tax benefits due to either the mishandling of the investment or tax law changes. BOLI purchases have received considerable scrutiny from the Internal Revenue Service.

Over the past five years, there has been a marked increase in purchases of BOLI in amounts at, near, or above 25% of core capital. The Northeast Region's latest financial monitoring analysis indicates that BOLI holdings by certain institutions now exceed 25% of core capital. (In some cases, the initial BOLI purchase amounted to 25% or less of core capital, but subsequent increases to the cash value of the policies outpaced the growth in core capital.)

Institutions nearing or exceeding this threshold will be reviewed in examinations or field visits to determine: (i) the analysis done by the institutions prior to purchasing BOLI; (ii) whether the concentrations pose safety/soundness concerns; and (iii) the actions that should be taken by institutions that are found to have unsafe and unsound concentrations.

As discussed in RB 32-26, institutions should not automatically assume that a concentration level as high as 25% of capital is always appropriate. If you are considering a purchase of BOLI, we urge you to review the guidance in RB 32-26. We also expect that you discuss any planned BOLI purchases with the Assistant Director or Field Manager assigned to your institution before committing to a purchase that could cause concentration concerns. (As a rule of thumb, planned purchases at or above 20% of core capital should trigger discussions with OTS.)

Finally, we expect any decision to purchase BOLI will be supported by:

- Internally prepared documentation that addresses the various pre-purchase analysis factors set forth in Section 250 of the Handbook;
- A resolution of the association's board of directors: (a) approving the purchase; (b) establishing limits as a percentage of capital; and (3) describing how the board will exercise its continuing responsibility to oversee the activity in the future; and
- An analysis comparing projected increases in the carrying value of the BOLI asset to projected growth in core capital over the next three years. (In other words, what would the projected ratio of BOLI to core capital be three years from the date of purchase?)

We ask that you share this letter with your board of directors at its next regularly scheduled meeting. We also have attached a copy of OTS Regulatory Bulletin 32-26 on Bank Owned Life Insurance for your benefit and guidance.

Yours Truly,



Robert C. Albanese
Regional Director

Attachment: RB 32-26