

TITLE 230 – DEPARTMENT OF BUSINESS REGULATION

CHAPTER 40 – BANKING

SUBCHAPTER 10 – LENDING

Part 1 - Derivative Transactions in Lending Limits

1.1 Authority

This Regulation (“Regulation”) is promulgated pursuant to the authority granted to the Department of Business Regulation (“Department”) by R.I. Gen. Laws Title 19, generally, and R.I. Gen. Laws §§ 19-3-3(b) and 19-4-16, specifically.

1.2 Purpose

The purpose of this Regulation is to clarify that any Rhode Island state-chartered Financial Institution that engages in Derivative Transactions is required to take into consideration Credit Exposure to Derivative Transactions with respect to the lending limits in R.I. Gen. Laws § 19-3-3 and any other relevant applicable lending limits in R.I. Gen. Laws Title 19 or Federal law.

1.3 Severability

If any provision of this Regulation or the application thereof to any Person or circumstance is held invalid or unconstitutional, the invalidity or unconstitutionality shall not affect other provisions or applications of this Regulation which can be given effect without the invalid or unconstitutional provision or application, and to this end the provisions of this Regulation are severable.

1.4 Definitions

A. Unless otherwise provided by this Regulation or unless the context clearly requires otherwise, terms used in this Regulation shall have the same meaning as the terms defined in R.I. Gen. Laws § 19-1-1 or in any other relevant provision of R.I. Gen. Laws Title 19. All definitions herein may be superseded by applicable amendments by the Rhode Island Financial Institution’s primary federal regulatory authority and any such amendment shall apply, as relevant and applicable, in that specific context.

1. “Credit exposure” (to a counterparty in connection with a Derivative Transaction) shall be determined based on an amount that the Financial Institution reasonably determines under the terms of the

derivative or otherwise would be its loss were the counterparty to default on that date, taking into account any netting and collateral arrangements and any guarantees or other credit enhancements; provided, that the Financial Institution may elect to determine credit exposure on the basis of such other method of determining credit exposure as may be permitted by the Financial Institution's primary federal regulatory authority.

2. "Director" means the Director of the Department or his or her designee
3. "Derivative transaction" shall include any transaction that is a contract, agreement, swap, warrant, note, or option that is based, in whole or in part, on the value of, any interest in, or any quantitative measure or the occurrence of any event relating to, one or more commodities, securities, currencies, interest or other rates, indices, or other assets.
4. "Financial institution" means any entity, other than a credit union, duly organized under the laws of this state which has the statutory authority to accept money on deposit pursuant to title 19, including an entity which is prohibited from accepting deposits by its own by-laws or agreement to form; the term includes, but is not limited to banks, trust companies, savings banks, loan and investment banks and savings and loan associations.

1.5 Criteria for Engaging in Derivative Transactions

A. Notice

1. Financial Institutions with no prior Derivative Transaction experience as of December 31, 2012 seeking to engage in Derivative Transactions for the first time after the effective date of this Regulation shall provide the Department written notice of that intention at least thirty (30) calendar days in advance of any binding contractual agreement and provide documentation that said Financial Institution is permitted to engage in Derivative Transactions pursuant to the definition of "Eligible Contract Participant" in 7 U.S.C. § 1(a)(18).
2. Financial Institutions with prior experience in Derivative Transactions shall provide notice of said fact and include the approximate date that the Financial Institution began engaging in Derivative Transactions. Said Financial Institution shall immediately conduct the relevant Credit Exposure impact and analysis for the Department's review during its next examination.
3. Should any Financial Institution's lending limit be exceeded by its participation in Derivative Transactions, said Financial Institution

shall immediately notify the Department in writing and prepare an analysis and corrective action remedying said issue.

- B. A Financial Institution seeking to participate in or currently participating in Derivative Transactions must document in its files that it:
1. is Well Capitalized in accordance with its Federal insurer's standards and not subject to any written agreement, order, capital directive, or prompt corrective action, directive to meet and maintain a specific capital level for any capital measure and has an ability to absorb and/or mitigate any Credit Exposure indicated by such participation;
 2. does not meet the definition of "Troubled condition" in 12 C.F.R. § 371.2(f);
 3. has a reasonable basis for engaging in the Derivative Transaction;
 4. has an ability to manage and assess Credit Exposure; and,
 5. has effective internal controls to manage, monitor, and assess Credit Exposure.
- C. Any Financial Institution that does not meet the conditions in § 1.5 (B)(1)(5) of this Part may request written permission from the Department to engage in Derivative Transactions.

1.6 Criteria for Evaluating Credit Exposure

- A. Rhode Island Financial Institutions shall comply with all requirements set forth in the Office of Comptroller of Currency's ("OCC") Final Interim Rule on Lending Limits 12 C.F.R. Parts 32, 159 and 160 (Effective July 21, 2012) with respect to Credit Exposure caused by Derivative Transaction participation on relevant lending limits.
- B. Rhode Island Financial Institutions shall act cautiously, responsibly and consistent with safe and sound banking practices in any Derivative Transaction participation.

1.7 Credit Unions

- A. While R.I. Gen. Laws § 19-5-15(2)(i) may be construed to allow Credit Unions to invest in Derivative Transactions, it is the Department's position that Rhode Island state-chartered Credit Unions are only permitted to participate in Derivative Transactions subject to the conditions in §§ 1.7(B) and (C) of this Part. §§ 1.5 and 1.6 of this Part do not apply to Rhode Island state-chartered Credit Unions.

- B. Before engaging in or taking any affirmative step toward participating in Derivative Transactions, Rhode Island state-chartered Credit Unions shall obtain a non-objection letter and/or written approval from the Department and National Credit Union Administration ("NCUA").
- C. If a Rhode Island state-chartered Credit Union obtains approval and/or non-objection to participation in Derivative Transactions from both the Department and the NCUA, the Department may impose appropriate conditions necessary to confirm the Credit Union's ability to manage, monitor, and assess Credit Exposure related to participation in Derivative Transactions and ensure the safety and soundness of the Credit Union.

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**TITLE 230 - DEPARTMENT OF BUSINESS REGULATION (INCLUDES
THE OFFICE OF THE HEALTH INSURANCE COMMISSIONER)**

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PART 1 - DERIVATIVE TRANSACTIONS IN LENDING LIMITS (230-RICR-40-10-1)

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