MEMORANDUM

May 29, 1981

TO : Ralph C. Ferrara, General Counsel
Office of the General Counsel

FROM : Peter J. Romeo, Chief Counsel PR
Division of Corporation Finance

RE : Your note of May 26 and the attached news release of the Comptroller on retail repos

I have reviewed the Comptroller's retail repo release, particularly pages 4-7 captioned "Securities Law Issues", and I generally agree with the securities law analysis. One point I might make is that in several places (such as the first paragraph of the cover page) the release characterizes a retail repo as a transfer and repurchase of an "interest" in a government security. Technically, it would be more correct to state that a retail repo involves the issuance of a bank obligation which is secured by an interest in a government security. I recognize, however, that this clarification is made in the body of the release (page 3), and therefore the Comptroller's position basically is consistent with the Division's characterization of retail repos.

For your information, I should also advise you that the Division currently is preparing responses to two no-action requests concerning the proposed issuance of retail repos. As soon as the Division receives certain additional information from one of the requestors, the Division intends to seek the Commission's authorization to grant these no-action requests, and also to publicize these responses through the issuance of a "wrap-around" interpretive release. Copies of our draft no-action responses and interpretive release will be circulated to OGC, as well as the Divisions of Enforcement, Investment Management and Market Regulation, before they are submitted to the Commission.

CC: Jack Shinkle

SEC

5/26/81

Joel Goldberg
Dan Goelzer
Jake Stillman
Eric Roiter
Don Langevoort
Alan Rosenblat
Peter Romeo
Irwin Borowski

I would like your comments on the attached ASAP.

Ralph Ferrara

Attachment

NEWS RELEASE

Comptroller of the Currency
Administrator of National Banks

81-15

Washington, D.C. 20219

For: IMMEDIATE RELEASE

Date: May 14, 1981

Comptroller of the Currency John G. Heimann today sent to national banks guidelines for operating so-called retail repurchase, or "retail repo", programs designed for consumers. Under a retail repo program, a bank transfers to a customer an interest, in a denomination of less than $100,000, in a U.S. government or agency security, and agrees to "repurchase" it at a date not more than 89 days in the future. The bank agrees to pay the customer the original purchase price plus a pre-determined rate of interest.

"Retail repos are a liability instrument that permits consumers to earn market rates of interest on relatively small amounts of money," Heimann said. "This product should allow national banks to compete more effectively with money market mutual funds. The intent is essentially to offer an instrument to the retail banking public that provides a yield roughly competitive with the yields available on certain short term instruments offered by non-bank competitors."

In issuing the office's guidance on such programs, which was outlined in a banking circular mailed to all national banks, the Comptroller noted that the number of banks and other financial institutions marketing retail repos has been increasing. He said that these offerings raise a number of issues involving disclosure, federal and state securities laws, Federal Reserve Board regulations, borrowing limits for national banks, and principles of safe and sound banking.

Heimann noted that customers may not fully understand the difference between a retail repo and a deposit, since both are offered by national banks. For that reason, and "in order to avoid potential liability under the securities laws, banks should fully disclose all material information regarding the retail repo offering," he said. Among other things, this disclosure should include a detailed explanation of the transaction.

The Comptroller said customers "should be clearly warned that the retail repo is not a deposit, is not FDIC-insured, and is not guaranteed in any way by the U.S. government or agency thereof. Language generally associated with deposits must be avoided to prevent creating the impression that insured deposits are being offered." Customers must be informed that they may become unsecured creditors of the bank if the market value of their shares in the underlying U.S. security falls below the amount of funds they invested.

Comments or questions about this banking circular should be directed to Chief National Bank Examiner, Office of the Comptroller of the Currency, Washington, D.C. 20219.

# # # #

BANKING ISSUANCE

Comptroller of the Currency
Administrator of National Banks

Type: Banking Circular

Subject: Retail Repurchase Agreements

TO: Chief Executive Officers of all National Banks, Regional Administrators and all Examining Personnel.

PURPOSE

This banking circular provides general guidance to national banks operating or proposing to operate so-called retail repurchase agreement ("Retail Repo") programs involving United States government or agency securities. It is intended to alert the banking industry to supervisory concerns and legal issues relating to such programs.

SCOPE

This circular applies to Retail Repos marketed to the public by national banks which involve a "sale" to customers of an interest in a U. S. government or agency security, in a denomination of less than $100,000 and for a term of less than 90 days, subject to an agreement by the bank to "repurchase" the interest. The intent of such a program is essentially to offer an instrument to the retail banking public which provides a yield roughly competitive with the yields available on certain short-term instruments offered by non-bank competitors.

DISCUSSION

Introduction

The number of banks and other financial institutions marketing Retail Repos has been increasing. These offerings raise a number of issues involving federal and state securities laws, Federal Reserve Board regulations D and Q, the borrowing limits of 12 U.S.C. 82, and principles of safe and sound banking. The attachment to this circular provides an analysis prepared by the OCC staff of significant legal issues. Because of the complexity of these issues, banks contemplating a Retail Repo program may find it advisable to consult legal counsel. The following discussion is intended to assist banks to operate such programs properly.

BANKING ISSUANCE

Comptroller of the Currency
Administrator of National Banks

Type: Banking Circular

Subject: Retail Repurchase Agreements

Safe and Sound Banking Issues

Maturity and Interest Rate Gaps

Retail Repos often attract volatile source funds from customers who may follow high yields as they become available elsewhere. In order to retain Retail Repo funds a bank must offer competitive rates. If the funds are used to purchase fixed rate assets with maturities longer than the Retail Repos, the bank may be caught paying higher rates than it is earning on the assets purchased. Moreover, the underlying securities may, in fact, depreciate significantly as rates rise so that a bank may be unable to liquidate the collateral and unwind the program without incurring significant losses. A number of banks have found themselves unacceptably exposed as a result of such interest rate and maturity differentials. Such exposure places severe strains on earnings, liquidity, and capital.

Written policies and procedures should be adopted to control maturity gaps between Retail Repo assets and liabilities. These policies should limit the duration of gaps and the maximum dollar amount permitted in each gap range. Banks should also adopt specific guidelines addressing the risks associated with: (i) accounts in excess of $10,000; (ii) customers with no other relationship with the bank; and (iii) customers residing or doing business outside of the bank's normal trade area. The written policies and procedures should include contingency plans to deal with the risks associated with a rapid run-off of Retail Repo funds.

Banks are expected to design and implement internal monitoring and reporting systems to insure adherence to the written policies and procedures. For example, monthly gap reports and securities valuations are essential. Detailed reports should be prepared to provide senior bank management with an analysis of Retail Repo purchaser concentrations by name, account size, geographic distribution and other relevant factors.

Market Coverage

To stay within the parameters of the exception to 12 U.S.C. 82 provided by OCC Interpretive Ruling 7.1131, the market value of the underlying security at the time of any purchase of a Retail Repo must at least equal the amount of the aggregate purchase price paid by Retail Repo purchasers secured by that security.

BANKING ISSUANCE

Comptroller of the Currency
Administrator of National Banks

Type: Banking Circular

Subject: Retail Repurchase Agreements

Security Interest

Banks should be especially careful to ensure that the customer's security interest in the underlying collateral is perfected under applicable state law. Banks may wish to use an independent custodian or trustee to hold title to government securities in which customers have security interests.

Disclosure and Advertising

As a matter of safe and sound banking practice and in order to avoid potential liability under the securities laws, banks should fully disclose all material information regarding the Retail Repo offering. Disclosure should include, at a minimum, appropriate background information regarding the bank and its financial condition, and the nature and terms of the Retail Repo (including minimum investment denominations, interest rates, maturities and any prepayment fees). The customer should be given a detailed explanation of the transaction. The security underlying the transaction should be specifically and accurately identified. The customer should be advised (1) that the Retail Repo is an obligation of the issuing bank and that the underlying security serves as collateral; (2) that the bank will pay a fixed amount, including interest on the purchase price, regardless of any fluctuation in the market price of the underlying security; (3) that the interest rate paid is not that of the underlying security; and (4) that general banking assets will most likely be used to satisfy the bank's obligation under the Retail Repo rather than proceeds from the sale of the underlying security. In addition, the customer should be advised at the time of purchase of the actual or approximate market value of the underlying security interest and he should be clearly warned that the Retail Repo is not a deposit, is not FDIC insured, and is not guaranteed in any way by the U. S. Government or any agency thereof. Language generally associated with deposits must be avoided to prevent creating the impression that insured deposits are being offered. The customer must be informed that he may become an unsecured creditor of the bank to the extent the market value of his security interest falls below the amount of the funds invested.

BANKING ISSUANCE

Comptroller of the Currency
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Type: Banking Circular

Subject: Retail Repurchase Agreements

As discussed in the attached OCC staff analysis of legal issues, even if a Retail Repo were determined to be a security under the Securities Act of 1933, it would appear to be exempt from the registration requirements of the Securities Act, the Uniform Securities Act (adopted in most states) and the OCC's securities offering disclosure rules. Although full disclosure is required in connection with an offering of Retail Repos, no specific offering document, such as a prospectus or offering circular, is prescribed. Banks may use any form of written disclosure document (e.g., an offering memorandum or brochure) so long as it contains disclosure which would be required for instruments subject to the anti-fraud provisions of the securities laws. (Banks may find the OCC's Securities Offering Disclosure Rules (12 CFR 16, Nov. 1980 Supplement to the Comptroller's Manual for National Banks) helpful as a guide for developing disclosure materials.)

Procedures should be implemented to guide bank employees in offering Retail Repos to the public. Banks may wish to circulate an internal memo to all involved bank personnel as a means of informing them appropriately with respect to Retail Repos and the necessary disclosure procedures. Such a memorandum might include general responses to questions likely to be asked by potential purchasers. These responses should conform in substance to the disclosure made in the offering materials. Bank personnel should be instructed to deliver a copy of the offering materials to each purchaser prior to the time of purchase.

Originating Office: Chief National Bank Examiner
Investment Securities Division

COMMENTS: Comments and questions about this banking circular should be directed to:

Office of the Comptroller of the Currrency
490 L'Enfant Plaza East, S.W.
Washington, D.C. 20219

BANKING ISSUANCE

Comptroller of the Currency
Administrator of National Banks

Type: Banking Circular

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Attention: Director, Investment Securities Division
[if regarding supervisory matters]
or
Attention: Director, Securities Disclosure Division
[if regarding legal issues]

John G. Heimann
Comptroller of the Currency

Attachment

OCC Staff Analysis of Certain Legal Issues Raised by Retail Repurchase Agreements

The following is a general analysis, prepared by the OCC staff, of various issues which are raised by Retail Repos (as defined in the Banking Circular to which this analysis is attached) under the federal and state securities laws, as well as the federal banking laws. Many of these issues involve novel and complex legal questions which have not yet been fully addressed by the courts or interested administrative agencies. 1/ Accordingly, this discussion of legal issues is only intended to bring such issues to the attention of national banks contemplating a Retail Repo program and should not be construed as presenting definitive legal interpretations.

Introduction

Regulation D 2/ of the Board of Governors of the Federal Reserve System ("FRB") requires the maintenance of reserves calculated as specified percentages of "deposits" held by depository institutions. FRB Regulation Q 3/ specifies limitations on the interest rates payable on deposits. In the case of national

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1/ For example, although the Securities and Exchange Commission ("SEC") has taken the position in a recent release that certain repurchase agreements are "securities" for purposes of particular provisions of the Investment Company Act of 1940 (15 U.S.C. § 80 a-1 et seq.) ("Investment Company Act"), it expressly declined to state a position as to the general status of repurchase agreements under other provisions of the federal securities laws. See Investment Company Act Release No. 10666 (April 18, 1979). At present, the SEC staff is not responding substantively to requests for interpretive or "no action" advice regarding the status of Retail Repos under the federal securities laws.

2/ 12 C.F.R. Part 204 (1980), as amended.

3/ 12 C.F.R. Part 217 (1980), as amended.

banks, federal banking law also sets a limit on the permissible indebtedness that such banks may incur. 4/

Regulation D contains an exception from its reserve requirements that excludes from the definition of "deposit" any obligation which

> [e]vidences an indebtedness arising from a transfer of direct obligations of, or obligations that are fully guaranteed as to principal and interest by, the United States or any agency thereof that the bank is obligated to repurchase. 5/

Until August 1979, Regulation Q provided a similar exception from its interest rate limitations. 6/ In addition, Interpretive Ruling 7.1131 of the OCC provides that the sale of securities under an agreement to repurchase is not a "borrowing" subject to the restrictions on bank indebtedness set forth in 12 U.S.C. § 82. 7/

A transaction involving the "sale" of a whole government security, typically between institutional parties, which is effected pursuant to the above exceptions to Regulations D and Q and 12 U.S.C. § 82, is commonly referred to as a wholesale repurchase agreement ("Wholesale Repo"). Such factors as the purpose of the transaction and its short term suggest that a Wholesale Repo is, in terms of essential economic realities, a

4/ 12 U.S.C. § 82. This limit is expressed as the amount of the bank's capital stock paid in and undiminished plus 50 percent of the amount of its unimpaired surplus fund.

5/ This exception was originally set forth in 12 C.F.R. § 204.1(f)(2)(1980). In accordance with the Monetary Control Act of 1980 (Title I of Pub. L. No. 96-221), on August 22, 1980, the FRB published a revised Regulation D, effective November 13, 1980. 45 Fed. Reg. 56,009 (1980) (to be codified in 12 C.F.R. Part 204). The revision of Regulation D has not altered the exception. See preamble to revised Regulation D, 45 Fed. Reg. at 56,014, and new § 204.2(a)(1)(vii)(B), id. at 56,019.

6/ See 12 C.F.R. § 217.1(f)(2)(1979).

7/ 12 C.F.R. § 7.1131. The ruling also notes that such agreements do not create obligations subject to the lending limit of 12 U.S.C. § 84. See also text at note 25 infra.

short-term collateralized borrowing.8/ But for the limited exceptions from Regulations D and Q and 12 U.S.C. § 82, it would be treated as either a reservable deposit subject to interest rate restrictions or a borrowing subject to § 82 limitations.

In August 1979, the FRB limited the exception contained in Regulation Q by providing that, for evidences of indebtedness of less than $100,000, it would only be applicable thereafter when the indebtedness had a term of less than 90 days and was not automatically renewable. 9/ Repurchase transactions effected pursuant to the conditions of the revised exception to Regulation Q are generally known as Retail Repos. The principal differences between a Wholesale and a Retail Repo are the nature of the typical "purchaser" involved (institutional entity versus individual investor) and the usual investment amount involved (an amount equal to the market value of the underlying security versus a fraction of that amount).

Although specific terms and conditions of Retail Repos may vary, most possess certain common attributes: the "sale" to the public of a small-denomination, undivided fractional interest in an underlying, larger face amount government security, subject to the bank's (i.e., the "seller's") unconditional obligation to repurchase that interest within 89 days or less for a predetermined amount, typically the sum of the original investment plus "interest." While a Retail Repo is variously styled by offering banks as a "sale" or "transfer" of a U. S. government security or of "participations" or "shares" in such a security, under a Retail Repo the so-called "purchaser" obtains only limited indicia of ownership with respect to the underlying government security. 10/ For example, the investment return on a Retail Repo is independent of fluctuations in the market value of, or interest paid on, that security. Thus, it appears that what is actually "transferred" is in the nature of a security interest in the underlying government obligation, and that, like the Wholesale Repo, the Retail Repo constitutes, in economic reality, a collateralized or secured borrowing.

8/ See, e.g., M. STIGUM, THE MONEY MARKET: MYTH, REALITY, AND PRACTICE 328 (1978). See also United States v. Erickson, 601 F.2d 296, 300 n.4 (7th Cir. 1979); SEC v. Miller, 495 F. Supp. 465, 467 (S.D.N.Y. 1980).

9/ 12 C.F.R. § 217.1(f)(2)(ii) (1980). The Federal Deposit Insurance Corporation ("FDIC") and the Federal Home Loan Bank Board ("FHLBB") issued similar regulations at that time. 12 C.F.R. §§ 329.10(b)(2) and 531.12 (1980).

10/ This, of course, may also be the case with a Wholesale Repo, depending on its specific terms.

Securities Law Issues

As discussed above, it appears that a Retail Repo is, in economic reality, a short-term borrowing transaction. In effecting such a transaction, the bank issues an "evidence of indebtedness" (embodied in the Retail Repo itself) whereby it unconditionally promises to pay a specified amount at a future date to the purchaser of the Retail Repo. This evidence of indebtedness (to which the bank's general assets are subject) is secured by an interest in the underlying government security which is "conveyed" to the Retail Repo purchaser. Although the precise status of a Retail Repo transaction under the securities laws has not been conclusively addressed, it could be found to involve the offer and sale of a "security" (i.e. the "evidence of indebtedness") 11/ within the meaning of those laws. 12/

Even if found to be securities under these statutes, as evidences of indebtedness issued by a bank, they would be exempt from the registration requirements of the Securities Act and the state securities laws. 13/ Such instruments would also not be subject

11/ For definitions of the term "security," see § 2(1) of the Securities Act of 1933 ("Securities Act"), 15 U.S.C. § 77b(1); § 3(a)(10) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78c(a)(10); § 401(1) of the Uniform Securities Act (to date enacted by 34 states and the District of Columbia).

12/ While the offering of a "participation" in the underlying security, coupled with an attendant repurchase obligation, might conceivably be viewed as involving three separate securities (i.e., the "participation," the repurchase agreement and the underlying government security), the transaction, if held to involve a "security" at all, is more likely to be characterized, when taken as an integrated "package," as involving only one security which is issued by the bank. Cf. in this regard SEC v. W. J. Howey Co., 328 U.S. 293 (1946) (real estate deed plus servicing contract was "investment contract" and hence a "security"); SEC v. C. M. Joiner Leasing Corp., 320 U.S. 344 (1943) (sale of oil lease plus seller's promise to drill one test well was "investment contract").

13/ See § 3(a)(2) of the Securities Act, 15 U.S.C. § 77c(a)(2). § 402(a)(3) of the Uniform Securities Act exempts bank-issued securities from registration. All states have similar provisions.

to the OCC's Securities Offering Disclosure Rules. 14/

To the extent that the structure of a Retail Repo deviates from the typical format described above, additional legal questions under the securities laws may be presented. For example, if a bank actually were to sell equitable "participations" in an underlying government security (the record ownership of which was not divisible into increments) it may be deemed to have created a separate entity which is an investment company required to be registered as such under the Investment Company Act. 15/ In addition to the obvious practical problems which would be presented if this were found to be the case, it also raises the possibility that the bank would be in violation of those provisions of the Glass-Steagall Act which prohibit national banks from underwriting certain types of securities and from being affiliated with any entity engaged principally in the issue, flotation, underwriting, public sale or distribution of securities. 16/

Technically this is not being done.

In any event, the ability of a bank to fractionalize record ownership of, or title to, a large face amount government security into increments less than the smallest denomination thereof is doubtful. 17/ The underlying government security is generally evidenced only by a book-entry maintained by one of the

14/ 45 Fed. Reg. 11,115 (1980) (to be codified in 12 C.F.R. Part 16). These instruments are not among those specifically enumerated in the definition of "security" contained in such rules. Id. at 11,117 (to be codified in 12 C.F.R. § 16.2(d)). In any event, construed as short-term collateralized borrowings, they appear to be excepted from that definition as an "indebtedness incurred in the ordinary course of business." Id.

15/ See 15 U.S.C. § 80a-3(a)(1). See also Franklin National Bank, SEC staff reply letter, [1973 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 79409; Moultrie National Bank, [1974-75 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 80081.

16/ 12 U.S.C. §§ 24, 377 and 378(a). See Investment Company Institute v. Camp, 401 U.S. 716 (1971), and Board of Governors of the Federal Reserve System v. Investment Company Institute, 49 U.S.L.W. 4161 (U.S., Feb. 24, 1981) (No. 79-927).

17/ See 31 C.F.R. §§ 350.2(a) and 350.6(a)(1) & (2). See also State National Bank of Maryland, SEC Release No. 34-16321, November 5, 1979 (Statement submitted to the SEC pursuant to § 21(a) of the Exchange Act).

Federal Reserve Banks, 18/ but a reserve bank is not authorized to indicate any such fractionalization of a security as part of the entry. 19/ Moreover, while a national bank may make a notation on its corresponding book-entry (e.g., when acting as a bailee 20/), it would appear that such a notation, if reflecting a fractionalization (i.e., a noted amount less than the smallest denomination of the underlying security), would not constitute anything beyond an "equitable interest" regardless of the characterization of the Retail Repo as a purchase/repurchase transaction. 21/

Finally, it should be emphasized that the exemption of a security from the registration requirements of the Securities Act and the state securities laws does not remove the offer and sale of the security from the ambit of the anti-fraud provisions of such laws. 22/ In accordance with these provisions, a bank must

18/ Since December 31, 1978, Treasury bills have been available only in book-entry form. 31 C.F.R. §§ 349.1(b) & (c); 350.0(b); 350.17(f) (1980).

19/ The Federal Reserve Banks are neither bailees for purposes of notification of pledges of Treasury bills nor "third parties in possession" from whom acknowledgement of transfers of pledges can be elicited, and any such notifications of pledges or advices of transfers have no effect. 31 C.F.R. § 350.4(b). With respect to these book entries, no filing or recording with a state recording office of such fractionalized pledges "shall be necessary or effective. . . ." Id. § 350.4(c).

20/ 31 C.F.R. § 350.6(a)(3).

21/ Treasury regulations leave the question of the appropriate method by which a commercial bank can effectively transfer the Treasury bill or perfect a pledge thereof to "applicable law." 31 C.F.R. § 350.4(b). The commercial entity, not the Federal Reserve Bank which maintains the book-entry, is the bailee and/or "third party in possession" with respect to any pledge or transfer of pledge. Id. § 350.6(a)(3). However, it is unclear under the law of most states how an incremental beneficial interest in an uncertificated security could be effected. See generally, Coogan, Security Interests in Investment Securities under Revised Article 8 of the Uniform Commercial Code, 92 HARV. L. REV. 1013 (1979); Aronstein, Haydock & Scott, Article 8 is Ready, 93 HARV. L. REV. 889 (1980).

22/ See § 17(a) of the Securities Act, 15 U.S.C. § 77q; § 10(b) of the Exchange Act, 15 U.S.C. § 78j and Rule 10b-5 issued thereunder, 17 C.F.R. § 240.10b-5. See also, § 101 of the Uniform Securities Act.

provide full disclosure of all material information necessary to enable an investor to make an informed decision whether to purchase a security. Failure to provide this information may subject the bank to substantial liabilities. The OCC is of the view that complete disclosure concerning a Retail Repo program is also necessary to safe and sound banking practice and for the protection of bank customers.

A general discussion of the miminum types of disclosure regarding Retail Repo programs which the OCC believes appropriate is set forth in the section captioned Disclosure and Advertising in the Banking Circular to which this analysis is attached. However, the anti-fraud provisions of the securities laws require disclosure of all material facts regarding the circumstances of a particular transaction. Accordingly, depending on the precise nature of a Retail Repo program, disclosures to prospective purchasers beyond those identified in the circular may be necessary.

Banking Law Issues

Regulations D and Q

As discussed above with respect to the reserve requirements of Regulation D, the FRB has excepted from the definition of "deposits" those "evidences of indebtedness" arising out of a "transfer" of a U. S. Government issued or guaranteed obligation which the bank is obligated to "repurchase." Similarly, the interest rate limitations for "deposits" under Regulation Q do not apply to such "evidences of indebtedness," if in a denomination of less than $100,000 with a maturity of less than 90 days which is not automatically renewable.

Both of these exceptions require a "transfer," but that term is not further defined. It would seem that the granting of a security interest in the underlying government obligation, as occurs in a Retail Repo transaction, should be a sufficient "transfer" for these purposes. 23/ In this regard, Regulations D

23/ The transfer of a security interest in the underlying security, or (in effect) a pledge of that security, has been held to be an "offer" or "sale" of the security for purposes of the anti-fraud provisions of the securities law. See Rubin v. United States, 49 U.S.L.W. 4103 (March 11, 1981) (No. 79-1013) (pledge of a security for a loan is an offer or sale within the meaning of § 17(a) of the Securities Act). The perfection of such a security interest is also important to provide collateral protection for the Retail Repo purchaser.

and Q by their own terms acknowledge the "borrowing" as well as the "sale/repurchase" aspects of the "transfer" involved in a repurchase transaction. 24/ Both provisions except any obligation which "evidences an indebtedness" arising from the transfer of a government security that the bank is obligated to "repurchase." Thus, it would seem that the term "transfer" as used in the foregoing provisions contemplates the transfer of less than complete ownership of, or title to, the government security. Therefore, it would appear that the terms of these two provisions could be satisfied by a "transfer" which in economic substance constituted a collateralized borrowing by the bank, creating and transferring to the "purchaser" of the Retail Repo a security interest in an underlying government security.

12 U.S.C. § 82

The OCC, as noted above, has taken the position that the "sale" of securities by a bank under an agreement to "repurchase" at the end of a stated period is not a borrowing subject to 12 U.S.C. § 82. However, for purposes of that interpretation, the "securities" involved have been defined to mean "identifiable federal government securities, securities fully guaranteed as to principal and interest by the federal government or an agency thereof, or identifiable state or local government securities." 25/

If a Retail Repo is viewed as a short-term collateralized borrowing, a question is presented as to whether the exemption from the limitations on borrowing contained in 12 U.S.C. § 82, which applies to Wholesale Repos, extends to Retail Repos. The OCC staff is of the view that, for purposes of Interpretive Ruling 7.1131, the "sale" of a fractionalized interest in an underlying government security is not distinguishable from the "sale" of the underlying security itself, where each is subject to repurchase. In either transaction, the repurchase agreement creates an obligation to repurchase what was "sold." Such "sales," whether of underlying securities, or of fractional interests therein, are liabilities of the bank.

24/ Even if the "purchaser" of the security interest subject to the repurchase agreement were to be viewed as holding title in a property law sense, in economic substance he is a lender of money with a security interest in the collateral. See, e.g., Union Planters National Bank of Memphis v. United States, 426 F.2d 115 (6th Cir. 1970) (interest paid on municipal securities, otherwise tax-exempt, is not exempt to the "purchaser" since it represents income to the "seller" which the "seller" bargains away as part of expense of the right of repurchase).

25/ Repurchase Agreements, OCC staff reply letter, [1977 Transfer Binder] FED. BANKING L. REP. (CCH) ¶ 85020.

Interpretive Ruling 7.1131 was promulgated in furtherance of the public policy that the marketing of government securities should be facilitated. The OCC staff believes that the marketing of Retail Repos, when properly structured, is consistent with this policy and that the transfer, as security, of an undivided fractional interest in an identifiable underlying government security comes within the meaning of "sale" as used above. 26/ Therefore, a Retail Repo is not regarded by the staff as subject to the borrowing limitations of 12 U.S.C. § 82.

It should be noted that, while Interpretive Ruling 7.1131 covers federal, state and local government securities, the exceptions from the definition of "deposit" contained in Regulations D and Q include only repurchase transactions involving federal government securities. Hence, in structuring a Retail Repo program intended to satisfy the conditions of these provisions, the narrower class of underlying securities should be utilized.

26/ Cf. note 23, supra.