

# Purchased Loan Participations

Directors College Material



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# Background

- Loan participation: sale or sharing of ownership between two or more institutions
- Lead bank administers the loan for the benefit of all participants
- Participation agreement defines roles and responsibilities of lead bank and participant(s)



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# Participation Agreement

- Basic Elements Should Include:
  - Parties involved
  - Total loan amount and amount purchased
  - Loan maturity date
  - Recourse provisions
  - Order of payment (pro rata, first-in, etc)
  - Collateral position
  - Rights and remedies for a breach of contract
  - Servicing responsibilities
  - Basis of revenue and expense distribution
  - Loan documentation responsibilities



# Participation Agreement (continued)

Other considerations:

- Timeliness of information sharing
- Consultation with participants prior to pursuing action on defaulted loans
- Resolution procedures to address disagreements between participants
- Termination provisions



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# Independent Credit Decision

- Prior to purchase, banks should obtain and analyze:
  - Loan closing documents
  - Borrower financial statements and appraisals
  - Any other information needed to make the loan decision
- Loan policy guidance



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# Ongoing Monitoring

- Documentation updates
  - Borrower and guarantor financial information
  - Collateral information
  - Credit memorandum
- Lead bank condition



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# Risks

- Over-reliance on selling institution
- Loss of flexibility
- Inability to obtain timely information
- Loss exposure under workout or liquidation
- Directed purchase from affiliate
- Over-reliance on recourse provisions
- Out-of-territory



# Resources

- Risk Management Manual of Examination Policies, Section 3.2, Loans
- Guidance for Third-Party Risk, FIL-44-2008
- Correspondent Concentration Risks Interagency Guidance, FIL-18-2010



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