

February 1, 2013

To the Chief Executive Officers of all Banks, Bank and Trust Companies, Savings Banks and Savings Associations:

The purpose of this letter is to provide guidance to all banks, bank and trust companies, savings banks and savings associations (together, “Institutions”) regarding the Commonwealth of Pennsylvania Department of Banking and Securities’ (the “Department”) position concerning the calculation of the credit exposure arising from a derivative transaction or a securities financing transaction entered into by an Institution for purposes of determining an Institution’s lending limit pursuant to Sections 306(b)(vi) and 516(b)(vi) of the Banking Code of 1965 (the “Banking Code”), 7 P.S. §§ 306(b)(vi) and 516(b)(vi).

As a matter of background, Institutions are generally pre-approved to engage in derivatives and securities financing transactions in parity with the ability of national banks and federal savings associations pursuant to Section 201(e) of the Banking Code, 7 P.S. § 201(e), and Section 701(a)(22) of the Savings Association Code of 1967, 7 P.S. § 6020-101(a)(22).¹ However, Section 611 of the federal Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”) amended the Federal Deposit Insurance Act to state that an insured state bank may engage in a derivative transaction “only if the law with respect to lending limits of the State in which the insured State bank is chartered takes into consideration credit exposure to derivative transactions.” *See* 12 U.S.C. § 1828(y). A “derivative transaction” for purposes of 12 U.S.C. § 1828(y) is “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.” *See* 12 U.S.C. § 84(b)(3). Section 610 of the Dodd-Frank Act amended the National Bank Act to similarly require national banks to take into account credit exposure to derivative transactions.

Pennsylvania incorporated the requirements of Section 611 of the Dodd-Frank Act into new Sections 306(b)(vi) and 516(b)(vi) of the Banking Code as part of Act 170 of 2012, which became effective December 24, 2012. This allowed Institutions to continue to fully engage in derivatives transactions when Section 611 of the Dodd-Frank Act became effective on January 21, 2013. Sections 306(b)(vi) and 516(b)(vi) of the Banking Code were modeled on Section 610 of the Dodd-Frank Act, which amended the lending limit statute applicable to national banks contained in 12 U.S.C. § 84, in order to allow the Department to be able to interpret the derivative transactions requirements of the Dodd-Frank Act consistent with the interpretations of the Office of the Comptroller of the Currency (the “OCC”) that are applicable to national banks.

¹ The Department reserves the right to restrict or prohibit an Institution from engaging in derivatives and securities financing transactions if the Department determines that engaging in such transactions presents a supervisory or safety and soundness concern.

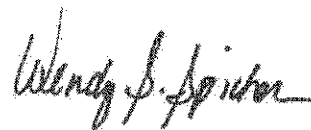
On June 21, 2012, the OCC issued an interim final rule under 12 U.S.C. § 84 amending its existing lending limit regulations contained in 12 CFR Part 32 to comply with the mandate of Section 610 of the Dodd-Frank Act to take into account credit exposures arising from derivative and securities financing transactions as part of the lending limit calculation.² Specifically, 12 CFR § 32.9 contains the rules regarding the calculation of the credit exposure arising from a derivative or securities financing transaction. These amended regulations will be effective on April 1, 2013. Consistent with the Department's goal of interpreting the derivative transactions requirements of the Dodd-Frank Act contained in Sections 306(b)(vi) and 516(b)(vi) of the Banking Code in conformance with the interpretations of the OCC, please be advised that **effective April 1, 2013, the Department will begin reviewing Institutions' credit exposures to derivatives and securities financing transactions under Sections 306(b)(vi) and 516(b)(vi) of the Banking Code in accordance with the requirements of 12 CFR § 32.9.**³ Therefore, you should carefully review and implement the requirements of 12 CFR § 32.9 if you wish to continue to engage in derivatives and securities financing transactions after April 1, 2013.

While derivatives and securities financing transactions can be useful tools for Institutions to use to hedge various risks, they can also be complex activities for an Institution to engage in; as such, you should seek guidance from your legal counsel prior to engaging in any derivatives or securities financing transactions and particularly for help in ensuring that you are properly implementing the requirements of 12 CFR § 32.9 in regard to credit exposures arising from such transactions.

If you currently engage in, or intend to engage in, derivatives and securities financing transactions, please provide a letter no later than March 31, 2013, describing the derivatives and securities financing transactions that your Institution engages in or contemplates engaging in to Robert C. Lopez, Director, Bureau of Commercial Institutions, at the address listed on this letter. This will aid the Department and Federal regulators in efficiently conducting an examination of your Institution.

Should you have any questions regarding this letter, feel free to contact Mr. Lopez at (717) 783-8240 or rolopez@pa.gov. In our supervisory and regulatory role, we at the Department continue to look forward to working with you to make the Pennsylvania state charter the "charter of choice" for financial institutions in Pennsylvania.

Sincerely,



Wendy S. Spicher
Deputy Secretary of Depository Institutions

² A "securities financing transaction" is a "repurchase agreement, reverse repurchase agreement, securities lending transaction, or a securities borrowing transaction." 12 CFR § 32.2(aa).

³ State-chartered savings associations are required to follow 12 CFR § 32.9 in regard to this activity by virtue of 12 U.S.C. § 1464(u)(1).