TO: All State-Chartered Banks  
FROM: Franklin W. Nelson, Bank Commissioner  
DATE: March 6, 2002  
RE: Legal Lending Limit; Loans to Corporate Groups

K.S.A. 9-1104 is the state legal lending limit law. The law was substantially re-written in 1996, and since that time, the number of lending limit questions received by our office has decreased dramatically. One section that all banks do not appear to be aware of, however, is paragraph (f) (4), Special Rules for Loans to Corporate Groups. This memorandum is being provided to bring the provision to your attention, and to explain the way the department applies the statute.

First, paragraph (A) of that section of the statute states:

(A) Loans by a bank to a borrower and the borrower’s subsidiaries shall not, in the aggregate, exceed 50% of the bank’s capital. At no time shall loans to any one borrower or to any one subsidiary exceed the general lending limit of 25%, except as allowed by other provisions of this section. For purposes of this paragraph, a corporation or a limited liability company is a subsidiary of a borrower if the borrower owns or beneficially owns directly or indirectly more than 50 percent of the voting securities or voting interests of the corporation or company.

Examples:

ABC corporation owns 60% of the stock of XYZ corporation. XYZ is a subsidiary for purposes of this provision in the statute, and the bank could not loan more than 50% of its capital to these two entities.

John Brown owns 51% of a limited liability company. The limited liability company is a subsidiary of John for purposes of this provision in the statute, and the bank could not loan more than 50% of its capital to John and the LLC. This example illustrates that because of the way the term “borrower” is defined in the statute, a corporate group may consist of an individual and a corporate entity, rather than two corporate entities.

It is important to note that no determination of direct benefit or common enterprise, as defined in K.S.A. 9-1104 ((f) (1) through (3), is required for the 50% limit to be applicable. In other words, in the first example, a bank could make a loan to ABC corporation, and with appropriate collateral, could go up to 35% of its capital. However, the bank could then only loan XYZ corporation 15% of its capital. This is not because of any determination of direct benefit or common enterprise between the companies, but because the maximum amount that could be lent to the two entities in the aggregate, is capped at 50% by the loans to corporate groups rule in the statute.
Next, paragraph (B) states:

(B) Loans to a borrower and a borrower’s subsidiaries that do not meet the test contained in (f)(4)(A) will not be combined unless either the direct benefit or common enterprise test is met.

This provision means that if a borrower owns something less than 50% of the voting securities or voting interests of an entity, then the 50% aggregate rule does not apply, and these credits would only be combined for lending limit purposes if the direct benefit or common enterprise test is met.

While these provisions have been in the lending limit statute since 1996, we do not believe they are widely understood or even known by bankers. Please keep these provisions in mind in your lending decisions. Feel free to contact your review examiner or the legal staff in this office, or send a general e-mail to the office at bankcomm@ink.org, if you have additional questions.