



Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

February 3, 2011

Interpretive Letter #1129
February 2011
12 USC 29

Mr. James L. Bornhauser
Executive Vice President
Boone County National Bank
8th and Broadway, Box 678
Columbia, Missouri 65205

Re: Request to Make Additional Expenditures on OREO Property

Dear Mr. Bornhauser:

This is in response to the request of Boone County National Bank, Columbia, Missouri (“Bank”), to the Office of the Comptroller of the Currency (“OCC”) to make additional expenditures on a parcel of other real estate owned (“OREO”) pursuant to 12 C.F.R. § 34.86(a). Based upon representations made by the Bank and subject to the limitations in the facts and conditions below, we conclude that the Bank may make the proposed expenditures in order to facilitate the disposal of the OREO.

Twelve U.S.C. § 29 provides that if conditions exist requiring a bank to expend funds for the development and improvement of real estate acquired in satisfaction of debts previously contracted, then a bank “may expend such funds as are needed to enable [it] to recover its total investment.” Judicial interpretations of section 29,¹ the OCC’s regulation implementing section 29,² and OCC interpretations³ have provided national banks reasonable latitude in dealing with their OREO properties. This flexibility available to national banks to deal with OREO property requires good faith on the part of the bank in improving the marketability of OREO property and reducing potential losses within the statutory time period. On the other hand, a bank cannot

¹ *E.g., Cockrill v. Abeles*, 86 F. 505, 511 (8th Cir. 1898) (national bank may purchase other interests in, or discharge encumbrances on, real property acquired in satisfaction of a debt “provided such action is necessary to enable it to manage or dispose of the property to better advantage”).

² 12 C.F.R. § 34.86(a). Although the regulation refers to a development or improvement project, there may be cases “where development or improvement of unimproved land would be reasonably calculated to reduce any shortfall between the parcel’s market value and the bank’s recorded investment amount and would not be speculation in real estate.” 58 Fed. Reg. 46529, 46533 (Sept. 2, 1993).

³ *E.g.,* No Objection Letter No. 87-2, reprinted in [1988-1989 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 84,031 (March 12, 1987) (no objection to bank’s commencing development on OREO, in anticipation of its sale, to preserve zoning, expiration of which would have substantially decreased value).

engage in impermissible real estate speculation under the guise of attempting to recover its investment in OREO property.

Where post-foreclosure, residential ground-up construction is commenced to achieve a greater return from the sale of completed residences than would be provided by available options to dispose of the OREO in its current undeveloped state, such construction is speculative and, therefore, not permissible under section 29. However, if a bank has a basis, other than the desire for a greater return, to construct a limited number of residences on the OREO and thereby facilitate its disposal, such construction may be permissible if the requirements of section 34.86(a) are satisfied. In this instance, we conclude the Bank has a permissible, non-speculative basis for proposing to develop two residential units on an existing OREO parcel.⁴

The Bank acquired the 14-acre OREO parcel in 2007. The parcel includes [] completed and sold residential units, with rights to construct approximately [] additional residential units. Due to the parcel's designation under state law as a condominium, the Bank cannot sell individual lots. Rather, to dispose of the OREO, the Bank must sell the entire parcel. The Bank's marketing efforts have been unsuccessful. From discussions with local real estate agents and builders, the Bank has concluded that additional sales of units likely will generate new prospects for selling the entire OREO parcel to a developer. We find that the Bank's proposal satisfies the three requirements in section 34.86(a) for additional expenditures on OREO. First, as explained above, the Bank's proposal is reasonably calculated to minimize the Bank's loss. Second, the Bank's proposal is not speculative, as discussed above. Third, the Bank's proposal is consistent with safe and sound banking practices. In order to minimize its exposure, the Bank would construct only two units, pre-selling each of the proposed units. Concurrently with construction, the Bank would continue to actively market the OREO parcel. The amount of the proposed construction costs is not disproportionate to the Bank's recorded investment in the property or significant relative to the Bank's capital and surplus.

Accordingly, based on the facts and representations provided by the Bank and subject to the conditions below, we conclude that the Bank may construct two units on its OREO parcel, as described above. The authority to engage in this activity is 12 U.S.C. § 29 and 12 C.F.R. § 34.86, and is subject to the following conditions:

- 1) Prior to commencing construction, the Bank's Board of Directors must make a written determination that the proposed construction is in the best interests of the Bank, complies with the requirements of 12 C.F.R. part 34, and would improve the ability to recover, or otherwise limit, its loan loss.
- 2) The Bank must provide such written determination to its Supervisory Office and must receive written notification of OCC supervisory non-objection to the proposed development, based upon an evaluation of the written determination by the Bank's Board of Directors and any supervisory considerations relevant to the proposed construction.
- 3) Prior to commencing the proposed construction, the Bank must have signed sales contracts for the units. Each sales contract must be with a non-affiliated party, must include an

⁴ The Bank would contract with a local builder to construct the building. The units would be on a portion of the parcel that already has streets, sewers, and utilities. The Bank anticipates that the sale price would fully cover the cost per unit, approximately \$[] to \$[].

adequate earnest money deposit, and must be for an amount that would fully compensate the Bank for the anticipated construction costs. Each purchaser must demonstrate the ability to obtain financing when construction is complete.

- 4) The Bank must continue to exert diligent efforts to dispose of the OREO parcel and must maintain current documentation reflecting that effort.

These conditions are conditions “imposed in writing by a Federal banking agency in connection with any action on any application, notice, or other request” within the meaning of, and enforceable under 12 U.S.C. § 1818. Our conclusions herein are specifically based on the Bank’s representations and written submissions describing the facts and circumstances of the subject transactions, and any change in facts or circumstances could result in a different conclusion.⁵

If you have any questions concerning this letter, please contact Steven Key, Special Counsel, at (202) 874-5300, or Christina Trojan-Masnyk, Special Counsel, at (312) 360-8805.

Sincerely,

signed

Julie L. Williams
First Senior Deputy Comptroller
and Chief Counsel

⁵ This approval and the activities and communications by OCC employees in connection with this approval, do not constitute a contract, express or implied, or any other obligation binding upon the OCC, the United States, any agency or entity of the United States, or any officer or employee of the United States, and do not affect the ability of the OCC to exercise its supervisory, regulatory, and examination authorities under applicable law and regulations. The foregoing may not be waived or modified by any employee or agent of the OCC or the United States.