June 24, 2019

Via Electronic Mail

Chief Counsel’s Office
Office of the Comptroller of the Currency
400 7th Street, S.W.
Washington, D.C.  20219

Re: Other Real Estate Owned and Technical Amendments, (Docket No. OCC-2019-000; RIN 1557-AE50)

Ladies and Gentlemen:

The Bank Policy Institute\(^1\) appreciates the opportunity to comment on the proposal issued by the Office of the Comptroller of the Currency to streamline and improve the clarity of its regulation on other real estate owned (OREO).\(^2\)

The OREO regulatory framework is not often the subject of rulemaking activity. The last update to the OREO regulations was more than twenty years ago. This stability has made sense as, by and large, we believe that the existing OREO framework has served the public interest by supporting bank loss mitigation efforts. Under the framework, national banks are afforded flexibility to carry out those efforts, including by preparing properties for sale or other disposition during the applicable holding period (the generally applicable five-year holding period and any extension period that may be granted).

In the proposal, the OCC notes that, as part of its effort to streamline and improve its OREO regulations (and apply the regulatory framework to OREO activities of Federal savings associations), it has taken stock of additional experience related to OREO gained through the supervisory process and interpretive issues that have arisen since the last update of the OREO regulatory framework. We applaud this approach especially as regulation

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\(^1\) The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation’s leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation’s small business loans, and are an engine for financial innovation and economic growth.

\(^2\) Other Real Estate Owned and Technical Amendments (OCC Docket ID OCC-2019-0004) (the “NPR” or “proposal”).

Although the NPR would revise regulations applicable to both the National Bank Act and the Home Owners’ Loan Act, the recommendations in this letter focus on issues particularly relevant for national banks.

For purposes of this letter, we refer to institutions covered by the proposal as banks, though we recognize that some non-bank financial institutions (federal savings associations) chartered by the OCC are covered as well.
and litigation risks have increased the non-capital costs of originating mortgage loans for banks since the OCC's last significant revision to the OREO regulations.\textsuperscript{3} Banks consider these costs, including the recordkeeping and mandatory disposition requirements of the OREO regulation, in determining whether or not to originate mortgage loans and how to price them. Non-banks now originate 55 percent of all mortgages.\textsuperscript{4} In view of these considerations, it is particularly timely and appropriate to seek public comment on ways to further streamline and improve the OREO regulation.

We believe that the recommendations described below relating to the OREO holding period, OREO-related expenditures and the disposition of OREO are consistent with the statutory language of the National Bank Act and the purpose of the proposal, including ensuring that national banks have sufficient flexibility to successfully carry out loss mitigation efforts in connection with OREO activities.

I. The OCC's regulations should not base the commencement of the OREO holding period on a uniform "bright line rule".

The OCC should continue to rely on state property laws rather than establishing a uniform "bright line rule" (such as an accounting standard test) for when property is acquired.\textsuperscript{5} "Bright line rules" do not capture the nuances of the various state law restrictions on real estate alienability which are essential for purposes of initiating the five-year holding period pursuant to the National Bank Act (in particular, 12 U.S.C. § 29). For example, U.S. accounting rules (U.S. GAAP) do not reflect important state-specific variations and require banks to classify loans as OREO even if the borrower has redemption rights that create a legal right to reclaim the real estate property after foreclosure, thereby creating a problematic inconsistency between U.S. GAAP and the date on which a bank actually acquires the ability to dispose of a property. Disposition is the ultimate goal of the OREO framework and therefore an appropriate trigger for commencement of the holding period.\textsuperscript{6} As a result, the holding period should not start until the redemption period is over. This is consistent with the current OCC approach.\textsuperscript{7} Accordingly, banks already have functioning systems to account for state-specific variations in this regard. We believe that this recommendation closely implements the statutory language and intent of 12 U.S.C. § 29.


\textsuperscript{4} See CFPB Data Point: 2017 Mortgage Market Activity and Trends: A First Look at the 2017 HMDA Data at 63.

\textsuperscript{5} See 12 C.F.R. § 34.82(b)-(c).

\textsuperscript{6} Accounting rules have changed in the past and can change at any time; and FASB is not required to consider the safety and soundness of the U.S. financial system or to promote consistency in the regulation of banks as part of its standard-setting process.

\textsuperscript{7} The current OCC regulation (12 C.F.R. § 34.82) provides flexibility for banks to account for an individual state's property laws, which, in some cases can restrict alienability even after a transfer of title occurs. For example, in a state that has a statutory redemption period, a borrower could pay the bank the principal, interest, and applicable fees etc. on a loan even where the bank has already foreclosed and taken title to the property within a certain statutory period of time, and receive the property back. In such states, even though the bank technically holds title, alienability is restricted during the period of time in which the former borrower could exercise their redemption rights. See 58 Fed. Reg. 46531 (1993) (the OCC’s commentary to the regulation notes that “...the beginning of the holding period should be delayed during the statutory redemption period because, as a practical matter, national banks cannot dispose of OREO subject to a statutory redemption period.”)
II. OCC regulations should be revised to more precisely reflect 12 U.S.C. § 29, which contemplates that the five-year OREO holding period commences only where a bank both holds legal title under applicable state law rules and has possession of the property.

In relevant part, 12 U.S.C. § 29 states that “no [national bank] shall hold the possession of any real estate under mortgage … or the title and possession of any real estate purchased to secure any debts due to it for a longer period than five years except as otherwise provided in this section.” In faithfully implementing the statute, the OCC’s regulations should clarify that the holding period commencement date is the later of the date when title passes to the bank for purposes of state law and the date possession is perfected (i.e., when the bank has acquired the unfettered ability to dispose of the property).

The OREO holding period is currently deemed to begin when “ownership’ of the [DPC] property is originally transferred to a national bank,” as opposed to the transfer of both “title and possession,” as described in 12 U.S.C. § 29. Past precedent and experience suggest that the OCC has evaluated “ownership” largely based on the bank’s interest in the title to a property, rather than also factoring in whether or not the bank holds “possession” of that property.

We believe that “possession,” as used in the statute, can exist only where a bank has, at a minimum, both (1) knowledge of ownership of the property, and (2) the ability to control the property. While such a standard is already implicit in the OCC’s current regulations governing the commencement of the holding period for former bank premises, contained in 12 C.F.R. § 34.82(b)(2)(3), the statutory standard is not fully reflected in regulations governing the commencement of the holding period for DPC property, 12 CFR § 34.82(b)(1). A regulation that hews more closely to the statute by also taking into account the components of “possession” could better address situations—from both a fairness and safety and soundness perspective—including where: (i) a bank is either unaware of the existence of a property that it is otherwise attributed title to due to an error in the recordkeeping practices of a predecessor institution, or (ii) where control of the property is contested in some way by another party.

A. Where eviction proceedings are ongoing, the OREO holding period should not commence until the later of the alienability date and the date on which eviction proceedings are complete and possession of the property is perfected.

Some states have laws requiring various processes for the eviction of tenants (both bona-fide tenants and non-bona-fide tenants such as squatters). When applicable, those laws do not necessarily serve as a barrier to alienability (although they can, in some circumstances); however, they serve as barriers to more practical considerations involved in selling—such as appraisal, inspections, marketing, etc. Further, the possession of the property by a tenant can (especially in the case of a squatter) diminish the property’s value—potentially impacting the bank from a safety and soundness perspective. The OCC should clarify that, in such situations, the holding period will not commence until tenant evictions or similar proceedings have been resolved and the bank’s possession of the property is perfected.

B. Although we generally support the OCC’s proposed clarification that the holding period commences on the acquisition or merger date when a national bank obtains OREO from a merged or acquired institution, the period should not run until the acquiring bank has actual knowledge of its ownership of the OREO property.

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8 See 12 CFR § 34.82(b)(1).
We support the OCC's proposed clarification that when a national bank obtains OREO from a merged or acquired institution, the relevant holding period would commence on the effective date of the merger or acquisition and would not include any period of time the OREO had been held by the acquired institution prior to the merger or acquisition. In cases where the surviving/acquiring institution has knowledge of the transfer of the property in connection with the transaction, we believe the proposal's approach will work well.

However, as described above, we believe that both (1) actual knowledge and (2) control are required for a bank to be found in “possession” of a property for the purposes of the statute. Where a bank is unaware of the existence of a property (e.g., where the property was not included on a predecessor institution's general or OREO ledgers) the bank should not be considered to hold possession of the property sufficient to permit the holding period to commence. This approach would be consistent with previous OCC commentary and interpretation (e.g., in the context of redemption periods and OREO acquired by national banks in a merger, consolidation, or conversion) that the holding period should be delayed where a bank is unable to dispose of OREO “as a practical matter.” Such an approach would not only better align with the statute, but would also better satisfy the interests of fundamental fairness—in that a bank should not be penalized for issues beyond its knowledge or control. We therefore recommend that in such circumstances the holding period not begin to run until such time as the successor to the OREO property becomes aware of its property rights therein (e.g., in the event it receives a tax collection notice or some other form of notice of its ownership).

C. The proposed holding period for properties backed by U.S. government programs should not run until the bank determines that it will no longer attempt to convey the property to the appropriate U.S. governmental agency.

With respect to instances of foreclosure where a loan is secured by a U.S. governmental entity (like the Federal Housing Administration) and the foreclosing institution is acting solely in its capacity as the servicer for the loan, the holding period should not begin to run until the institution determines that it will treat the property as OREO and will no longer attempt to convey the property to the governmental entity. This approach is necessary and consistent with the statutory language, because between the time that the institution forecloses on the property and the time a non-conveyance determination is made, the institution does not have control of an asset underlying an insured loan and is essentially acting as agent for the governmental entity—in that the institution intends only to make a claim and only has the ability to recover the full unpaid principal balance on the loan from the governmental entity. During that period, the institution has no exposure to the value of the real estate collateralizing the loan, and is making a claim for cash rather than proceeding toward disposition of the asset.

III. National banks should continue to have the flexibility to incur additional operating expenses in furtherance of OREO loss mitigation efforts and, accordingly, the OCC should clarify that the list of permissible operating expenses in proposed Section 34.86 is only for illustrative purposes.

The OCC should clarify that the proposed list of permissible operating expenses set out in proposed Section 34.86 is merely illustrative rather than exhaustive. National banks need flexibility concerning the means used to prepare property for sale during the holding period. For example, banks may need to commission surveys, or incur engineering expenses, expenses related to mitigating risks to endangered species, or various property-related legal

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9 See OCC Interpretive Letter N. 633 (Sept. 20, 1993), indicating that “[i]t is not appropriate to engage the holding period during a period when the national bank cannot dispose of the property.” See also 58 Fed. Reg. 46529, 46531 (1993) and note 7 above.

10 The use of the word “including” in proposed Section 34.86 suggests that the OCC intended the list to be illustrative rather than exhaustive.
fees (adjacent owners, easement issues, etc.) among others in order to effectively market and dispose of a particular OREO property. The types of operating expenses that may be appropriate in any given situation are necessarily fact and circumstance-specific and not readily predictable considering all of the potential “real life” situations that banks may face (e.g., atypical properties or unusual real estate conditions). Accordingly, the illustrative list of permissible expenses in the proposal should be construed as just that—illustrative, rather than exhaustive—in order to ensure sufficient flexibility.

IV. National banks should continue to have flexibility in terms of the particular actions that they choose to take to dispose of OREO within the specified holding period without any compliance requirements to meet specific benchmarks during the holding period.

The current rules on disposition appropriately include several alternative methods. We support the proposal’s retention of the existing disposal methods and the addition of a new provision that would allow the disposition of OREO is other ways approved by the OCC to provide for additional flexibility.11

The types of disposition-related actions that may be appropriate for a given OREO property are necessarily fact and circumstance-specific. At times, a national bank’s holding the OREO property for the entire five-year period is necessitated by circumstances involving:

- The current real estate conditions for like properties;
- Applicable rules and restrictions (e.g., zoning requirements) imposed by cities/townships and/or local state agencies;
- Timetables for contractors to complete their work;
- Trust-estates-related issues;
- Appraiser valuations;
- Litigation issues;
- Title issues;
- Easement issues;
- Environmental issues; or
- Endangered species concerns.

New compliance requirements to meet specific benchmarks during the holding period would add an unnecessary cost and burden to bank risk mitigation efforts. Additional regulatory risks presented by this type of requirement (e.g., potentially restricting the ability of banks to effectively negotiate on price for the disposition of OREO as potential purchasers will be fully aware of the bank’s compliance responsibilities) would be taken into account in pricing mortgage loans and could well be counterproductive from a safety and soundness perspective.

The statutory holding period and the OCC’s implementing regulations create important safeguards that provide assurance that banks do not engage in speculative activities. National banks are currently required to make diligent efforts to dispose of each parcel of OREO and maintain appropriate documentation. These existing safeguards render any more specific actions unnecessary and even potentially counterproductive.

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11 The current regulation (12 U.S.C. § 334.83) also appropriately recognizes each of the following disposition approaches: (i) transactions recognized as sales under state real property laws, and (ii) transactions recognized as sales for purposes of applicable accounting standards.
The Bank Policy Institute appreciates the opportunity to comment on the proposal. If you have any questions, please contact the undersigned by phone at 646-736-3960 or by email at gregg.rozansky@bpi.com.

Respectfully submitted,

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