Comptroller of the Currency
Administrator of National Banks

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Interpretive Letter #758
January 1997
12 U.S.C. 29

April 5, 1996

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Dear [ ]:

This letter is in response to our telephone conversations of February 13 and 23, 1996, and your letter dated February 23, 1996. It has come to the attention of the Office of the Comptroller of the Currency ("OCC" or "Office") that the [ ] ("Bank") recently leased to a third party a portion of a large piece of undeveloped real estate that the Bank currently owns in [ ]. As a result, questions have been raised regarding the Bank's ownership and use of this real estate. Your letter, and the OCC's files, indicate that this Office has previously reviewed the Bank's ownership of the real estate in question. Specifically, a letter dated March 12, 1981 ("1981 OCC Letter") from then Regional Administrator Mr. M.B. Adams of the 13th National Bank Regional Office in Portland, Oregon, to the Bank's Board of Directors discusses the Bank's ownership of this real estate. Based on these various sources, my understanding of the facts is as follows.

FACTS

The Bank acquired a 160-acre property (commonly referred to as the [ ] tract) in 1924 in satisfaction of debt previously contracted. The [ ] tract is about a thirty-minute drive from downtown Anchorage and is located on the shore of the [ ] and at the foot of the [ ] Mountains. When the [ ] property was acquired in 1924, the Bank was a Territorial Bank, organized under the laws of the Territory of [ ] until 1950, when the Bank converted to a national charter. Throughout this period, consistent with Territorial Law, the value of the [ ] property had been reduced on the Bank's books to $1.00 and then subsequently charged-off. The property has been used as a picnic ground by bank employees and customer groups since 1958 or 1959. It is my understanding that the Bank does not currently operate a branch facility upon the property.

On June 21, 1976, the Bank changed the classification of the property from other real estate owned ("OREO") to bank premises, based on the increased use of the property as a recreation area for employees and the promotion of bank business. The Bank views the property as a valuable public relations and employee benefit tool. For example, in 1980, 46 organizations requested and were granted permission to use the picnic grounds. Estimated usage of the picnic grounds for that single year was approximately 9,000 people. In addition, your letter mentions that various community groups use the picnic grounds, including the [ ], [ ] Guild, churches, unions, high school reunions, and boy scout troops. You state that the Bank benefits considerably from the goodwill brought by this simple picnic area.

Recently, the Bank leased a 20-acre portion of the [ ] tract to [ ] Company ("Co."). This leased 20-acre portion encompasses a small hill, and [Co.] will pay a royalty to remove the hill. Although not stated in your letter, I understand that the small hill contains granite deposits that may be removed by [Co.]. I assume the royalty payments that the Bank may receive from [Co.] are based upon the amount of granite that is mined from this hill. You represent that the mining of this hill will not interrupt the recreational use of the remainder of the [ ] property. In fact, you state that the removal of the hill will enhance the recreational value of the property. However, it is my understanding that the Bank has received consumer complaints and been the subject of community group protests pertaining to the proposed mining of the hill. Because of federal laws governing national bank ownership and use of real estate, questions have arisen in this Office regarding the Bank's ownership and use of the [ ] tract.

LEGAL ANALYSIS

As you know, a national bank's authority to own real estate is governed by 12 U.S.C. § 29 ("Section 29"). Section 29 provides that:

> A [national bank] may purchase, hold, and convey real estate for the following purposes, and no others:
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> First. Such as shall be necessary for its accommodation in the transaction of its business.
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> Second. Such as shall be mortgaged to it in good faith by way of security for debts previously contracted.
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> Third. Such as shall be conveyed to it in satisfaction of debts previously contracted in the course of its dealings.
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> Fourth. Such as it shall purchase at sale under judgments, decrees, or mortgages held by the [bank], or shall purchase to secure debts due to it.

> But no such [bank] shall hold the possession of any real estate under mortgage, or the title and possession of any debts due to it, for a longer period than five years except as otherwise provided in this section.
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> Notwithstanding the five-year holding limitation of this section or any other provision of this chapter, any [national bank] which on October 15, 1982, held, directly or indirectly, real estate, including any subsurface rights or interests therein, that since December 31, 1979, had not been valued on the books on such [bank] for more than a nominal amount, may continue to hold such real estate, rights, or interests for such longer period of time as would be permitted a State chartered bank by the law of the State in which the [bank] is located. . . .

12 U.S.C. § 29.

As observed in the early case of Union National Bank v. Matthews, 98 U.S. 621 (1875), the purposes of the statute are to ensure the maintenance of liquidity, prevent speculation in real estate, and frustrate the accumulation of large masses of property by national banks. Based on the representations in your letter, the 1981 OCC letter, and your remarks made during our telephone conversations, the Bank is not in violation of Section 29.

Ownership of [ ] Property

Bank Premises

Under Section 29, a national bank may acquire and hold real estate to secure or satisfy debts owed to it or to accommodate the transaction of its business. The 1981 OCC Letter from Regional Administrator Adams to the Bank found no objection to the Bank continuing to hold the [ ] property as part of bank premises. Mr. Adams considered the extensive use of the property by Bank employees, customers, and others, and noted the Bank's representation that the usefulness of the [ ] tract lies in the property's value as an employee benefit and a good public relations builder. Further, Mr. Adams agreed with the Bank's contention that the property has significant promotional value for the bank in the age of increasing competition for retail banking customers.

Based on our phone conversations and your letter, I am not aware of any new or additional facts regarding the property that would warrant a different conclusion from that reached by Mr. Adams in 1981. I will simply note that the OCC's regulations explicitly provide that, pursuant to Section 29(First), real estate necessary to the accommodation of the bank's business includes real estate **other than that upon which the bank buildings are located**. 12 C.F.R. § 7.3005. The OCC's interpretive rulings at 12 C.F.R. Part 7 have recently been revised. See 61 Fed. Reg. 4849 (1996). Revised Part 7 was published in the Federal Register on February 9, 1996, and becomes effective April 1, 1996. Twelve C.F.R. § 7.3005 has been revised and renumbered as 12 C.F.R. § 7.1000. Consistent with Section 7.3005, revised

Section 7.1000 provides that, for purposes of 12 U.S.C. § 29(First), real estate that is necessary for the transaction of banking business **includes property for the use of bank officers, employees, or customers**. See 12 C.F.R. § 7.1000(a)(2)(v).

Twelve U.S.C. § 29(First) does not restrict a national bank to owning or leasing a building sufficient only for its on own current use. The key point is that a bank must hold the property for banking premises and not for real estate speculation. See letter by Deputy Chief Counsel John M. Miller (January 29, 1981) (unpublished). Consistent with the statute and interpretive ruling, the OCC opined as early back as 1973 that a national bank may acquire property to be used for the benefit and convenience of bank employees. See letter by Deputy Comptroller Gwin (August 27, 1973) (unpublished) (stating that a national bank may acquire property, either by purchase or lease, to be used as a day care center for the children of the employees). I am not aware of evidence to suggest that the Bank, in this case, is holding the [ ] tract for speculative purposes. To the contrary, the facts strongly suggest that the Bank, similar to the bank referred to in the 1973 day care letter, has long used the property to accommodate its employees, customers, and various consumer groups. Therefore, the Bank may continue to hold the [ ] property pursuant to the 1981 OCC Letter.

Alaska State Law

Section 29 also permits a national bank to hold real estate for longer than the five-year holding limitation of the section for property acquired to secure or satisfy debt owed to it if the bank held the property on October 15, 1982, and the property was not valued on the books of the bank for more than a nominal amount since December 31, 1979. The national bank may continue to hold such real estate for such longer period of time as would be permitted a state chartered bank by the law of the state in which the bank is located if the aggregate amount of earnings from such real estate is separately disclosed in the annual financial statements of the association.

Section 245 of the Alaska Banking Code provides that:

> All real and personal property not necessary for the convenient transaction or promotion of a banking business under AS 06.05.230 that comes into the possession of a state bank shall be disposed of as soon as possible. If the real or personal property is not sold within the time limit prescribed by the department in regulations, it shall be written off and may not be carried as an asset of the bank.

Alaska Stat. 06.05.245 (1995).

The statute permits a state bank to hold real estate indefinitely so long as it is not valued and carried on the bank's books as an asset. This interpretation is consistent with the State's

Division of Banking, Securities, and Corporations implementing regulations.[1] This provision of Section 29 may also permit the Bank to retain ownership of and hold onto the [ ] property for the period permitted an Alaska state bank, which appears to be indefinitely, so long as the other requirements of the provision are met.

The Bank clearly held the property before October 15, 1982. In addition, it is my understanding that the property had been charged-off as an asset on the Bank's books prior to becoming a national bank in 1950. It is not clear whether the property was reinstated on the books of the Bank at a certain value when the Bank reclassified the property as bank premises in 1976. During our phone conversation on February 13, you had stated that the property was valued by the Bank at a "nominal amount." This being the case, so long as the Bank makes the proper disclosures, if applicable, in the Bank's financial statements, the Bank may also lawfully retain ownership and possession of the [ ] tract pursuant to the provision in Section 29 that refers to state law.

Accordingly, based on the two independent legal reasons discussed above, it is my opinion that the Bank may continue to own and possess the 160 acre [ ] tract property in question. Below, I will discuss whether the Bank may lease a portion of the property to [Co.] for purposes of removing a hill.

Permissible Use of Property

This issue of whether the Bank may lawfully retain ownership and possession of the [ ] tract is separate and distinct from whether the Bank may lease out a portion of the real estate to [Co.] to remove a hill and mine granite deposits. Consistent with Section 29, both the courts and this Office have recognized that it is appropriate for a bank to maximize the utility of its banking premises. Thus, in Brown v. Schleier, 118 F. 981, 983-84 (8th Cir. 1902), aff'd, 194 U.S. 18 (1904), it was recognized that:

> [T]he land which [a national bank] purchases or leases for the accommodation of its business is very valuable, [therefore,] it should be accorded the same rights that belong to other landowners of improving it in a way that will yield the largest income, lessen its own rent, and render that part of its funds which

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[1] Section 135(a) of the Alaska Administrative Code provides that:

> The time limit for disposing of real estate not necessary for the convenient transaction or promotion of a banking business, including property acquired to satisfy loans, is two years from the date the bank receives title to the property. Real property not disposed of within two years shall be written down annually at the rate of 20 percent of the book value at the time of acquisition until the book value is reduced to $10. The book value of the property must remain at $10 until disposed of by the bank. Alaska Admin. Code tit. 3, § 2.135.

> are invested in realty most productive. There is nothing in the National Bank Act, when rightly construed, which precludes national banks so long as they act in good faith, from pursuing the policy outlined above.

Accordingly, a national bank is not restricted to constructing premises that are sufficient only for its own current use. Once a bank has purchased land for the construction of its premises, it may build with an eye toward leasing out the unused portion and thereby lower its operating cost. It is consistent with Section 29, therefore, to lease out portions of a real estate parcel owned by the bank and used in part for bank premises in order to obtain maximum return from the property. The law allows this use when the property remains undivided and assumes that ownership of the entire parcel is for the accommodation of the Bank's business. See memorandum by Andrew Campbell, Attorney, Legal Advisory Services Division ("LASD") (May 4, 1984) (unpublished).

It is also well established that national banks may lease their excess office space to others pursuant to 12 U.S.C. § 29. See Wirtz v. First National Bank and Trust Co., 365 F.2d 641, 644 (10th Cir. 1966). This Office also has concluded that a bank may lease excess space in its lobby and receive rent in the form of a percentage of the volume of sales or gross income from the rented lobby space. Interpretive Letter No. 274 from Brian Smith, Chief Counsel (Dec. 2, 1983), reprinted in Fed. Banking L. Rep. (CCH) ¶ 85,438 ("Smith Letter"); see also Interpretive Letter No. 342 from Peter Liebesman, Assistant Director, LASD (May 22, 1985), reprinted in, Fed. Banking L. Rep. (CCH) ¶ 85,512 ("Liebesman Letter").

The Smith Letter observed that incidental to a national bank's authority to lease its office space is its authority to establish appropriate lease terms based on whatever terms are customary in the leasing of commercial office space. Such terms must be consistent with safe and sound banking practices. Accordingly, the Smith Letter reasoned that a lease to an insurance agency based in part on the volume of sales or gross income is a valid lease for a national bank lessor to make because such leases are currently widespread. Further, participating in such a leasing arrangement did not mean that a bank was engaging in the insurance business or acting as an insurance agent in violation of 12 U.S.C. §§ 92 and 24(Seventh).

Also, the Liebesman Letter, citing the Smith Letter, approved a national bank's leasing of branch space to a travel agency. Warning that the bank could not enter into a partnership or joint venture with the travel agency, the letter cautioned that an inference of partnership arises when the percentage required in a percentage leasing arrangement is too high. Accordingly, this Office advised the bank to include a clause in the leasing contract expressly negating a partnership or joint venture, and expressly precluding any bank liability for the lessee's debts and liabilities. See also letter by William B. Glidden, Assistant Director, LASD (February 10, 1986) (unpublished) (finding that a bank's proposed use of OREO property to store, maintain, and recondition property repossessed by the bank is considered "use in the business of the bank"; letter by John R. Powers, District Administrator, Midwestern District, (December 23,

1986) (unpublished) (concluding that it is not a violation of 12 U.S.C. §§ 29 and 24(Seventh) for a national bank to lease space above its parking garage to a third party for the purposes of erecting an office building).

Based on this authority, it is my opinion that the Bank may properly lease a portion of the [ ] property to [Co.] for removal of a hill. As with the situations described above, the Bank lawfully owns and possesses the [ ] property. Therefore, it may lease out the unused portion to lower its costs and maximize the utility of the land as could other landowners. Furthermore, the lease arrangement with [Co.] whereby the Bank receives royalty payments from removal of the hill and granite deposits is also permissible. However, the Bank should be careful so as to not enter into a partnership or joint venture with [Co.]. Therefore, the leasing agreement should be reviewed by the Bank to make sure that the royalty payments are normal and customary for such agreements consistent with the standards in the Smith and Liebesman Letters.

I trust this letter clarifies this Office's position with respect to the Bank's ownership and use of the [ ] real estate. Of course, my opinions in this letter are based on the facts as I understand them to be and reiterated in this letter. Should any of the facts or representations underlying this opinion differ, the conclusions could change. If you have any questions regarding this issue, please contact me at (415) 545-5980.

Sincerely,

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Jimmy Singh
Attorney