Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

March 2, 2006

Mr. Thomas M. Stevens, GRI, CRB, CRS
President
National Association of REALTORS®
500 New Jersey Avenue, N.W.
Washington, D.C. 20001-2020

Dear Mr. Stevens:

I appreciate the opportunity to continue to address the issues you have raised about three interpretive letters recently issued by the OCC – Interpretive Letters No. 1044, 1045, and 1048. Before responding to the specific points contained in your letter of February 16th, let me re-emphasize several key points. First, the letters in question have nothing to do with banks getting into the real estate brokerage business. Second, we agree that the authority of national banks to invest in real estate is subject to very substantial limitations and constraints and that national banks are not authorized to engage in the real estate development business. Third, because of these restrictions, the activities described in these letters do not breach the traditional separation of banking and commerce.

As reflected in Interpretive Letters No. 1044 and 1045 ("Bank Premises Letters"), the authority of national banks to hold and develop real estate for use as bank premises is circumscribed. The acquisition of real estate for bank facilities must be conducted in good faith in furtherance of a bank's banking operations, and not as a real estate development business. In addition, the proposed use must not be speculative or motivated by realizing a gain on appreciation of the real estate property value. In the Bank Premises Letters, we concluded that each bank demonstrated that the proposed bank premises development was justified by a legitimate business need for accommodation of the bank's business activities.

Interpretive Letter No. 1048 ("Project Financing Letter"), follows precedents that recognize that in limited circumstances, a bank may hold a limited interest in a company or its assets as an integral component of a financing arrangement. Our approval was expressly premised on the bank's interest being structured so as to ensure its economic substance as a loan, rather than a speculative equity investment. In particular, unlike a traditional controlling equity investment, the bank (1) may not participate in the operation of the business receiving the bank's financing; (2) may not realize any gain on the appreciation of the value of its interest in the business or assets held by the business; and (3) must provide in the project agreement many of the same terms, conditions, and covenants typically found in lending and lease financing transactions to protect its interests. Moreover, the interest held by the bank was essential to allow the bank to

capture tax benefits that were enacted to promote the flow of capital to alternative sources of energy.

I will now turn to the particular issues raised in your letter.

The Bank Premises Letters

You raise several points regarding the Bank Premises Letters:

Timeframe for occupancy of premises. You assert that Interpretive Letter No. 1044 does not contain a timeframe for the bank's occupancy of the office space. This is not correct. The bank's occupancy is directly tied to the expiration dates of leases in other buildings. The bank represented that it currently leases a substantial amount of office space in buildings owned by third-parties and that these leases will start to expire in 2013. The Bank projects that development of the proposed premises would commence in 2006, with completion targeted for 2009. The bank expects that it would start moving employees into the new bank premises immediately prior to the expiration of the existing leases and that once the move is complete the bank would occupy at least 25% of the office space in the proposed premises. In addition, the bank anticipates that at least one of its current headquarters complex buildings likely will undergo renovations in the coming years, and the new building would provide the bank with office space for employees displaced by the renovations.

Percentage occupancy. You assert that in Interpretive Letter 1044, the bank's level of occupancy in the proposed premises is 16.7%, not 25%. You reach this figure by including the four floors of residential condominiums, which the bank will not own, in your calculation of bank premises space. As previously explained in my letter of January 31, 2006, even if one were to include the condominium space in the bank premises calculation, the resulting percentage occupancy by the bank is still consistent with case law. *Wingert v. First Nat'l Bank*, 175 F. 739, 741 (4th Cir. 1909), *appeal dismissed* 223 U.S. 670 (1912). Moreover, the bank's sale of excess space in its bank premises is at least as consistent, if not more consistent, with the policies underlying Section 29, than if the bank retained the space and leased it out. Finally, it is useful to note that space in which a bank no longer holds an interest is not fall within the definition of bank premises. *See* 12 C.F.R. §§ 5.37 and 7.1000.

Analysis of the Wingert case. Your letter repeats an assertion that you previously made that this case cannot provide support for our conclusions in Interpretive Letter No. 1044 because *Wingert* stands for the proposition that development of excess bank premises only may occur on property long-held by the bank. As we explained in our previous letter, your analysis misreads *Wingert*.

However, even if there were a requirement that the property be long-held by the bank, that requirement is satisfied here. The bank at issue in Interpretive Letter No. 1044 acquired the property in a series of transactions between 1982 and 1998. The bank in Interpretive Letter No. 1045 acquired the property in question in 1994.

Significance of Brown v. Schleier case. Your letter next contends that *Brown v. Schleier*, 118 F. 981 (8th Cir. 1902), *aff'd*, 194 U.S. 18 (1904), does not offer support for the Bank Premises Letters. We fundamentally disagree. For decades – indeed, for over 100 years – courts have recognized *Brown* as one of the leading, if not the leading, case on the authority of national banks to establish bank premises in excess of their banking needs.

The authority of a national bank to acquire bank premises in excess of its needs and to lease the excess space was directly at issue in *Brown*. The court concluded that a national bank, consistent with the National Bank Act, may acquire and develop bank premises in excess of the bank's needs and may lease to third parties the portion of the premises not needed for banking operations. This holding directly supports both Bank Premises Letters.

Your contention that *Brown* cannot support the Bank Premises Letters because the decision does not indicate a specific percentage occupancy by the national bank is puzzling. *Brown* represents a definitive statement of the authority of a national bank to acquire and develop bank premises in excess of the bank's needs and to lease to third parties the portion of the premises not needed for banking operations.

The significance of this case for this purpose is beyond dispute. *See, e.g., Morris v. Third Nat'l Bank*, 142 F. 25, 32 (8th Cir. 1905), *cert. denied*, 201 U.S. 649 (1906);[1] *Wingert v. First Nat'l Bank*, 175 F. 739, 741 (4th Cir. 1909), *appeal dismissed* 223 U.S. 670 (1912); *Second Nat'l Bank v. U.S. Fidelity & Guaranty Co.*, 266 F. 489, 493 (4th Cir.), *appeal dismissed*, 254 U.S. 660 (1920); *Perth Amboy Nat'l Bank v. Brodsky*, 207 F. Supp 785, 788 (S.D.N.Y.1962) (*citing Brown* for the conclusion that "[i]t is clear beyond cavil that the statute permits a national bank to lease or construct a building, in good faith, for banking purposes, even though it intends to occupy only a part thereof and to rent out a large part of the building to others"); *Farmers' Deposit Nat'l Bank v. W'ern Penn. Fuel Co.*, 215 Pa. 115, 118 (1906).

The OCC also has long recognized *Brown* as the leading court decision on excess bank premises. *See, e.g.*, Interpretive Letter No. 888 (May 14, 2000); Corporate Decision No. 98-26 (Apr. 21, 1998); Interpretive Letter No. 811 (Dec. 12, 1997); No-Objection Letter No. 86-15 (Jun. 6, 1986); Interpretive Letter No. 274 (Dec. 2, 1983).

The *Brown* case also contains important limiting principles that also have long been recognized by the courts and the OCC. The fundamental principle recognized in *Brown* and followed in other cases is that when a national bank acts in good faith to acquire real estate for a legitimate purpose, *i.e.*, for the accommodation of its banking business, the bank may lease or sell the portion of the premises that the bank does not use for its banking business. These are precisely the limitations applied by the OCC in all bank premises proposals, including the Bank Premises Letters. The suggestion that the Bank Premises Letters will permit "national banks to engage in

[1] In *Morris*, the Eighth Circuit noted that "it has been held by this court [in *Brown*] that ... a national bank having a lease of a plot of ground for 99 years may erect thereon a building of *a size largely in excess* of its own immediate requirements for the purpose of renting apartments to others." *Morris, supra* at 32 (emphasis added).

virtually any type of commercial activity that enables national banks to achieve a reasonable economic return, if there is some physical or temporal relationship to bank premises" is simply incorrect.

Meaning of "necessary." 12 U.S.C. Section 29 provides that national banks may purchase, hold, and convey real estate "such as shall be necessary for its accommodation in the transaction of its business." Your letter suggests that "necessary" as used in section 29 means "indispensable" or "absolutely required," such that there is no other alternative. However, the courts have rejected such a narrow construction of this word both in the context of section 29 and in the context of section 24(Seventh), where the term also appears. *See Wells Fargo Bank, N.A. v. Boutris*, 419 F.3d 949 (9th Cir. 2005); *Security Industry Ass'n v. Clarke*, 885 F.2d 1034 (2nd Cir. 1989), *cert. denied*, 493 U.S. 1070 (1990); *M&M Leasing Corp. v. Seattle First Nat'l Bank*, 563 F.2d 1377 (9th Cir. 1977), *cert denied*, 436 U.S. 956 (1978); *Arnold Tours, Inc. v. Camp*, 472 F.2d 427 (1st Cir. 1972); *Morris v. Third Nat'l Bank*, 142 F. 25 (8th Cir. 1905), *cert. denied*, 201 U.S. 649 (1906); *Exchange Bank of Commerce v. Meadors*, 184 P.2d 458 (Okla. 1947); *Trustees of First Presbyterian Church v. National State Bank*, 29 A. 320 (N.J. 1894).[2]

Use of the term "includes." You also assert that where our regulation, 12 C.F.R. § 7.1000, provides that permissible types of bank premises uses "includes" a list of activities, that those activities are an exclusive list of permissible bank premises uses. This construction is inconsistent with the common definition of the term, with well-settled principles of statutory construction,[3] and with how the OCC explained section 7.1000 when the rule was promulgated. Because the term "includes" means "not limited to," the final version of the regulation omitted the phrase "but is not limited to" as unnecessary surplusage in order to simplify the text. *See* 61 F.R. 4849, 4850 (Feb. 9, 1996). As the preamble to the proposed rule explained, "[p]roposed section 7.1000 provides an updated, non-exclusive list of real estate the OCC considers as bank premises for purposes of 12 U.S.C. 29, ..." 60 Fed. Reg. 11924, 11925 (Feb. 3, 1995).

Meaning of "bank premises." Your letter also seems to argue that the interpretation of "bank premises" in the Bank Premises Letters is somehow at odds with the definition of that term in 12

---

[2] The Supreme Court has interpreted a similar concept in the Constitution in the same way:

> Under the "necessary and proper" clause of the Constitution, the quoted words are not limited to such measures as are absolutely and indispensably necessary, without which the powers granted must fail of execution; but they include all appropriate means which are conducive or adapted to the end to be accomplished, and which in the judgment of Congress will most advantageously effect it.

Legal Tender Case, 110 U.S. 421, 440 (1884). *Accord Jinks v. Richland County, S.C.*, 583 U.S. 456, 461 (2003) ("[W]e long ago rejected the view that the Necessary and Proper Clause demands that an Act of Congress be 'absolutely necessary' to the exercise of an enumerated power.").

[3] It is well-settled as a matter of statutory construction that the words "includes" or "including" are not limitations but, in fact, have the opposite effect:

> [T]he term "including" is not one of all-embracing definition, but connotes simply an illustrative application of the general principle.

Federal Land Bank v. Bismarck Lumber Co., 314 U.S. 95, 100 (1941).

C.F.R. § 5.37. This regulation relates to investments in bank premises that require OCC approval under 12 U.S.C. § 371d. However, it is not apparent where the asserted inconsistency lies. Section 5.37(c) provides that "[b]ank premises for purposes of this section *includes* the following: . . ." (emphasis added). As with section 7.1000, discussed above, the term "includes" means "not limited to," precisely to allow for new interpretations in the future. As explained in the Bank Premises Letters, all of the bank properties discussed are permissible bank premises pursuant to 12 C.F.R. § 7.1000 and are bank premises subject to 12 C.F.R. § 5.37.

1997 NationsBank application. Your letter next asserts that Interpretive Letter 1044 is inconsistent with a prior OCC decision not to approve a proposal to develop residential condominiums as bank premises. You refer to a 1997 NationsBank, N.A., request for permission to sponsor the development of a building containing approximately 45 residential condominium units.

The answer here is very simple; the 1997 request did not involve bank premises. Instead, the bank was seeking approval under a now-repealed regulation, former 12 C.F.R. § 5.34(f),[4] to engage, through a "special operating subsidiary," in real estate development that was not permissible for its parent bank, in areas that were "adjacent to or near" bank premises locations of NationsBank. Twelve C.F.R. § 5.34(f) dealt exclusively with activities that were not permissible for a national bank to engage in directly.

You are correct that OCC did not grant that approval, but the OCC response had nothing to do with the proposed development qualifying or not qualifying as bank premises pursuant to 12 C.F.R. §§ 5.37 and 7.1000. The nature and scope of permissible bank premises was not at issue in the 1997 application.

It is useful to note here that the bank submitted an amended request a year later. This amended request did involve bank premises – a complex of office buildings, including a data processing and software development center, two employee parking garages and employee food service and related facilities. This request was approved in Conditional Approval Letter No. 298 (Dec. 15, 1998).[5]

---

[4] The Gramm-Leach-Bliley Act of November 12, 1999, made it clear that operating subsidiaries of national banks could engage only in activities that are permissible for national banks to engage in directly. In response to this statute, the OCC removed section 5.34(f) from its operating subsidiary regulation effective March 11, 2000.

[5] Footnote 2 of this decision observed that a portion of the land would be sold to a third party prior to the bank's development of the remaining portion of the land as bank premises. This sale stemmed from the fact that the residential condominium building would not be part of the bank premises development planned by the bank.

Project Financing Letter

Finally, your letter asserts that Interpretive Letter No. 1048 is a "dramatic step in the direction of eroding the separation of banking and commerce." As I described in detail in my letter of January 31, 2006, the facts of this financing arrangement compellingly demonstrate that this simply is not the case.

First, the Project Financing Letter requires that the bank extend the funds based upon its analysis of the likelihood that the funds would be repaid. Thus, the decision on whether to provide financing to the company would be based upon a full credit review of the transaction made pursuant to the bank's standard loan underwriting criteria.

Second, at the end of the ten year holding period the bank would sell at book value – which is expected to be a small percentage of the bank's original investment – its remaining interest in the LLC. The bank would not share in any appreciation in value of its interest in the wind energy company or the company's assets.

Third, the bank would not participate in operation of the wind energy company, production of the wind energy, and sale of the wind energy.

Fourth, the LLC agreement proposed must contain many of the same terms, conditions, and covenants typically found in lending and lease financing transactions to protect the bank's interests. These terms, conditions, and covenants would include representations and warranties, conditions precedent to the funding pertaining to the mitigation of risks, covenants requiring the company and other investors to provide the bank with customary financial information, and covenants restricting the company from taking certain actions.

Finally, with respect to foreclosure and collateral rights, the bank would be in a similar situation under the project financing as an oil/gas production payment loan. The bank may sell its interest in the wind energy company to minimize or avoid loss on the financing. Alternatively, as proposed, the LLC agreement would give the bank the ability to force a vote to liquidate the wind energy company to minimize or avoid loss on the financing.

Conclusion

I appreciate this opportunity to respond to your concerns. If you have any further questions, I welcome the opportunity to address them.

Sincerely,

Julie L. Williams
First Senior Deputy Comptroller and Chief Counsel