Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

December 5, 2005

Interpretive Letter #1044
December 2005
12 USC 29

Re: Bank Premises Proposal from **[*Bank, City, State*]**

Dear **[ ]**:

This is in response to your request for a legal opinion addressing the proposal by **[*Bank, City, State*]** ("Bank"), to develop a new, mixed-use office building adjacent to the Bank's current headquarters buildings in **[*City*]**. The Bank would use and hold the building as bank premises. For the reasons discussed below and based upon the representations made by the Bank, we find that the Bank's proposal is permissible under 12 U.S.C. § 29.

Bank's Proposal

The Bank's corporate headquarters complex currently consists of two adjacent office buildings that occupy a portion of one city block in downtown **[*City*]**. The Bank uses 100% of the space in the first building and approximately 92% of the space in the second building. In addition, the Bank leases substantial office space in other nearby office buildings. The Bank's various leases for this office space start expiring in 2013.

The Bank now proposes to construct a third building ("Proposed Premises") to provide the Bank with additional office space in an expanded headquarters complex. The Bank expects that the office space in the Proposed Premises would provide the Bank with ability to move Bank employees from the leased office space in the nearby buildings to the Bank's headquarters complex. 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 Proposed Premises would provide the Bank with office space for employees displaced by the renovations.

The Proposed Premises would be built adjacent to the Bank's current office buildings and on property currently held by the Bank as bank premises. The Bank anticipates that development of the Proposed Premises would commence in early 2006, with completion targeted for early 2009.[1]

For the reasons described below, the Bank proposes that the Proposed Premises would be a mixed-use building. As proposed, the building would have ground level retail and restaurant space, twelve floors of office space totaling approximately 360,000 square feet, five floors of hotel space (158 rooms), and four floors of condominiums (32 units). The condominiums would be sold through an unaffiliated real estate broker and, once sold, the Bank would retain no ownership interest in the top four floors of the building.[2]

Once the Proposed Premises is completed, the Bank initially expects to occupy a small percentage of the office space.[3] As the Bank's leases expire in other office buildings and as the Bank renovates one or both of the current buildings, the Bank anticipates moving additional employees into the Proposed Premises. In the years immediately following the expiration of the Bank's leases in other office buildings, the Bank projects that it would occupy approximately 100,000 square feet of office space in the Proposed Premises, or approximately 25% of the available office space. Over time, the Bank anticipates that its occupancy of office space in the Proposed Premises may increase.

With respect to the hotel space, the Bank would contract with a national hotel management company to manage and operate the hotel on a day-to-day basis. The hotel would be of a business class quality appropriate for and competitive in downtown **[*City*]**.[4] The Bank would place a substantial majority of its visiting employees, officers, directors, and customers in the hotel and would commit to occupying a certain number of room-nights per year in the hotel. Based on its 2004 figures, the Bank projects that it would occupy approximately 10% of the room-nights available in the hotel on a yearly basis and that, during certain times throughout the year, the Bank may occupy a larger percentage of the rooms. In addition, the

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[1] The Bank is authorized to invest in bank premises under 12 U.S.C. § 371d and 12 C.F.R. § 5.37. The Bank does not need to file an application or notice with the OCC because its aggregate investment in bank premises does not approach the amount of the Bank's capital stock and surplus. *See* 12 U.S.C. § 371d(a)(2) and 12 C.F.R. § 5.37(d)(1). As of September 30, 2005, the Bank's aggregate investment in bank premises was approximately $1.2 billion, and the Bank's capital and surplus was approximately $6.3 billion.

[2] The Bank employed a real estate consulting group to study the market for residential condominiums in downtown **[*City*]**. The consulting group concluded that the downtown market would support between 28 and 36 residential condominiums as part of the Proposed Premises and that all condominiums would be sold within two to three years of completion of a model sales unit.

[3] The Bank has an informal agreement with a prospective tenant for that tenant to occupy five of the twelve floors of office space. The Bank would have a right of first refusal to lease the remaining office space.

[4] The Bank hired a hospitality consulting firm to study the hotel market in downtown **[*City*]**. The consulting firm concluded that the downtown market would support a business class hotel with approximately 160 rooms and that such hotel would achieve, and thereafter maintain, an occupancy rate of 72% – the industry standard – within three years of operation.

Bank will make use of the hotel's conference facilities when it requires additional meeting space or off-site meeting space.[5]

The Bank's decision to develop the Proposed Premises as a mixed-use building is driven by two factors. First, the Bank believes that the specific combination of office, hotel, and residential space described above is the combination of uses that makes the building economically viable in the downtown **[*City*]** market. For example, revenue generated from including a hotel and selling the condominiums is important to financing the construction of the building, and several of the state and local economic benefits are related to one or more of the mixed uses.

Second, the Bank views the Proposed Premises as an important part of a rejuvenation effort for downtown **[*City*]**. Such an effort benefits the Bank by protecting the value of the Bank's current headquarters buildings and enhancing the Bank's brand and image, especially in light of the fact that the to-be-developed lots currently have run down, dilapidated buildings. In addition, complementary development by unrelated third parties may take place in the block across the street from the Proposed Premises.

Discussion

A national bank's authority to own real estate is governed by 12 U.S.C. § 29. Section 29(First) provides that a national bank may purchase, hold, and convey such real estate "as shall be necessary for its accommodation in the transaction of its business." Consistent with section 29, the bank's activities must be conducted in good faith, that is, for banking purposes and not in a speculative manner. Section 29's limitations are designed "to keep the capital of the banks flowing in the daily channels of commerce; to deter them from embarking in hazardous real estate speculations; and to prevent the accumulation of large masses of such property in their hands, to be held, as it were, in mortmain."[6]

However, section 29 does not prohibit a national bank from owning or leasing a building larger than its current needs dictate. Both the OCC[7] and the courts[8] have recognized that it is appropriate for a bank to maximize the utility of its banking premises. For example, in *Brown v. Schleier*, the court stated:

> If the land which [a national bank] purchases or leases for the accommodation of its business is very valuable, 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

[5] The Bank anticipates that its percentage usage of the hotel's conference facilities would be consistent with its percentage usage of the hotel's rooms.

[6] *Union Nat'l Bank v. Matthews*, 98 U.S. 621, 626 (1879).

[7] *E.g.*, Interpretive Letter No. 1034, *reprinted in* [Current Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81-563 (Apr. 1, 2005).

[8] *Brown v. Schleier*, 118 F. 981 (8th Cir. 1902), *aff'd*, 194 U.S. 18 (1904); *Perth Amboy Nat'l Bank v. Brodsky*, 207 F. Supp. 785, 788 (1962).

> rent, and render that part of its funds which are invested in realty most productive. There is nothing, we think, in the national bank act, when rightly construed, which precludes national banks, so long as they act in good faith, from pursuing the policy above outlined. *Id. at 984.*

The basic requirement, therefore, is that the Bank's development of the Proposed Premises must be done in good faith, that is, for banking purposes and not in an effort to violate section 29. Once the banking purposes have been established, section 29 permits the Bank to maximize utilization of the Proposed Premises. The *Brown* decision continued:

> When an occasion arises for an investment in real property for either of the purposes specified in the statute, the national bank act permits banking associations to act as any prudent person would act in making an investment in real estate, and to exercise the same measure of judgment and discretion. The act ought not to be construed in such a way as to compel a national bank, when it acquires real property for a legitimate purpose, to deal with it otherwise than a prudent landowner would ordinarily deal with such property. *Id.*

National banks may maximize the utility of their banking premises by leasing excess premises to third parties.[9] In addition the OCC previously has concluded that, consistent with section 29, a national bank may develop a bank premises building and sell some of the excess space (in contrast to leasing all of the excess space).[10]

In this instance, we conclude that the Bank is acting in good faith. The property upon which the Bank would develop the Proposed Premises currently is held by the Bank as bank premises. Given the Bank's near total use of its current headquarters buildings and the upcoming expiration of leases for substantial space in other buildings, the Bank has a demonstrated need for additional office space. The Bank expects that it would start moving Bank employees into the Proposed Premises immediately prior to the expiration of its existing leases, with the Bank anticipating that shortly thereafter it would occupy at least 25% of the office space.[11] Moving Bank employees from leased space into the Bank's headquarters complex would reduce the Bank's annual expenses to lease office space elsewhere and to transport employees between the current headquarters buildings and the leased office space.

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[9] Interpretive Letter No. 1034, *supra* (bank to lease approximately 78 percent, and possibly as much as 89 percent, of space in bank premises to third parties); Conditional Approval No. 298 (Dec. 15, 1998) (bank to lease as much as 75 percent of space to third parties).

[10] OCC Interpretive Letter (Aug. 14, 1985) (published in Lexis-Nexis) (under section 29, bank permitted to develop portion of new bank building as office condominiums and sell the condominiums).

[11] Bank premises includes real estate held for use as future bank premises. *See* 12 C.F.R. § 7.1000. Twelve C.F.R. § 34.84 provides that a national bank "*normally* should use real estate acquired for future bank expansion within five years." (emphasis added) The language of section 34.84 suggests a degree of flexibility in the timeframe for use of future bank premises. For example, there may be a need to permit a bank to construct a building, then immediately lease most of the space for non-bank tenants but to occupy an increasing percentage of the building over the useful life of the building. *Compare* 12 C.F.R. 7.5004(b)(2) (excess electronic capacity based on future anticipated growth).

The Bank also has established that development of the Proposed Premises as a mixed-use building is necessary to make such development economically viable in the downtown **[*City*]** market. Revenue generated from including a hotel and selling the condominiums is important to financing the construction of the Proposed Premises, and several of the state and local economic benefits are related to the inclusion of one or more of the mixed uses. Moreover, the Bank believes that the mixed use nature of the Proposed Premises will aid in the rejuvenation of downtown **[*City*]**, which in turn would protect the value of the Bank's current headquarters buildings. The Proposed Premises also is consistent with development that may take place in the block across the street from the Bank's headquarters.

With respect to the hotel, the Bank has demonstrated both a need to include hotel space in the Proposed Premises and a need for such space to lodge its visiting employees, officers, directors, and customers. Given these needs, the Bank does not propose to create more hotel space than is consistent with legitimate banking purposes. The size of the hotel, at 158 rooms, is driven by conclusions derived from an analysis of the downtown **[*City*]** market. In addition, the Bank anticipates using approximately 10% of the hotel's room-nights annually and, periodically as a result of the Bank's business, the Bank anticipates that its visitors may occupy a larger percentage of the hotel's rooms.[12]

Overall, the Bank anticipates that it would occupy approximately 22% of the office and hotel space in the Proposed Premises. This level of usage exceeds what has been expressly permitted in the case law on bank premises. Therefore, under these circumstances, we find that the Bank may lease the excess office and hotel space to third parties in order to maximize the utility of its premises.[13]

With respect to the four floors of condominiums that the Bank would sell, the Bank represents that including the development of these condominiums for sale is necessary to make construction of the Proposed Premises economically viable. As discussed above, once bank premises property is acquired in good faith, national banks should be treated like any other landowner and permitted to make best economic use of property. If including the condominiums is necessary to the economic viability of the development of the Proposed Premises, then their construction and sale should not be prohibited by 12 U.S.C. § 29.[14] Indeed, when viewed in light of the purposes underlying section 29,[15] it seems reasonable to conclude that the sale of excess space in the Proposed Premises also is consistent with these enunciated purposes. Such a sale of

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[12] OCC Interpretive Letter, dated July 8, 1993 (to be published) (national bank that permissibly maintains residential condominium as lodging for use of visiting auditors, consultants, and customers may rent condominium when not being used by such visitors as means of offsetting lodging's expenses); OCC Interpretive Letter, dated January 21, 1993 (to be published) (given scarcity and cost of other commercial lodging, bank may maintain residential condominium for use of outside consultants, auditors, and customers).

[13] *See* note 9, *supra.*

[14] *See* note 10, *supra,* and accompanying text.

[15] *See* note 6, *supra,* and accompanying text.

excess space would enable the Bank to keep its capital flowing in commerce and would reduce the amount of property held by the Bank "in mortmain."

Conclusion

Based upon the information and commitments you provided, we find that the Bank's proposal to develop the Proposed Premises is consistent with 12 U.S.C. § 29. If you have any questions, please contact Steven V. Key, Senior Attorney, Bank Activities and Structure Division, at 202-874-5300.

Sincerely,

signed

Julie L. Williams
First Senior Deputy Comptroller
and Chief Counsel