Getting Back in Gear:
Finding Ways to Move Stalled and Vacant Foreclosures Forward

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Overview

• OCC regulatory expectations for managing properties in default and foreclosure

• Public Welfare Investment authority

• CRA and stabilization-related activities
OCC Regulatory Expectations

- Comptroller’s Handbook—Other Real Estate Owned

- Outlines 8 categories of risk:

<table>
<thead>
<tr>
<th>Credit</th>
<th>Interest rate</th>
<th>Liquidity</th>
<th>Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operational</td>
<td>Compliance</td>
<td>Strategic</td>
<td>Reputation</td>
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- Explains bank/thrift requirements for management of properties in default as:
  - Owners
  - Servicers, or
  - Securitization trustees
Holding Period Restrictions

• Time restrictions on holding OREO—
  – Dispose as soon as prudent judgment dictates, but must dispose within 5 years
    • Holding period begins once ownership of property transfers or a redemption period ends
    • OCC may approve extension up to an additional 5 years, if earlier disposition detrimental
  
  – Rental for reasonable period (1 year or less) as part of prudent disposition strategy
    • Must have appropriate risk management framework
    • Document reasonable ongoing sales efforts
Minimum Obligations as Owner

• Assume former owner’s responsibilities for—
  – Maintenance and security
  – Payment of taxes and insurance
  – Determine upkeep, maintenance, and security requirements imposed by localities, including homeowners’ associations
  – Duties as landlord, if rental property
    • Protecting Tenants at Foreclosure
• Determine if Servicemembers Civil Relief Act protections apply
• Following foreclosure, record ownership interest
• Register property with locality, if required
• OREO appraisal and accounting requirements
Additional Issues

• Sufficient staff to manage foreclosed property portfolio
  – Policies/procedures to manage 3rd party relationships

• When disposing of foreclosed properties, consider:
  – Disposition costs and delays
  – Provision of financing
  – Negative reaction and potential reputation risk of policies that favor cash buyers over owner-occupants that need financing
  – Opportunities to participate in land bank programs, neighborhood stabilization, redevelopment programs, anti-blight programs, or to enhance owner-occupancy
Releasing a Lien Rather Than Foreclosure

• May decide to release lien due to financial considerations, e.g. cost exceeds market value
  – Ensure valuation provides best information
  – Abandoned property has potential reputation and legal risk

• Lender or servicer must:
  – Notify or attempt to notify borrower—
    • Not pursuing foreclosure and mortgage lien has been released
    • Borrower may continue to occupy property
    • Borrower is obligated to maintain property, pay taxes, and the debt is still owed
  – Make appropriate notifications to local jurisdiction
Servicer

• Obligations—
  – Advance funds for taxes, insurance, HOA dues
  – Maintenance, security, serving as landlord for rentals, and marketing property
  – Routine upkeep
  – Register vacant or foreclosed properties, if required
  – PSA or servicing documents outline specific responsibilities

• Additional Issues—
  – Sufficient staffing and 3rd party vendor oversight of property management
  – Rehabilitation or improvement should comply with local building codes, licensing requirements, and requirements in servicing agreements
  – When disposing of foreclosed properties, consider:
    • Contractual requirements for valuing and marketing properties
    • Even if following requirements, may involve reputation and litigation risks
    • Legal authority for OREO expenditures and meet FHA requirements
    • Opportunities to participate in land bank programs, neighborhood stabilization, redevelopment programs, anti-blight programs, or to enhance owner-occupancy
Securitization Trustee

- Primary responsibilities—hold lien on trust assets for investors’ benefit and administer trust in conformance with PSA, trust agreement, or indenture

- Be aware of potential reputation and litigation risk, because trustee is named as secured party in foreclosure

- As permitted by PSA, trustee should work with servicer to ensure performance
Public Welfare Investment

- Use Public Welfare Investment authority to make a grant by transferring OREO properties:
  - To a Community and Economic Development entity for rehabilitation and sale or lease to LMI
  - To bank subsidiary Community Development Corporation
    - Must seek prior written approval from the OCC
    - Current appraisal must document FMV at time of transfer
    - OCC will review whether CDC (or a CEDE) has or can develop property management experience to rehabilitate and lease or sell properties
  - Post-transfer, properties not subject to 5-year holding period limit
Public Welfare Investment

• Use Public Welfare Investment authority to:
  — Make investments in community development entities that will rehabilitate and sell or rent properties to LMI individuals
  — Transfer OREO properties to a bank subsidiary Community Development Corporation
    ▪ Must seek prior written approval from the OCC
    ▪ OCC will review whether CDC (or a CEDE) has or can develop property management experience to rehabilitate and lease or sell properties
    ▪ Post-transfer, properties not subject to 5-year holding period limit
• Current appraisal must document FMV at time of transfer
CRA and Community Stabilization

- Large Banks and Intermediate Small Banks (ISBs) can get CRA consideration for certain OREO disposition activities.
  - Investment
  - Lending
  - Services

Must have community development purpose
CD Investment Test

• Property donation or below-market disposition of OREO or nonperforming notes

• CRA consideration for difference between fair market value (FMV) and the discounted disposition price of the property/note
CD Lending

• Loans to LMI borrowers to purchase or rehabilitate foreclosed properties
• Loans to nonprofit organizations serving primarily LMI housing or other community development needs for affordable housing acquisition or rehabilitation
• Loans to financial intermediaries, including CDFIs, CDCs or community loans funds/pools that primarily lend to (or facilitate lending to) promote community development
• Loans to state and local governments for community development activities
- Capacity building for non-profit organizations

- Banks can offer technical services, such as:
  - Lending employees to a qualified community development organization
  - Providing management training or financial consulting to help organizations with their acquisition or rehabilitation activities
  - Provide assistance with marketing financial services, including development of advertising or promotions
Expanded Definition of Community Development

• Amended definition of community development in §__12(g)(5) provides consideration for loans, investments, and services for projects or activities that meet “eligible uses” criteria and relate to approved NSP plans
  – Must be in designated target areas
  – Must be provided no later than two years after last date appropriated funds are required to be spent
  – May be outside AA as long as needs of AA are adequately addressed
  – Key change – may benefit middle-income borrowers or geographies
Expanded Definition of Community Development

- Expanded CD definition applies to “eligible uses” under NSP:
  - Financing mechanisms for foreclosed properties
  - Purchase & rehabilitation of abandoned or foreclosed homes & residential properties
  - Land banks for foreclosed properties
  - Demolition of blighted structures
  - Redevelopment of demolished or vacant properties
Questions