

**STATE OF LOUISIANA
OFFICE OF FINANCIAL INSTITUTIONS
BATON ROUGE, LOUISIANA**

Revised Effective March 14, 2005

**POLICY NO. DI-01-2005
(B,SB,SL,HC)**

**[Rescinds Policy Nos.
B-02-95, SB-02-95,
SL-02-95]**

INVESTMENT IN REAL ESTATE FOR BUSINESS PURPOSES

- I. **PURPOSE:** The purpose of this policy is to provide guidance regarding the acquisition, holding, and disposition of real property to be used, currently being used, or formerly used in the proper transaction of a bank, thrift, or holding company's business.
- II. **APPLICABILITY:** This policy applies to all state-chartered banks, thrifts, holding companies, and their subsidiaries.
- III. **GENERAL**

In general, Louisiana Banking Law (LBL)¹ allows a state bank or thrift to lawfully purchase, hold, and convey any immovable property which is necessary for the proper transaction of its business. After consideration is given to the guidance included in this policy, an apparent violation of these statutes may be cited if a bank or thrift acquires excessive property which is not necessary for the proper transaction of its business.

If there is any question that the proposed acquisition may be in contravention of this policy and may jeopardize the ability of an institution to expand as it intends, the institution should contact this office for guidance.

A. **Future Use**

Management is expected to document its future expansion plans in the institution's strategic plan or in its board minutes, with the plans made at a board meeting transferred to the strategic plan as the plan is updated. Plans should identify the specific market areas in which the institution is interested in expanding in the future. As circumstances change, the strategic plan should be updated. Also, if an institution has any branches, it must have a branch closing policy in place in accordance with the Interagency Policy Statement Concerning Branch Closing Notices and Policies.

¹ LSA-R.S. 6:243(A)(1) for banks and thrifts. This section was made applicable to savings banks in 6:1229.1 and savings and loan associations in 6:822(3)(d).

B. Investment Limitations

In accordance with LAC 10:I.1101, which became effective on November 20, 2004, institutions should limit their investment in fixed assets to no more than 50 percent of Tier 1 capital plus the allowance for loan and lease losses (ALLL) for existing institutions or 45 percent for new institutions². Fixed assets held at a bank-owned subsidiary should be consolidated into this amount, but fixed assets held at the holding company or a subsidiary of the holding company should not be consolidated into this amount to calculate total investment in fixed assets. Any deviation from this limitation will require the prior approval of this office. A request for an exception to this limitation should be addressed to the Commissioner and include specific plans for achieving compliance within a reasonable period of time.

C. Acquisition of Additional Property

For an institution with a composite CAMELS rating of 1 or 2 or one with at least a Satisfactory CRA rating, prior regulatory approval is **unnecessary** to acquire property to be used for legitimate business purposes³. However, prior approval of this office **is** necessary before any institution may establish a new branch office, open a loan production office, or relocate a main or branch office; the prior approval of the primary federal regulator may also be necessary in these cases. Institutions considered to be in troubled condition⁴ or with a less than satisfactory CRA rating are **required** to obtain the prior approval of the Commissioner before acquiring any property or an option to purchase any property.

For an institution purchasing an existing structure (through direct acquisition or DPC) or constructing a new building, at least 50 percent of the facility should be utilized at the date of acquisition. If an institution will be utilizing less than 50 percent at acquisition, a specific plan for achieving this utilization rate must be submitted and approved by the Commissioner **prior** to the acquisition of the property. The transaction **may** be permitted if at least a 25 percent utilization rate is initially achieved and 50 percent utilization will be reached within a reasonable period of time. In addition, the Commissioner may grant exceptions to this section of the policy if the

² New institutions are those that have been in existence for less than three years.

³ A 'legitimate business purpose' **does not** include investment in real estate for development. A general discussion on whether or not an investment in real estate would be considered as being used for development is included in the following paragraphs and depends on the utilization rate of an existing structure or the reasonableness of property held for future expansion.

⁴ An institution is considered to be in "troubled condition" as defined in LSA-R.S. 6:121.4(D). In general, an institution in 'troubled condition' includes an institution (1) with a composite rating of 4 or 5, (2) that is subject to a proceeding to terminate or suspend deposit insurance, (3) that is subject to a cease and desist order or written agreement issued by either the commissioner or the appropriate federal regulatory agency that requires action to improve the financial condition of the financial institution or holding company, or (4) that is informed by the commissioner or the appropriate federal regulatory agency that it is in troubled condition.

institution's overall financial condition is **very strong** and its investment in fixed assets will remain **relatively low** following the transaction. Proper documentation of the initial occupancy rate and support of a 50 percent occupancy rate within a reasonable period of time should accompany the request.

The purchase of a vacant tract of land which is in excess of the amount of property necessary for the reasonable completion of a project and any reasonable future development needs is not allowed unless the institution has a written commitment to sell the excess property simultaneously with the acquisition or within a short term. Failure to do so will result in a violation of LSA-R.S. 243.

Part 323 of the FDIC's Rules and Regulations (for state nonmember banks and savings banks), Section 225.61 et seq. of Regulation Y (for state member banks), and Part 564 of the OTS' Rules and Regulations (for savings and loan associations) requires an USPAP-conforming appraisal performed by a Louisiana certified GENERAL real estate appraiser whenever property is purchased in excess of \$250,000. Appropriate estimates of value should be obtained on parcels valued at less than \$250,000 in accordance with these regulations.

D. Leasing Property for a Branch Office

If a financial institution leases property for a branch location, the lease contract must allow the institution to comply with LSA-R.S. 6:507 for banks and savings banks and 6:853 for savings and loan associations.

E. Purchases of Property in Excess of Appraised Value

An institution may purchase property at a price that is within 110% of the appraised value without the prior approval of the Commissioner. In these cases, the board minutes should adequately document the reason(s) why the purchase price was in excess of fair market value. If the purchase price exceeds 110% of the appraised value, the institution must obtain the Commissioner's prior approval. The request for prior approval should be addressed to the Commissioner and include a full justification for paying the premium.

F. Insider Transactions

If a director, executive officer, or 10 percent or larger shareholder (insider) has any involvement in the acquisition of property to be used as premises, the prior written approval of the Commissioner is required. Involvement may include, but is not limited to, being the seller, acting as the real estate agent, being the closing attorney, etc. Additionally, if an insider renders any

services with respect to the transaction, the institution must maintain a detailed breakdown of the costs of those services.

Management and the Board of Directors should ensure that the acquisition of property for future expansion is not to the detriment of the financial institution. Failure to do so may constitute an unsafe and unsound practice and result in the institution being cited in apparent violation of LSA-R.S. 6:291(A) for banks and bank holding companies, 6:786(A) for savings and loan associations, and 6:1190(A) for savings banks.

While in rare instances an exception may be justified, institutions are strongly encouraged to refrain from entering into any lease arrangements that may involve insiders.

G. Holding Period for Future Expansion Property

Property purchased for future expansion may be carried as premises for up to five years at the bank or thrift level and for a reasonable period of time, as determined by the FRB, at the holding company level. However, immediate transfer to Other Real Estate Owned (OREO) is required under either of the following conditions:

1. Construction or utilization as premises has not begun at the end of the five-year period for banks and thrifts and as determined by the FRB for holding companies.
2. The institution's plan for use as premises is abandoned.

H. Contiguous Property⁵

From time-to-time, adjacent or contiguous property may become available to an institution. However, before the institution acquires adjacent or contiguous property, the institution must ensure compliance with the investment in fixed assets limitation, consistency with its strategic plan, and properly document its deliberations regarding the reasonableness of the acquisition. Contiguous property acquired at the bank or thrift level for the purpose of future expansion is not subject to any holding period.

I. Branch Closures

In order to close a branch office, an institution must be in compliance with LSA-R.S. 6:507 for banks and savings banks and 6:853 for savings and loan associations as well as its branch closing policy.

J. Property Formerly Used as Premises or for Future Expansion

⁵ Contiguous property includes property across the street from the institution's property.

Property that is no longer used as premises or for which the institution no longer has plans to utilize for future expansion must immediately be transferred to Other Real Estate Owned (OREO) and treated as OREO in accordance with LSA-R.S. 6:243(B) and (D) for banks and thrifts. A well-documented estimate of value must support the value of the property (the lower of acquisition cost or market) at the time of transfer.

Once the property is no longer being used for the proper transaction of an institution's business or the institution no longer wishes to use the property for future expansion, the transfer of the property to the holding company will not satisfy the requirement to divest. A holding company may not invest in real estate for purposes other than the proper transaction of its or its bank/thrift subsidiary's business. If the property is not being operated as an ongoing business, divestiture may be accomplished by writing the property down to \$1 and transferring it to a subsidiary of the bank or thrift in accordance with LSA-R.S. 6:243(D)(1).⁶

If the facility is on leased property, upon closure, the institution may continue leasing the property through the current term of the lease. However, the lease may not be renewed or extended. The institution may sublease the property during the remainder of the current term of the lease.

K. Acquisitions Requiring Prior Approval

1. In determining whether prior approval is necessary, the institution should consider the following:
 - a. Will the institution's ratio of fixed assets to Tier 1 capital plus the ALLL exceed the investment in fixed assets limitations set in LAC 10:I.1101 after the acquisition? [See Section IIIB on p. 2 of this policy.]
 - b. Is the institution in troubled condition or did it receive less than a satisfactory rating at its last CRA examination? [See Section IIIC on p. 2 of this policy.]
 - c. Will the institution utilize at least 50 percent of the building at time of acquisition? [See Section IIIC on pp. 2 and 3 of this policy.]
 - d. Is the purchase price for the property in excess of 110% of the appraised value? [See Section IIIE on p 3 of this policy.]
 - e. Does the transaction involve an insider? [See Section IIIF on pp. 3 and 4 of this policy.]

If there is any question that a proposed acquisition of property may be unreasonable or in non-compliance with this policy, the institution should contact this office for guidance.

⁶ Guidance regarding what constitutes the operation of an 'ongoing business' will be included in our OREO Policy.

2. If prior approval is necessary, the institution must submit the following information:
 - a. A pro-forma balance sheet that reflects the institution's investment in fixed assets (detailed to show land, building, and FF&E) at the time of purchase, at the end of that calendar year, and at the following two calendar year-ends. In addition, if any additional changes to the premises account (sale of a branch, closure of a branch, etc.) or any additional injections of capital are contemplated, the financial statements should reflect these amounts and a footnote explanation.
 - b. The type of facility intended (e.g., full service branch, loan production office, operations center, etc.) and the projected time frame for utilization of the property.
 - c. The terms of acquisition (e.g., available cash, lease/purchase or mortgage financing). If other than a cash sale, provide a copy of the contract or agreement to be executed.
 - d. Full disclosure of any transactions involving insider(s). This would include an itemized listing of any carrying costs or other expenses relating to the purchase price of the property.
 - e. A copy of the appraisal. If the proposed purchase price is 110 or more of the appraised value of the property to be acquired, provide a full explanation for the payment of any premium above appraised value.
 - f. If less than 50 percent of the structure to be acquired will be utilized by the institution, provide a detailed estimate of the utilization percentage as well as the estimated timeframe within which a 50 percent utilization rate will be achieved. A minimum utilization rate of 25 percent must be achieved initially.

L. Prospective Treatment

The requirements of this policy shall apply prospectively from the date of this policy. The guidance contained in this policy is not intended to change or modify any existing agreements between this office and a bank, thrift, or holding company.

M. Contraventions of this Policy

Compliance with this policy will be reviewed at on-site examinations. Any contravention(s) as well as any apparent violation(s) of law will be cited in the Report of Examination.

N. Exceptions

Any exception to this policy requires the prior written approval of the Commissioner.

John Ducrest
Commissioner of Financial Institutions

Date

Attachments:

1. LSA-R.S. 6:243 (<http://www.ofi.state.la.us/rs-6-243.pdf>)
2. LAC 10:I.1101 (<http://www.ofi.state.la.us/rulelimitinvest.pdf>)
3. LSA-R.S. 6:121.4 (<http://www.ofi.state.la.us/rs-6-121-4.pdf>)
4. Part 323 of the FDIC's Rules and Regulations
(<http://www.ofi.state.la.us/re-fdicpart323.pdf>)
5. Subpart G of Regulation Y (<http://www.ofi.state.la.us/re-frbsubgregy.pdf>)
6. Part 564 of the OTS' Rules and Regulations
(<http://www.ofi.state.la.us/re-otspart565.pdf>)
7. LSA-R.S. 6:507 (<http://www.ofi.state.la.us/rs-6-507.pdf>)
8. LSA-R.S. 6:853 (<http://www.ofi.state.la.us/rs-6-853.pdf>)
9. LSA-R.S. 6:291 (<http://www.ofi.state.la.us/rs-6-291.pdf>)
10. LSA-R.S. 6:786 (<http://www.ofi.state.la.us/rs-6-786.pdf>)
11. LSA-R.S. 6:1190(<http://www.ofi.state.la.us/rs-6-1190.pdf>)

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