

1st Discussion DRAFT – OREO Rule

WAC 208-476

WAC 208-476-010 – Reason for rule

Why do Washington State-chartered credit unions need a rule on the handling of “other real estate owned” (OREO), property legally owned by the credit union as the result of foreclosure, or acquired as the result of default on a loan collateralized by real property?

Although most financial institutions that do real estate lending have experienced an occasional foreclosure, the volume and asset value of foreclosed property has significantly increased recently. Due to the economic downturn that began in 2008, credit unions are now experiencing a greater number of foreclosures and acquiring portfolios of OREO. Because this type of economic effect is cyclic, it is useful for credit unions to be prepared to handle OREO property in a safe and sound manner. Some credit unions may find their number of OREO properties is becoming more difficult to manage. Some credit unions may be dealing with OREO properties for the first time.

The Department of Financial Institutions, Division of Credit Unions, is responsible for regulating to protect the integrity of credit unions as cooperative institutions, and to ensure that they remain viable and competitive. RCW 31.12.015. It is important to provide regulatory standards for safe and sound management of OREO. RCW 31.12.005(24).

WAC 208-476-020 – Rulemaking authority

What is DFI’s rulemaking authority for these OREO rules?

The Division of Credit Unions is delegated rulemaking authority by the Director of DFI. DFI’s rulemaking authority is based upon the of the Washington Credit Union Act, RCW 31.12.516(2), which allows the Director to adopt rules that are reasonable and necessary to carry out the purposes of the WCUA. The Director has the power and broad administrative discretion to administer and interpret the provision of the WCUA. RCW 31.12.516 (4). In addition, the Director has specific rulemaking authority regarding secured or unsecured loans to members. RCW 31.12.426 (1).

WAC 208-476-030 – Authority of Director to require reports

What legal authority does DFI have to require special reports from credit unions, accounting for OREO?

The Director has the statutory authority to require a credit union to file any financial or statistical report the Director may require. The Director, therefore, has the authority to require special reports on OREO properties held by Washington state-chartered credit unions. RCW 31.12.567.

WAC 208-476-040 – Authority for credit unions to hold real estate

What is the legal authority for a credit union to acquire, hold and dispose of OREO?

A Washington state-chartered credit union is permitted to own foreclosed and other OREO property, based on its statutory power to make secured and unsecured loans to its members. RCW 31.12.426(1). If the borrower defaults on a loan secured by real property, the credit union has the authority to obtain title to the property as a power incidental to its normal course of business.

WAC 208-476-050 – Definitions

For purposes of these rules, the following definitions apply:

“Appraisal” means a written report by a certified or licensed appraiser containing sufficient information to support the DCU’s evaluation of OREO, taking into consideration market value, analyzing appropriate deductions or discounts, and conforming to Generally Accepted Appraisal Standards, unless principles of safe and sound credit union practices require stricter standards.

“DCU” means the Division of Credit Unions of the Washington State Department of Financial Institutions

“DFI” means the Washington State Department of Financial Institutions

“Director” means the Director of the Department of Financial Institutions, or the Director’s designee, typically the Director of the Division of Credit Unions

“Fair value” and “fair market value” mean the cash price that might reasonably be anticipated in a current sale under all conditions requisite to a fair sale, in which the buyer and the seller are each acting prudently, knowledgeably and under no necessity to buy or sell. An appraisal at fair value estimates the cash price that might be received upon exposure to the open market for a reasonable time, considering the property type and local market conditions.

“Foreclosure” means the termination of all rights of a mortgagor or grantee in the property covered by a mortgage.

“GAAP” means “Generally Accepted Accounting Principles”

“GAAS” means “Generally Accepted Appraisal Standards,” as stated in the Uniform Standards of Professional Appraisal Practice by the Appraisal Standards Board.

“Home Valuation Code of Conduct” means the Federal Housing Finance Agency (FHFA)’s current “Home Valuation Code of Conduct” for the improved reliability of home appraisals.

“OREO” means [CHOOSE ONE]

1. **property acquired by a lender through foreclosure and held in inventory. (Barron’s’ Dictionary of Business Terms)**
2. **real property, including improvements, mineral interests, surface, and subsurface rights, owned in whole or in part or leased by a Washington state-chartered credit union, no matter how acquired, and which is not real property acquired for the credit union’s own use in conducting business or for future credit union expansion under RCW 31.12.438. (based on Texas Admin. Code Title 7, part 2, Chap. 19 Subchap. C, Rule 19.51)**
3. **a class of property owned by a lender, typically a financial institution, after an unsuccessful sale at a foreclosure auction. A financial institution will typically set the opening bid at a foreclosure auction for at least the outstanding loan amount. If there are no bidders that are interested, then the financial institution will legally repossess the property. As soon as the financial institution repossess the property, it is listed on its books as “Other Real Estate Owned,” and is categorized as a nonperforming asset. (online encyclopedia-Wikipedia)**
4. **real estate acquired by a lender through foreclosure in satisfaction of a debt and held in inventory until sold. A loan secured by foreclosed real estate is counted as a nonperforming loan in reporting loan quality in call reports to financial institutions supervisory agencies. Foreclosed real estate is normally auctioned off through a bidding process. Normally, the lender bids what is owned and no more. If there are no higher bids, the lender takes the property and it becomes “Other Real Estate Owned.” (online business dictionary @ AllBusiness.com)**
5. **real estate acquired by a Washington state-chartered credit union:**
 - a. **through purchase at sales under judgments, decrees, or mortgages, where the property was security for debts previously contracted;**
 - b. **through conveyance in satisfaction of debts previously contracted;**
or
 - c. **through purchases to secure debts previously contracted. (Tennessee Department of Financial Institutions, Chapter 0190-14, “Regulations Pertaining to Other Real Estate”)**
6. **“debt previously contracted” real estate, including capitalized and operating leases acquired by a financial institution through any means in full or partial satisfaction of a debt previously contracted. (12 CFR Subpart E – Other Real Estate Owned)**

7. real property that a financial institution holds as a consequence of defaults on loans. It is typically a poor or non-earning asset and a financial institution's acquisition of a limited amount of OREO is an unavoidable result of normal business operations. OREO is acquired in the following ways:

- Real estate in judgment.
- Real estate acquired through foreclosure.
- In-substance foreclosures.
- Real estate acquired through deed in lieu of foreclosure.
- Any real property exchanged for foreclosed real estate.

(Examination Handbook, 251, Real Estate Owned and Repossessed Assets, federal Office of Thrift Supervision)

“Sheriff’s sale” means a sale of property by the sheriff under authority of a court’s writ of execution in order to satisfy an unpaid obligation.

WAC 208-476-100 – Limitations on Holding of OREO

(RESERVED)

Alternative approaches

WAC 208-476-200 – Accounting for OREO

(RESERVED)

Acquisition

Holding

Disposition and sale

GAAP

WAC 208-476-300 – Safe and sound practices for OREO

(RESERVED)

Board OREO policy

Valuations

Analysis prior to acquisition

Acquisition

Holding

Disposition

Internal controls