

May 5, 1992

James A. Rauer
Manager
Arlington Schools Federal Credit Union
P.O. Box 8008
Falls Church, VA 22041-8008

Re: Mortgage Foreclosures (Your Letter of April 6, 1992)

Dear Mr. Rauer:

You requested an opinion letter regarding the ability of a federal credit union ("FCU") to bid on property on which it holds a second mortgage at a foreclosure sale. An FCU may bid on property in this situation. You also asked if the FCU could bid on the same property after the foreclosure sale from the successful purchaser at the foreclosure sale. An FCU would not normally be permitted to purchase property in this situation, although it may apply to the Regional Office for approval. The Regional Office may allow this based upon individual facts and circumstances. Moreover, you inquired as to any operable restrictions imposed by the NCUA on these activities. The restrictions are ones of safety and soundness, as explained in this letter.

ANALYSIS

The authority of an FCU to bid on property in foreclosure arises from Sections 107(4) and 107(5) of the FCU Act. 12 U.S.C. §§ 1757(4) and (5). Section 107(4) grants an FCU the power "to purchase, hold, and dispose of property necessary or incidental to its operations." Section 107(5) grants an FCU lending authority. The NCUA has set forth an accounting policy on the repossession and sale of collateral property.

It makes no difference whether the credit union is in possession of the collateral by virtue of legal process, or whether possession results from voluntary action by the borrower (or comakers). In either event, the credit union is responsible for the collateral and has a responsibility to liquidate or dispose of the collateral as promptly as possible consistent with the best interests of both the credit union and the borrower (or comakers). NCUA Accounting Manual for FCUs, § 5110.1 (1989).

This policy will apply when an FCU bids for member property collateralizing an FCU loan at a foreclosure sale. See NCUA Opinion Letter from me to John Cipriano, entitled "Bidding on Property," dated August 31, 1990 (enclosed). As that letter states: "[w]e view this as part of the collection process on a defaulted loan." *Id.* It is possible for NCUA to object to this practice on safety and soundness grounds.

The practice of purchasing the property (upon which the FCU holds a mortgage or encumbrance) after another bidder has successfully purchased it at a foreclosure sale is another matter. If the primary mortgagee has purchased the property at the foreclosure sale, as in your situation, subsequent and junior mortgagees or encumbrancers ordinarily lose their rights in the property. See 55 Am.Jur.2d Mortgages § 801 (1971). This results in the extinguishment of the FCU's rights in the property. Even if a purchaser other than the primary mortgagee purchases the foreclosed property, the rights of any subsequent and junior mortgagees may be terminated. See 55 Am.Jur.2d Mortgages §§ 780-800; 47 Am.Jur.2d Judicial Sales §§ 268 and 328. Although the result is dependent upon state law, it is probable that an FCU as a junior lienholder will have no legal interest in the property after the foreclosure sale. We would advise the FCU to seek legal counsel on the effect a foreclosure would have in a particular case. As the FCU would likely have no legal interest

in the property after the foreclosure sale to another party, it would seem not to have the authority to purchase the property from the successful third party bidder who purchased the property at the initial foreclosure sale. See 12 U.S.C. ~1757. To do so would result in the acquisition of a speculative, unauthorized investment that must be accounted for as Other Real Estate Owned and sold as soon as possible. However, it is conceivable that special circumstances might exist under which the NCUA would permit an FCU to make such a purchase upon request to a Regional Office. No extenuating circumstances are described in your letter, nor is any plan of action for quick sale of property so purchased delineated, so at this time it would seem that your FCU may not purchase the property in question from the purchaser at the foreclosure sale. However, you may contact the Regional Office if you so desire.

Sincerely,

Hattie M. Ulan,
Associate General Counsel

cc: Kent Buckham,
Acting Director,
Division of Supervision,
Office of Examination and Insurance

Foster Bryan,
Region II Director

Enclosure
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