



December 6, 2017

submitted via email to comments@FDIC.gov
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Re: RIN 3064-AE59 – Comments on the Proposed Simplifications to the Capital Rule

Ladies and Gentlemen,

Thank you for the opportunity to comment on the proposed rulemaking titled “Simplifications to the Capital Rule Pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996.”

After reviewing the proposed rulemaking we believe that, on balance, it would be an improvement to the current rule. Specifically, we believe that the proposed rulemaking:

- is, in fact, somewhat simpler than the current rule;
- would make it easier to identify higher-volatility loans than the current rule does;
- properly excludes from an HVADC designation those loans that are permanent loans and those for community development purposes; and
- smartly eliminates the current, illogical provision that requires, in order to avoid a loan having a high-volatility designation, *more* borrower equity into a project as the appraisal *increases*.

However, we believe that the proposed rulemaking needs further clarification related to the exclusion of loans as HVADC under the permanent loan and community development provisions. As we compared the proposed rule to the types of acquisition, development and construction loans we make, we were left without sufficient clarity in the following examples:

Owner-occupied properties

1. Say we extend a loan to an owner-occupant borrower for the construction or expansion of his/her business facility. The loan is structured with an initial interest-only construction phase, and upon completion it automatically converts to a longer-term permanent phase requiring amortizing payments of principal and interest. The repayment of the loan is underwritten in reliance on the borrower’s *projected* cash flow – i.e. the borrower does not historically

demonstrate an ability to repay the debt, but his/her projections, taking into account the effects of the newly constructed/expanded facility upon his/her business operation, do. (E.g., the borrower's expanded facility will incorporate additional production space for his/her business, which will generate added revenue, income and cash-flow.) We have analyzed the projections, together with all of the other characteristics of the credit, and we have concluded that the projections are sound and worthy of reliance in extending the loan. We therefore believe the loan has been "prudently underwritten" with a "clearly identified ongoing source of repayment sufficient to service amortizing principal and interest payments aside from the sale of the property." Does this fact pattern satisfy the Permanent Loan exclusion from HVADC at the inception of the loan?

2. Use the same facts as above, except in this case say the owner-occupant borrower has not prepared projections. In several recent years, though not all, the borrower demonstrated an ability to repay the debt. The borrower attributes the fluctuation in his/her operating results to the inherent vagaries of business. After analysis, we agree, and together with all of the other characteristics of the credit, we conclude that there is a satisfactory basis to extend the loan. We therefore believe the loan has been "prudently underwritten" with a "clearly identified ongoing source of repayment sufficient to service amortizing principal and interest payments aside from the sale of the property." Does this fact pattern satisfy the Permanent Loan exclusion from HVADC at the inception of the loan?

Please note, both of the above examples, and countless variations of them, are routinely encountered by banks lending on owner-occupied properties. *And we don't believe that loans on owner-occupied properties are the regulators' intended target of high-volatility risk assignment and the HVADC designation.* Wouldn't it be best and simplest to clearly stipulate in the rule that loans which finance the acquisition, development and construction of majority owner-occupied real property projects be excluded from HVADC?

Non-owner-occupied properties

In discussing types of Permanent Loan exclusions from HVADC, the proposed rule notes that for "many acquisition, development, or construction projects, the source of repayment will be derived from the property once the project is completed and tenants begin paying rent..." Given its placement within the surrounding examples, it seems the intent of that statement was to indicate that such loans qualify for a Permanent Loan exclusion. But in our opinion that's not 100% clear as written. So we pose the following examples:

1. Say we finance the acquisition and development of a pad site for lease to a single tenant. The loan is structured with an initial interest-only development phase, and upon completion it automatically converts to a longer-term permanent phase requiring amortizing payments of principal and interest. The lease between the borrower and tenant is executed prior to our closing of the loan, and the lease provides for satisfactory cash flow to service the amortizing loan payments. However, the tenant's obligations under the lease are subject to the borrower's

timely and satisfactory development and delivery of the pad site to the tenant, and the lease payments will not commence unless/until that agreed-upon delivery is made. We believe the borrower has the ability to complete the project and deliver the project in conformance with the lease terms and, together with all of the other characteristics of the credit, we conclude that there is a satisfactory basis to extend the loan. We therefore believe the loan has been “prudently underwritten” with a “clearly identified ongoing source of repayment sufficient to service amortizing principal and interest payments aside from the sale of the property.” Does this fact pattern satisfy the Permanent Loan exclusion from HVADC at the inception of the loan?

2. Say we finance the acquisition, development and construction of a 5+ multi-family apartment building. The loan is structured with an initial interest-only construction phase, and upon completion automatically converts to a longer-term permanent phase requiring amortizing payments of principal and interest. The borrower has not yet leased the units, but his/her projections demonstrate an anticipated cash flow satisfactory to service the amortizing loan payments. We believe the borrower has the ability to complete the project and we are satisfied with the reasonableness of the borrower’s projections regarding occupancy and the building’s cash flow. Together with all of the other characteristics of the credit, we conclude that there is a satisfactory basis to extend the loan. We therefore believe the loan has been “prudently underwritten” with a “clearly identified ongoing source of repayment sufficient to service amortizing principal and interest payments aside from the sale of the property.” Does this fact pattern satisfy the Permanent Loan exclusion from HVADC at the inception of the loan?

3. Say we provide acquisition, development, and construction financing of a non-owner-occupied commercial property which is being built speculatively, for lease. The loan is structured with an interest-only construction phase, and upon completion it automatically converts to a longer-term permanent phase requiring amortizing payments of principal and interest, *irrespective of the borrower’s success in leasing the property*. There are guarantor(s) of the loan who generate sufficient ongoing, outside cash flow to service amortizing principal and interest payments aside from the lease the property. This outside cash flow is believed to be reliable and is unrelated to the property being financed, and therefore the ‘global cash flow’ is satisfactory to service our debt even if the speculatively-built property is not leased as the borrower intends. Together with all of the other characteristics of the credit, we conclude that there is a satisfactory basis to extend the loan. We therefore believe the loan has been “prudently underwritten” with a “clearly identified ongoing source of repayment sufficient to service amortizing principal and interest payments aside from the sale of the property.” Does this fact pattern satisfy the Permanent Loan exclusion from HVADC at the inception of the loan?

Community Development/SBA

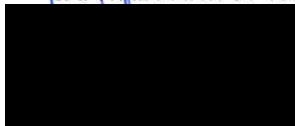
We aren’t certain that the proposed Community Development exclusions as written relating to Small Business Administration (SBA) loans provide an automatic exclusion from HVADC for all SBA 7(a) and SBA 504 loans. Given the substantial credit enhancements provided by both of those programs, they

should be explicitly excluded. And if that is the intention, it should be stated more succinctly in the rule, e.g. "No SBA 7(a) loan or SBA 504 loan shall carry an HVADC designation."

Again, thank you for the opportunity to comment. Greater simplicity and clarity for the above types of transactions would further improve the proposed rule.

Should you have any questions, please do not hesitate to contact any of the undersigned.

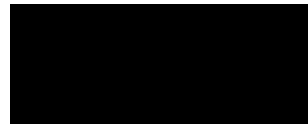
Sincerely,
CAPITAL BANK OF NEW JERSEY



David J. Hanrahan, Sr.
President and CEO



Joseph F. Rehm
EVP and Chief Lending Officer



Stephen Modzelewski
Credit Department Officer

cc: Rob Nichols, President and CEO, American Bankers Association
John McWeeney, President and CEO, New Jersey Bankers Association