Capitol Federal®

JOHN B. DICUS, CHAIRMAN

December 22, 2017

Office of the Comptroller of the Currency

Re: Docket ID OCC-2017-0018. Simplifications to the Capital Rule Pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996.

Capitol Federal Savings Bank appreciates the opportunity to comment on the proposed changes regarding Simplifications to the Capital Rule Pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996. This comment letter is to specifically address the changes proposed in Section A. HVADC Exposure. Capitol Federal is not providing comments regarding other sections of the proposal.

In general, the Bank agrees that the current High Volatility Commercial Real Estate (HVCRE) regulations are complex and allow for different interpretations of which acquisition, development and construction loans fall under the HVCRE rules. We appreciate that the regulatory agencies are attempting to simplify and bring clarity with the issuance of a new definition, High Volatility Acquisition, Development and Constructions (HVADC). The new HVADC definition does simplify the process; however, we have concerns that the proposal treats all commercial real estate (CRE) construction loans the same and does not allow for differentiating risk.

Proposal to eliminate the exclusion based upon equity injection from the borrower. Under HVCRE, loans where the borrower injected 15% or more equity based upon the "as complete" value, the equity was injected prior to any disbursements from the Bank, and the equity was retained in the project for the life of the loan, were excluded from HVCRE requirements. A loan where the borrower made a significant equity contribution (greater than 15%) is risk weighted at 100% for capital requirements. In converse, a loan that did not meet the contributed equity requirement would be considered higher risk and would be subject to the 150% capital requirement. The concept of a higher capital requirement for higher risk loans, particularly higher risk due to less up-front borrower equity, is prudent.

Under the HVADC proposal, all CRE construction loans that do not meet one of the exemptions will be risk weighted at 130% without taking into consideration how much equity was injected into the project. A loan where a borrower only contributed 5% equity would be treated the same as a loan where the borrower contributed 20% equity. The proposed regulations would "grandfather" loans currently held in portfolio; however, the Bank retroactively applied the new HVADC definition to the CRE construction loan portfolio to estimate the effect on a go forward basis assuming similar origination volume continues into the future. The Bank's analysis determined that the HVADC proposal would have resulted in a 295% increase in risk weighted assets and a decrease in the Bank's capital ratios of 1.40%. The borrower injected 20 to 25% equity for most of the loans included in the analysis.

The Bank believes that the HVADC definition should exclude loans where the borrower has injected at least 15% equity into the project. We also recommend that the project budget or cost be used instead of the "as complete" value to determine the amount of equity required to be contributed to be exempt under HVADC. When analyzing and pricing a loan, the project budget or cost is used to determine the loan to value and the expected amount of equity to be contributed to be exempt. If the appraisal results in an 'as complete' value that is higher than the project budget, the bank would have to require additional equity injection from the borrower even though nothing in the project has changed. After consummation, if the actual cost to build exceeds the budget due to change orders or other increases in costs, the borrower is expected to cover any shortfall, which increases the borrower's equity injection. This is more equitable to the borrower, as the borrower has some level of control over the project cost. The cost is a more definitive number than the "as complete" value.

HVADC Permanent Loan Exemption. Capitol Federal Savings agrees with the permanent loan exemption and believes this reduces the regulatory burden. The Bank recommends that this exemption be included in the final regulation.

HVADC grandfathering provision. Capitol Federal also agrees that the grandfathering provision should be included in the regulation to reduce the regulatory burden.

Thank you for allowing the Bank to comment on the proposal.

Respectfully submitted,

[redacted]

Kevin Morgison
First Vice President

cc: Sharon Whitaker, Vice President of Commercial Real Estate Finance, American Bankers Association