NCBANKERS
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DELIVERED VIA E-MAIL

Office of the Comptroller of the Currency
250 E Street SW
Mail Stop 1-5
Washington, DC 20219

Docket No. 06-01
regs.comments@occ.treas.gov

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Docket No. OP-1248
regs.comments@federalreserve.gov

Mr. Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

comments@fdic.gov

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street NW
Washington, DC 20552

Attention: No. 2006-01
regs.comments@ots.treas.gov

Re: Concentrations in Commercial Real Estate Lending; Sound Risk Management Practices
71 Fed. Reg. 9, 2302 (January 13, 2006)

Ladies and Gentlemen:

The North Carolina Bankers Association (NCBA) appreciates the opportunity to submit these comments in response to the proposed guidance entitled *Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices*. The NCBA membership includes all 146 banks, savings institutions, and trust companies headquartered or doing business in North Carolina. Based on communications with our members, we must express our strong opposition to the proposed guidance.

The guidance sets thresholds for determining whether a financial institution has a commercial real estate (CRE) concentration. The two thresholds are: (1) total reported loans for construction, land development, and other land represent 100% or more of the institution's total capital; or (2) total reported loans secured by multifamily and nonfarm nonresidential properties and loans for construction, land development, and other land represent 300% or more of the institution's total capital. Under the proposal, institutions exceeding threshold 1 should have heightened risk management practices appropriate to the degree of CRE concentration risk. Institutions exceeding threshold 2 should quantify the dollar amount of those loans that meet the definition of a CRE loan and should have heightened risk management practices.

CRE loans are defined as exposures secured by raw land, land development and construction (including 1-4 family residential construction), multi-family property, and non-farm nonresidential property where the primary or a significant source of repayment is derived from rental income associated with the property or the proceeds of the sale, refinancing, or permanent financing of the property. Loans to REITs and unsecured loans to developers that closely correlate to the inherent risk in CRE markets would also be considered CRE loans.

The NCBA's first concern with the guidance is its broad scope. The stated justification for the guidance is that some institutions have high and increasing concentrations of commercial real estate loans on their balance sheets and the agencies are concerned that these concentrations may make the institutions more vulnerable to cyclical commercial real estate markets. A better approach would be to evaluate institutions on a case-by-case basis under the existing guidelines. If some financial institutions' loans are not sufficiently diversified and lack risk mitigating factors, then the agencies already have sufficient authority to direct that corrective action be taken.

We are also deeply troubled by the stated thresholds. In the absence of information about how these triggers were calculated, the thresholds seem arbitrary and too low. Using these thresholds would have a disproportionate impact on the nation's community banks. Competition, particularly from the tax-advantaged credit union industry, has forced community banks to direct more of their energies to CRE lending because it remains one of the few, consistently profitable areas. Imposing the proposed thresholds could drastically curtail CRE lending in many markets and lead to job losses. Any resulting shortage of available credit would substantially affect real estate prices and community development. Additional harm could also occur if financial institutions are forced to turn to riskier investments to try to remain profitable.

Another aspect of the guidance that is troubling is its lack of specificity. The discussion of risk management principles is vague when it comes to what steps should be taken to comply with agency expectations. If the objective is to allow for more flexibility in implementation, that is a laudable goal; however, it must be balanced against the need for predictability in examinations. Examples of how the guidance would be applied are needed. Take for instance a financial institution that has a CRE concentration that is twice the first threshold stated in the guidance. The institution currently has risk management practices similar to those outlined and has consistently been rated as well-capitalized and well-managed. Would such an institution have to divest itself of much of its CRE portfolio or develop a strategy to increase capital in order to be in compliance? The question really hinges on whether the proposed regulation would completely change the regulatory landscape.

Financial institutions are greatly concerned about the implications of this guidance and question whether it gives sufficient consideration to their existing underwriting processes. A classic maxim is that no two borrowers are the same. Any proposed CRE lending test needs to retain the flexibility so that loans to well-qualified borrowers can continue to be made. It should also be flexible enough to take into account the unique character of each real estate region.

For these reasons, the NCBA asks that you consider withdrawing or substantially amending the proposed guidance. If you have any questions, then please contact us.

Sincerely,

Nathan R. Batts

Nathan R. Batts
Associate Counsel