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March 2, 2006

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Re: Comment on Proposed Guidance: "Concentrations in Commercial Real Estate Lending" (Fed Docket No. OP-1248)

Ladies & Gentlemen:

The Board of Directors of Peoples Bank, Lawrence, Kansas appreciates the opportunity to comment on the proposed guidance entitled "Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices (Guidance)". Our comments are as follows:

We object to the proposed Guidance and urge the Agencies to reconsider the Guidance for the following reasons:

A. The Guidance is Vague and Ambiguous and Subject to Inconsistent Application.

B. Depending on Interpretation, Application of the "Suggestions" of the Guidance would be Burdensome and Oppressive.

C. The Guidance Represents Poor Policy as it is Potentially Counter Productive to Sound Credit Quality.

By way of background, Peoples Bank is a $320,000,000 community bank with operations in northeast Kansas and northern New Mexico. Our earning assets consist primarily of loans made within the communities in which we do business. A very large percentage of our loans are secured by commercial and residential real estate. As Commercial Real Estate ("CRE") is defined in the Guidance, CRE loans of Peoples Bank are as follows:

(1) Total reported loans for construction, land development, and other land represent two hundred twenty three percent (223%) of Peoples Bank's total capital; and

(2) Total loans secured by multi-family and non-farm residential properties and loans for construction, land development, and other land represent five hundred ninety seven percent (597%) of Peoples Bank's total capital.

At our recent examination conducted by the State of Kansas, Peoples Bank received a Credit Quality Rating of which we are very proud. We believe that our lending practices, policies and procedures are prudent and result in high credit quality and protection of the capital of the Bank.

The Kansas City, Albuquerque and Lawrence real estate Markets have not experienced the (apparently) excessive housing price escalation of some Markets. According to an article[1] on www.moneycentral.msn.com which ranks the 276 Metropolitan Statistical Areas (MSAs) separate geographic Markets, the three Peoples Bank MSA Markets rank as follows:

		Price Appreciation Percentage		
	Annual Housing Price Index Ranking	1-yr	4th Quarter	5-year
Kansas City	210	4.92	0.99	29.06
Albuquerque	75	16.58	3.95	42.23
Lawrence	197	5.59	0.86	32.52

A. **The Guidance is Vague and Ambiguous and Subject to Inconsistent Application**.

A review of the Guidance reveals that the word "should" is used sixty four (64) times in the document when describing action which the Guidance proposes (or suggests) be taken by banks. With respect to the sixty-four (64) "Suggested" actions, very few if any of the actions are clearly and specifically outlined in the document. For example, in the section entitled "**Board of Management Oversight**" nine (9) proposed actions appear as follows:

1. "Explicitly approve the overall CRE lending strategy and policies of the institution."
2. "Receive reports on changes in CRE market conditions and the institution's CRE lending activity that identify the size, significance, and risks related to CRE concentrations."
3. "Use this information to provide clear guidance to management regarding the level of CRE exposures acceptable to the institution."
4. "Ensure that senior management implements the procedures and controls necessary to comply with adopted policies."

[1] Rankings for house-price appreciation from the Office of Federal Housing Enterprise Oversight (OFHOE) released March 1. The OFHOE House Price Index tracks average house price changes in repeat sales or refinancing of the same single-family properties. OFHOE's index is based on analysis of data obtained from Fannie Mae and Freddie Mac from more than 30 million repeat transactions over the last 30 years. See attached article.

5. "Periodically review and approve CRE aggregate risk exposure limits and appropriate sub-limits to conform to any changes in the institution's strategies and to respond to changes in market conditions."
6. "Ensure that management compensation policies are compatible with the institution's strategy and do not create incentives to assume unintended risks."
7. "Implement the CRE strategy in a manner that is consistent with the institution's stated risk tolerance."
8. "Develop and implement policies, procedures, and limits that provide for adequate identification, measurement, monitoring, and control of the CRE risks."
9. "Adopt and maintain a written policy that establishes appropriate limits and standards for all extensions of credit that are secured by liens on or interests in real estate, including CRE loans."

Few of the "Suggested" actions above are identified with sufficient clarity so as to allow the Board of Directors of Peoples Bank to predict with certainty whether regulatory authorities will determine whether Peoples Bank has or has not complied with the "Suggestions".

In fact, with respect to the suggested activities, Peoples Bank believes that it currently carries out most of these Suggestions. It is unknown from the reading of the Guidance, however, whether the actions currently being taken by Peoples Bank satisfy the Suggestions of the Guidance. **Without further specifics as to how compliance with each "Suggestion" will be determined, it is inappropriate to expect prudent bankers to be able to predict whether their actions will comply with the Guidance.**

B. **Depending on Interpretation, Application of the Suggestions of the Guidance would be Burdensome and Oppressive**.

While Peoples Bank welcomes the opportunity to improve its credit quality policies, practices and procedures and we believe that we can and should improve those practices, policies and procedures, compliance with each and every "Suggestion" of the Guidance in a manner which is strictly interpreted by the Regulators would be oppressive and needlessly burdensome on Peoples Bank and other community banks.

It is also noted that commercial real estate loans are, for the most part, lumped together in the Guidance even though they serve different purposes, to different end users and industries and in different geographic markets. To combine all non-owner occupied real estate in the fashion proposed is over simplistic and potentially burdensome.

C. **The Guidance Represents Poor Policy as it is Potentially Counter Productive to Sound Credit Quality**.

Finally, Peoples Bank believes that well underwritten loans which are secured by real estate are sound and are much less subject to significant loss than loans secured by personal property or intangibles. In particular, loans secured by real estate are generally much less susceptible to loss than loans secured by other types of collateral such as receivables, business inventory, farm equipment, general intangibles, restaurant FF&E, equipment leasing, automotive floor plans, credit card lending, unsecured lending, high tech lending and other types of collateral.

Further, if Peoples Bank and other banks are effectively forced to reduce the amount of loans secured by commercial real estate, the amount and percentage of loans secured by other less reliable collateral will no doubt increase. Application of this Guidance will have the practical effect of increasing loans in Peoples Bank and other community banks which are secured by less reliable collateral. Therefore, application of the proposed Guidance as a practical matter is virtually certain to result in an increase in loans which are subject to greater loss than loans secured by real estate.

As a part of an Attachment to this letter, we incorporate further comments and questions posed by Ron Megli, Chief Credit Officer of Peoples Bank. Those comments are incorporated by reference as a part of this letter.

In summary, the Board of Directors of Peoples Bank objects to the Guidance as written. We do, however, look forward to working with State and Federal Regulators (Kansas Office of the State Bank Commissioner (OSBC) and Federal Reserve) to improve the practices, policies and procedures of Peoples Bank with respect to commercial real estate lending.

Very truly yours,

Wint Winter, Jr.

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Encl.

**ATTACHMENT TO PEOPLES BANK (LAWRENCE, KANSAS)
COMMENT ON PROPOSED GUIDANCE**

Comments by Ron Megli, Chief Commercial Lender

A. We note that the low interest rate environment that we have had since the recession of 2000 and 9/11 have produced the intended result of stimulating a successful national economic recovery. To a large extent, real estate construction, development and refinancing in the commercial and residential sectors have contributed substantially to lead us out of this recession. Now that the economy is performing well and interest rates have increased, the Guidance note that there are "some" institutions that have high and increasing concentrations of commercial real estate loans that are vulnerable to cyclical commercial real estate markets. Because of the real estate concentrations of "some", it appears that all financial institutions are being penalized with eight plus pages of a "Guidance" which may have more than the intended effect of reducing the industry's exposure to real estate.

- The Guidance appears to go beyond its stated intention of reinforcing previous real estate guidance as it states in the background--to limiting real estate exposure by identifying institutions with CRE concentrations vis-à-vis their capital. The intended consequences of the Guidance is clear. To reduce industry exposure to commercial real estate.
- The unintended consequences are not clear and the following questions come to mind when considering unintended consequences:
    - What impact will the Guidance have on credit availability to the real estate industry?
    - What effect will the Guidance have on pricing real estate loans?
    - What effect will the Guidance have on sellers and buyers of real estate?
    - What effect will the Guidance have on the ability to participate real estate loans to other financial institutions?
    - What effect will the Guidance have on the commercial secondary financing market?
    - What effect will the Guidance have on a financial institution's portfolio and the industry at large when it moves away from making commercial real estate loans?
    - What effect will the Guidance have on local and national economies?

B. We also pose the additional questions regarding the Guidance:

1. It is assumed that the 100% and 300% CRE definitions are supported by a significant body of information. Since we have not been provided with that information, it is difficult to determine if the conclusions are valid and necessary. Can this information be shared with us so that we can understand how these percentages were determined and so that we can offer an alternative remedy, if one is indeed necessary?

2. What percentage of all institutions already exceed these percentages, i.e. how widespread is this CRE issue?

3. What is the total dollar amount of CRE loans and loans to related industries that all financial institutions would have to divest themselves of to no longer have a CRE concentration?

4. What would the impact of the industry divesting itself of its real estate concentrations have on the local, regional, and national economies? What if all institutions were required to reduce their commercial real estate exposures at the same time?

5. Could the implementation of the CRE Guidance cause exactly what they are trying to prevent? Is the cure worse than the illness? Should there be some phase-in period or grandfathering of existing exposures?

6. Has the Guidance been stress tested as you suggest that we should test our real estate portfolios?

7. How much additional time and how much additional cost is estimated to be incurred to implement, monitor, and assure compliance with the Guidance for financial institutions under $100 million, $100-$500 million, $500 million to $1 billion, and over $1 billion in assets?