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March 31, 2006

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, DC 20429

RE: FDIC 2006-01
Concentrations in Commercial Real Estate Lending

Dear Mr. Feldman:

This letter is in response to the proposed guidance entitled Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices (Guidance).

I am the President and CEO of Danversbank, a $1.1 billion state chartered, mutual savings bank, which is regulated by the FDIC and by the Massachusetts Division of Banks. For many years commercial real estate (CRE) lending has been an important business line for my institution and for many other banks in Massachusetts. Community banks play an essential role in creating local economic growth by providing credit to small and medium-sized businesses for construction and land development. While I understand that the federal regulatory agencies have expressed concern with the high concentrations of commercial real estate loans at some institutions, I believe the proposed guidance will have a serious impact on community banks and local economies in general. The proposed guidance will place a significant regulatory burden on banks that have a market niche in commercial real estate loans, limiting the institutions' future growth in this area and possibly forcing some banks out of the market altogether. Many of our local community banks are already near or above the proposed guidance limits and may be forced to substantially reduce or to eliminate their CRE lending. We have all seen instances where the substantial reduction or elimination of lending capital has negatively impacted market values. This type of impact could potentially turn the concern over the health of the real estate market into reality.

I agree that it is prudent to remind institutions that the Board of Directors and Senior Management have a responsibility to maintain and follow policies and controls to operate in a safe and sound manner. For years our Senior Management has made quarterly reports to our Board providing information on all of our constructions loans, detailing concentrations in each town, on the type of product being built, on loan exposure and on speculative exposure. Our portfolio of CRE loans is spread over our entire market area with no significant concentration in any one town or in any one type of property. As required, our loan policies are annually updated and approved by the Board. Our solid management team, combined with experienced CRE lenders and prudent lending polices and procedures, have earned us outstanding asset quality and a total commercial delinquency rate, including CRE, of 0.25%.

I am particularly concerned with the “one-size-fits-all” nature of the proposed guidance. Institutions are automatically classified as having a “CRE concentration” simply if they exceed the thresholds. Portfolio diversification or other risk mitigation procedures are not taken into consideration. Because real estate markets vary greatly from region to region, and even within a particular state, the agencies should focus more attention on local market conditions and the overall condition and management of the individual institution than generic thresholds broadly applied to all banks.

Another troubling aspect of the guidance is that it makes blanket assumptions that certain types of commercial lending is more risky than others with no empirical data to support the assumption. For example, the guidance seems to suggest that somehow owner occupied commercial real estate lending is less risky than properties which rely on unaffiliated third party rental payments. I can site numerous examples in which the existence of third party rent actually enhanced the credit quality of a particular loan because the borrower was able to demonstrate multiple sources of revenue to support the debt service. Moreover, one could make an argument that a commercial real estate property in which a related operating entity is the sole source of the rental income actually exposes the lender to greater risk due to lack of diversification of income streams.

A quick loan concentration test does not account for the differences in risks taken by large money center, major regional and community banks. Certainly there is a difference between a large bank construction loan that finances a major commercial real estate project on a non-recourse basis and a personally guaranteed single-family construction loan in a community bank’s local market. There is also a difference between financing small owner/operators who invest in non-class A real estate and local residential construction versus the extremely large single loan exposures that larger banks assume when lending to REITs, big box retailers, the hotel and resort industry and a host of other large commercial speculative projects. The guidance does not take into account differences in property type, Debt Service Coverage Ratios, Loan to Values, personal guarantees versus non-recourse, smaller multifamily (6-family) versus very large rental complexes (100 plus units), and single tenant occupancy versus multiple tenants. No adjustment for risk appears to be made for investment property loans made on leased properties that have proven solid Debt Service Coverage Ratios and consistent tenancy.

The most recent real estate crisis of the late eighties and early nineties provided for significant new regulations, elevated examination guidelines and guidance on real estate lending. The FDIC Rules and Regulations, Part 365, Real Estate Lending Standards provides considerable detail for establishing and maintaining a prudent loan policy and loan requirements:

> “The agency’s regulations require that each insured depository institution 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 or made for the purpose of financing the construction of a building or other improvements. These guidelines are intended to assist institutions in the formulation and maintenance of a real estate lending policy that is appropriate to the size of the institution and the nature and scope of its individual operations, as well as satisfies the requirements of the regulation.
>
> Each institution's policies must be comprehensive, and consistent with safe and sound lending practices, and must ensure that the institution operates within limits and according to standards that are reviewed and approved at least annually by the Board of Directors. <u>Real estate lending is an integral part of many institutions'</u>

> <u>business plans and, when undertaken in a prudent manner, will not be subject to examiner criticism</u>."

I believe the proposed guidance is unnecessary and could simply create a threshold that is not properly evaluated as to risk as measured under all existing policies, procedures and guidelines already in place. It could cause, without intention, some financial institutions to seek diversification into much riskier assets which could in the aggregate pose more risk than CRE lending.

Alternative commercial lending opportunities are also an issue as the country's manufacturing sector has been dramatically reduced, just in time inventories are prevalent and many commercial businesses have evolved into service industries. Service industries have substantially lower borrowing needs than the manufacturing sector, which limits banks' commercial lending opportunities.

The proposed guidance recommends increased capital levels for banks with CRE concentrations. This requirement will place a serious burden on mutual institutions, which represent 70 percent of the banks in Massachusetts and who rely on earnings as their sole source of new capital. Therefore, these institutions would be forced to reduce levels of a strong earning asset in commercial real estate during a period of significantly reduced margins. Furthermore, the current Risk Based Capital policy in place already requires commercial real estate loans to be classified at 100% risk-weighting, thus requiring banks which engage in this type of lending to maintain higher capital levels then non commercial real estate lenders.

In closing, I am concerned that the continued tightening of regulations is approaching the point whereby a community bank will no longer be able to compete in the market and comply with all the required regulations. This trend will, in my opinion, accelerate the consolidation of the industry, which will ultimately be detrimental to the communities and to the consumer.

Thank you again for the opportunity to comment on the proposed guidance and for considering my views.

Very truly yours,

Kevin T. Bottomley

Kevin T. Bottomley
President & CEO