WELLS FARGO

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November 27, 2018

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
Attn: Docket ID OCC-2018-0026
400 7th Street SW, Suite 3E-218, Mail Stop 9W-11
Washington, D.C. 20219

Ann E. Misback
Secretary
Attn: Docket No. R-1621
Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, N.W.
Washington, D.C. 20551

Robert E. Feldman
Executive Secretary
Attn: Comments/Legal ESS, RIN 3064-AE90
Federal Deposit Insurance Corporation
550 17th Street, N.W. Washington, D.C. 20429

Re: Regulatory Capital Treatment for High Volatility Commercial Real Estate (HVCRE) Exposures

Ladies and Gentlemen,

Wells Fargo & Company ("Wells Fargo" or "we") is a diversified financial services company with over $1.8 trillion in assets providing banking, investments, and mortgage products and services, as well as consumer and commercial financial services. We appreciate the opportunity to comment on the proposed rule related to the *Regulatory Capital Treatment for High Volatility Commercial Real Estate (HVCRE) Exposures*.

The proposed rule would amend the definition of HVCRE Exposure within the capital rules to conform to the statutory definition of HVCRE ADC Loan in Section 214 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA).

We appreciate and welcome the opportunity to comment on the proposed rule. We support the desire to simplify the definition of HVCRE Exposure and to ensure that banks implement the definition consistently. To those ends, we wish to provide our commentary on this proposal and to support comments supplied by other groups.[1]

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[1] See comments from the American Bankers Association, the Banking Policy Institute, and the Commercial Real Estate Finance Council.

Summary

We recommend eliminating the HVCRE category from the capital rules. The definition remains complicated and requires banking organizations to track and analyze significant amounts of information, the cost of which is not justified by the resulting amount of HVCRE Exposures likely to be identified under the proposed definition. Additionally, the historical justification for maintaining a separate HVCRE Exposure category relied, in part, on maintaining consistency with agreements reached by the Basel Committee on Banking Supervision (BCBS). The HVCRE ADC Loan definition under EGRRCPA is no longer consistent with the BCBS agreements.

If the agencies do not remove the HVCRE Exposure category, we believe they should provide additional specificity to reduce some of the compliance burden associated with the proposed definition and to ensure that banking organizations implement the rule consistently.

Eliminate the HVCRE Exposure Category

HVCRE Exposures under the proposal would be subject to a risk weight of 150 percent under the Standardized Approach, while other acquisition, development and construction loans (ADC) would be subject to a 100 percent risk weight under the Standardized Approach. There are very few instances in the Standardized Capital Approach in which the same type of loan is subject to two different risk weights based on underlying risk parameters. In general, despite what may be very large differences in the risk of two loans of the same type, the loans are subject to the same risk weight. Under the Advanced Approaches, HVCRE Exposures would be subject to a higher correlation factor. Separate correlation factors are only applied to HVCRE Exposures and exposures to certain financial institutions.

Beyond the capital rules, the agencies' supervision activities ensure the stability of the banking industry by identifying undue risks and weak risk management practices regarding significant concentrations of risk at certain banking organizations. We believe that the fundamental risk management practices, verified through the examination process, serves to safeguard the integrity of the banking system as compared to a cumbersome replacement of regulatory supervision process through an arbitrary increased risk-weight for a difficult-to-define population of loans. In short, our view is that that the post-crisis examination process has generally worked well, is not broken with respect to ADC lending, and should not be supplanted by indiscriminately increasing risk weights for a likely immaterial loan population.

We don't believe the small amount of exposures that would meet the proposed HVCRE Exposure definition warrants a particularly punitive treatment in the capital rule. If such an approach is warranted, it would seem to be warranted for other types of loans and in both directions (i.e. low risk ADC loans should be subject to lower risk weights).

According to the proposal, EGRRCPA, "states the agencies *may* only require a depository institution to assign a heightened risk weight to an HVCRE exposure, as defined under the capital rule, if such exposure is an HVCRE ADC loan under EGRRCPA." Accordingly, EGRRCPA does not require the agencies to apply a heightened risk weight to any HVCRE exposures. The proposal does not attempt to justify the continued inclusion of a separate HVCRE exposure definition within the capital rules. Further, some of the historical justification for such a category is no longer operative. In particular, the new definition of the HVCRE Exposure category is no longer consistent with BCBS standards, on which the old definition of the HVCRE Exposure category was based.

Additionally, the HVCRE Exposure category still puts a significant operational burden on banking institutions. Our estimates suggest that the proposed definition will result in a significant reduction in HVCRE Exposures relative to the historical definition on our portfolio. Given the significant decline in the amount of HVCRE Exposure that institutions across the industry are likely to report we do not believe the costs of this proposal are outweighed by the benefits of continuing the category.

Additional clarification

If the agencies believe the additional HVCRE Exposure category is still warranted, we suggest more explicitly tying the definition of HVCRE Exposures to the Call Report and providing additional burden relief related to loan-to-value (LTV) measurements.

Alignment with the Call Report

We suggest aligning relevant terms as closely to those in the Call Report as possible. In addition, where possible, specific references to Call Report line items should be provided to enhance consistency.

As proposed, banking organizations would follow the Call Report definition of "loan secured by real estate" and "farmland," but deviate from the Call Report definition of "one-to-four-family residential property" and instead follow the definition in the interagency real estate lending standards. In that respect, the proposal creates unnecessary confusion.

Ideally, the identification of HVCRE Exposures should start from a specific population identified on the Call Report. We suggest explicitly limiting the potential population of HVCRE Exposures to those reported on line items to RC-C.1.a.(2) and RC-L.1.c.(1).(b). From there, banking organizations would assess the population against the exclusion criteria in the rule.

LTV Calculations

The agencies invited comment on several topics that relate to calculating loan-to-value (LTV) amounts (e.g. the contributed capital calculation and the appraisal value). The identification of HVCRE Exposures relies on LTVs set forth in the interagency real estate lending standards. Those standards define the loan-to-value ratio as:

> Loan-to-value ratio means the percentage or ratio that is derived at the time of loan origination by dividing an extension of credit by the total value of the property(ies) securing or being improved by the extension of credit plus the amount of any readily marketable collateral and other acceptable collateral that secures the extension of credit. The total amount of all senior liens on or interests in such property(ies) should be included in determining the loan- to-value ratio. When mortgage insurance or collateral is used in the calculation of the loan-to-value ratio, and such credit enhancement is later released or replaced, the loan-to-value ratio should be recalculated.

HVCRE appraisal requirements do not align with appraisal regulations or the Uniform Standards of Professional Appraisal Practice (USPAP) methods. Specifically, regulations and methods require an appraisal to be based on "market value"; however, market value may not be exclusive to "as is" or "as completed" valuations which are noted in the proposed guidance. In practice then, there are several types of LTVs, none of which are specifically required by the interagency real estate lending standards. For example, "as is," "as completed," and "as stabilized" values may suffice for LTV standards per an institution's underwriting and monitoring standards. Firms should be allowed to use whatever LTV calculation(s) they currently track for purposes of identifying HVCRE Exposures. The proposal allows banks to rely on their underwriting standards for exclusions from HVCRE that rely on calculating cash flows, debt service amounts and expense amounts. Similarly, the proposal should rely on LTVs that firms are already calculating and tracking in internal systems for LTV standards.

In addition, the proposal's requirement to rely on "as-completed" LTV introduces a potential mismatch to common underwriting practices which may include commitment amounts to carry the project through stabilization. For example, a portion of the proceeds of construction loan may be designated for the "completion" of the project while a second portion is designated for the "stabilization" of the project. Stabilization generally includes (but is not limited to) tenant improvements and leasing costs. Therefore, when the full commitment of the construction loan (i.e. including stabilized loan amounts) is used against the "as complete" appraisal value of a project, the loan-to-value calculation may be overstated. Accordingly, if an "as-completed" valuation is required, the proposal should clarify that the numerator of the LTV ratio is the loan proceeds required solely for completion of the project.

Other items

- The proposal excludes from HVCRE Exposures any loan originally made prior to January 1, 2015. We seek additional clarity regarding loans that were originally made prior to January 1, 2015, but subsequently modified or extended in some way. Are such loans still excluded based on the statutory January 1, 2015 standard?

- We support the agencies' interpretation of the term "project" and believe it is reasonably clear. To further enhance clarity, an example from the agencies of the LTV and contributed capital calculations for an exposure that includes multiple draws and multiple projects would help ensure consistent application of any final rule.

- Finally, we support providing additional clarity within the rule text for terms on which the agencies provided interpretive views. The identification of HVCRE Exposures will still require significant effort and we believe implementation across firms should be as consistent as possible. To that end, we request additional clarity, in as many cases as possible.

Conclusion

We recommend the agencies eliminate the HVCRE Exposure category from the capital rules. We believe that this suggestion is consistent EGRRCPA, cost/benefit analysis, and the manner in which other types of loans are treated by the capital rules.

We appreciate the opportunity to comment on the proposal and are available to provide additional input or clarifications as you proceed with further deliberations on this topic. If you have any questions, please contact me at (980) 260-6434.

Sincerely,

[redacted]

Richard D. Levy