June 7, 2021

MEMORANDUM TO: Board of Directors

FROM: Doreen R. Eberley
Director
Division of Risk Management Supervision

SUBJECT: **Notice of Proposed Rulemaking: Real Estate Lending Standards**

Summary of Recommendation

Staff recommends the Board of Directors of the Federal Deposit Insurance Corporation (FDIC) approve and authorize publication in the *Federal Register* the attached Notice of Proposed Rulemaking: Real Estate Lending Standards (NPR) for a 30-day comment period. The NPR proposes to amend the Interagency Guidelines for Real Estate Lending Policies[1] (Real Estate Lending Standards) to calculate the ratio of loans in excess of the supervisory loan-to-value limits (LTV Limits) using tier 1 capital plus the appropriate allowance for credit losses[2] in the denominator. The purpose of the NPR is to align the Real Estate Lending Standards with the community bank leverage ratio (CBLR) rule,[3] which does not require electing institutions to calculate tier 2 capital or total capital. The proposed revision would provide a consistent approach for calculating the ratio of loans in excess of the supervisory LTV Limits at all FDIC-supervised institutions and also avoid any regulatory burden that could arise if a FDIC-supervised institution subsequently decided to switch between different capital frameworks.

CONCUR:

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Nicholas J. Podsiadly
General Counsel

[1] FDIC: 12 CFR Pt. 365, App. A, Subpart. A

[2] Banking organizations that have not adopted the current expected credit losses (CECL) methodology will use tier 1 capital plus the allowance for loan and lease losses as the denominator. Banking organizations that have adopted the CECL methodology will use tier 1 capital plus the portion of the allowance for credit losses attributable to loans and leases.

Supplementary Information

Background

The Real Estate Lending Standards, which were issued pursuant to section 304 of the Federal Deposit Insurance Corporation Improvement Act of 1991, 12 U.S.C. 1828(o), prescribe standards for real estate lending to be used by FDIC-supervised institutions in adopting internal real estate lending policies. The FDIC recognizes the LTV Limits as one of several pertinent credit factors to be considered when prudently underwriting a real estate loan. The current Real Estate Lending Standards establish supervisory LTV criteria for various real estate lending transaction types, but also allow exceptions to the supervisory LTV Limits. The Real Estate Lending Standards also establish an expectation that institutions limit LTV exceptions, measured against total capital, as defined in the footnote to the Real Estate Lending Standards to be equivalent to that defined in the capital rules.

Section 201 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA), Pub. L. 115-174, 132 Stat. 1296 (2018), amended provisions in the Dodd-Frank Wall Street Reform and Consumer Protection Act relative to the capital rules administered by the agencies. The CBLR rule was issued by the FDIC, the Board of Governors of the Federal Reserve System (FRB), and the Office of the Comptroller of the Currency (OCC) to implement section 201 of the EGRRCPA, and it provides a simple measure of capital adequacy for community banking organizations that meet certain qualifying criteria.[4]

Proposal

The NPR would conform the method for calculating the ratio of loans in excess of the supervisory LTV Limits, as set forth in the Real Estate Lending Standards, with the capital framework established in the CBLR Rule. In the Real Estate Lending Standards, total capital is the denominator used to calculate the ratio of loans in excess of the supervisory LTV Limits. However, qualifying community banking organizations[5] that elect the CBLR framework (Electing CBOs) are not required to calculate or report tier 2 capital or total capital.[6] Under the proposal, the Real Estate Lending Standards would be amended so as to calculate the ratio of loans in excess of the supervisory LTV Limits using tier 1 capital plus the appropriate allowance for credit losses[7] in the denominator.

The proposed revision would provide a consistent approach for calculating the ratio of loans in excess of the supervisory LTV Limits at all FDIC-supervised institutions. The proposed revision

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[4] 85 Fed. Reg. 64003 (Oct. 9, 2020).

[5] The CBLR rule defines qualifying community banking organizations as depository institutions and depository institution holding companies with less than $10 billion in total consolidated assets and that meet other qualifying criteria, including a leverage ratio (equal to tier 1 capital divided by average total consolidated assets) of greater than 9 percent.

[6] *See* the CBLR rule at 12 CFR 324.12. Total capital means the sum of tier 1 capital and tier 2 capital. *See* 12 CFR 324.2

[7] Banking organizations that have not adopted the current expected credit losses (CECL) methodology will use tier 1 capital plus the allowance for loan and lease losses as the denominator. Banking organizations that have adopted the CECL methodology will use tier 1 capital plus the portion of the allowance for credit losses attributable to loans and leases.

also would approximate the historical methodology specified in the Real Estate Lending Standards for calculating the ratio of loans in excess of the supervisory LTV Limits without creating any regulatory burden for Electing CBOs and other banking organizations. Further, the proposed revision would avoid any regulatory burden that could arise if Electing CBOs subsequently decided to switch between the CBLR framework and the generally applicable capital rules. Staff is proposing to amend the Real Estate Lending Standards only relative to the calculation of loans in excess of the supervisory LTV Limits, due to the change in the type of capital information that will be available, and is not proposing any revisions to other sections of the Real Estate Lending Standards.

The proposed revision to the calculation of loans in excess of the supervisory LTV Limits would provide regulatory burden relief, because with the changes in the capital information available after the implementation of the CBLR rule, CBLR institutions are not required to report tier 2 capital, which is part of "total capital." Changing the reference to "total capital" further supports the burden relief efforts of the CBLR rule as it ensures that institutions that have elected the CBLR framework are not disadvantaged. The proposed revision would ensure the approach for calculating the ratio of loans in excess of the supervisory LTV Limits is consistent for all FDIC-supervised institutions, regardless of the institution's CBLR election status.

Staff proposes to make all provisions of the rule effective upon publication of the final rule in the Federal Register. The Administrative Procedure Act (APA) allows for an effective date of less than 30 days after publication "as otherwise provided by the agency for good cause found and published with the rule."[8] The purpose of the 30-day waiting period prescribed in APA section 553(d)(3) is to give affected parties a reasonable time to adjust their behavior and prepare before the final rule takes effect. Staff believes that this waiting period would be unnecessary as the proposed rule would lift burdens, as noted above. Consequently, staff believes it would have good cause for the final rule to become effective upon publication.

Lastly, even though the Real Estate Lending Standards were issued on an interagency basis, each agency has its own agency-specific language for its institutions in the Real Estate Lending Standards with respect to the definition of "total capital." Accordingly, the FDIC would be able to update its agency-specific Real Estate Lending Standards independent of the FRB and the OCC.

Recommendation

Staff recommends that the Board approve the attached Resolution to authorize publication of the attached Notice in the *Federal Register* for public comment.

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Attachments

[8] 5 U.S.C. 553(d)(3).