April 13, 2006

VIA FACSIMILE AT 202/452-3819
4448
Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitutional Ave. NW
Washington, DC 20551
Docket No. OP-1248

VIA FACSIMILE AT 202/874-
Office of the Comptroller of Currency
250 E Street, SW Mail Stop 1-5
Washington, DC 20219
Docket No. 06-01

VIA EMAIL AT COMMENTS@FDIC.GOV
6518
Federal Deposit Insurance Corporation
Mr. Robert E. Feldmen, Executive Secretary
550 17th Street, NW
Washington, DC 20429

VIA FACSIMILE AT 202/906-
Office of Thrift Supervision
Regulation Comments Chief Counsel's Office
1700 G Street, NW
Washington, DC 20552
Docket No. 2006-01

RE: Proposed Interagency Guidance on Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices. FRB Docket No. OP-1248, OCC Docket No. 06-01, and OTS Docket No. 2006-01.

Dear Sirs and Madams:

The Wisconsin Bankers Association (WBA) is the largest financial institution trade association in Wisconsin, representing 310 state and nationally chartered banks, savings and loan associations, and savings banks located in communities throughout the state. WBA appreciates the opportunity to comment on the proposed interagency guidance on concentrations in commercial real estate lending.

The Board of Governors of the Federal Reserve System (FRB), Office of the Comptroller of Currency (OCC), Federal Deposit Insurance Corporation (FDIC), and Office of Thrift Supervision (OTS)(collectively, the Agencies) have proposed an interagency guidance on commercial real estate (CRE) lending. The guidance seeks to create two new thresholds of CRE lending, which, if met, requires a

4721 SOUTH BILTMORE LANE
MADISON, WI 53718
P.O. BOX 8880
MADISON, WI 53708-8880
608-441-1200
FAX 608-661-9381
www.wisbank.com

financial institution to heighten its risk management practices and increase its capital. While WBA strongly supports the importance of sound CRE lending, WBA recommends the proposed guidance be withdrawn and instead recommends the Agencies utilize current policies and examination procedures to better address the concerns of the Agencies.
If the Agencies are unwilling to do so, the proposed guidance should then be modified to remedy the following concerns: (1) the definition of CRE is too broad; (2) the proposed thresholds are too restrictive; (3) the parameters which trigger an Agency's use of the CRE guidance in an examination are not clearly defined; and (4) the proposed additional portfolio risk monitoring and assessment procedures are too burdensome for management. To help the Agencies address these concerns, WBA offers the following comments.

The proposed definition of CRE is overly broad and inappropriately results in a one-risk-fits-all approach to commercial real estate lending.

In the proposed guidance, the Agencies define CRE loans in the following manner:

> [E]xposures 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 (that is, loans for which 50 percent or more of the source or repayment comes from third party, non-affiliated, rental income) or the proceeds of the sale, refinancing, or permanent financing of the property.

A common denominator in each loan listed above is that each is secured by commercial real estate. This simple commonality should not, however, equate to an assumption that each loan imposes the same heightened risk for an institution. Take, for example, a CRE loan intended for the construction and development of a commercial office and retail space and compare it to a CRE loan intended for the construction and sale of a 1-4 family residential building. The CRE loan for the office and retail space not only has the typical risks associated with construction in general, but also has risks associated with occupancy/vacancy issues, renter turn-over, and market saturation. Typically the repayment source of such a loan is largely from rent collected from its commercial tenants, which, if the space is not fully occupied, may cause the developer greater repayment concerns. These factors impact the ability and promptness for CRE loan repayment and may possibly increase the potential risk to an institution.

Now compare this with the 1-4 family residential construction. While these CRE loans also struggle with similar general construction risks as that of the office and retail space construction, 1-4 family residential constructions have historically posed less overall risk. This is due to quicker occupancy, less renter turn-over, and less overall vacancy. Many 1-4 family residential constructions are built under contracts to purchase with permanent financing in place. This results in immediate occupancy by the consumer and for the institution, repayment of the debt obligation. Hence, such transactions pose minimum risk to the institution.

Despite the clear difference of risk level in these transactions, the inclusion of 1-4 family residential construction results in a defacto one-risk-fits-all approach. Simply put, the definition is too broad. To remedy this issue, WBA recommends the CRE definition be revised to exclude 1-4 family residential construction loans, as the risk for these loan transactions does not rise to a level that requires additional management review and increased capital reserves.

<u>If the Agencies fail to remove 1-4 family residential constructions from the CRE loan definition, the proposed thresholds should then be increased, and modifications made to recognize an institution's existing risk management and internal controls.</u>

The Agencies have outlined in the proposed guidance two thresholds for determining whether a financial institution has a concentration in CRE lending warranting use of heightened risk management practices. The first threshold is identified as total reported loans for construction, land development, and other land which represents one hundred percent (100%) or more of the financial institution's total capital. The second threshold is that of total reported loans secured by multifamily and non-farm nonresidential properties and loans for construction, land development, and other land representing three hundred percent (300%) or more of the financial institution's total capital. Under the proposal, institutions exceeding these thresholds are deemed to have a concentration in CRE and must therefore have heightened risk management practices in place.

If 1-4 family residential constructions remain in the CRE definition, they will be included in the threshold calculations causing many institutions to quickly exceed these thresholds. WBA fears this will cause a large number of institutions to be subjected to the additional burdens proposed in the guidance regardless of how well an institution is currently managing and controlling the risks related to CRE lending. As a result, institutions would incur additional costs due to new monitoring requirements and would likely decrease the volume of such lending despite local communities' credit needs. If 1-4 family residential constructions remain in the CRE loan definition, WBA urges the Agencies to revise the guidance to increase the proposed threshold percentages.

Additionally, these two proposed thresholds fail to take into consideration the location or size of the institution, or its total loan portfolio makeup. Under the proposed guidance, any institution falling into either proposed threshold would be subject to additional management scrutiny and increased capital requirements with no consideration for the institution's existing risk management and internal controls used to monitor its lending practices and control risk. Modification of the guidance must be made to recognize an institution's existing risk management strategies and internal control mechanisms, and to ensure that all institutions are impacted fairly taking into account their location, size, current internal procedures, and employee resources.

The Agencies need to clarify the terms "sharp increase", "short period of time", and "significant concentration" so institutions understand when the guidance will be applied in examinations.

In the proposed guidance, the Agencies have stated examiners are to apply the guidance "on a case-by-case basis to any institution that has had a sharp increase in CRE lending over a short period of time or has a significant concentration in CRE loans secured by a particular property type." Without clearer definitions to these terms, an institution may be unprepared to be examined according to the guidance requirements since an institution is left guessing about an examiner's interpretation and application of these terms. For instance, just what percentage increase in an institution's loan volume constitutes a "sharp increase?" How many months or years are to be taken into calculation to determine what is "a short period of time?" Or how many loan transactions secured by a particular property type does it take for an institution to now be considered to have a "significant concentration?" WBA recommends the Agencies more clearly define these terms to allow an institution the ability to plan, strategize and alert management that the institution will be subject to the additional proposed guidance requirements.

The additional regulatory review and monitoring requirements need to be revised to recognize current internal procedures, avoid duplication, and reduce regulatory burden.

The Agencies have provided a laundry list of activities that an institution's board of directors and staff must actively review and implement when the institution determines a high CRE threshold has been met. In particular, the proposal calls for: (1) review of market condition reports; (2) director-issued guidance; (3) review of risk exposure limits; (4) CRE strategic plans; (5) additional risk assessment and monitoring of CRE loans; (6) enhanced underwriting and much more. This additional regulatory burden is required without recognition of current internal procedures and controls, review of history of losses, current management of CRE portfolio, or current bank reserves. WBA is concerned that these additional requirements will strain the limited staff and economic resources of smaller institutions as not only will they need to ensure compliance with the new guidance but also continue with existing management and portfolio risk assessment requirements, thus placing them at a competitive disadvantage.

For all of the above-stated reasons, WBA recommends the Agencies reconsider implementation of this proposed guidance. WBA strongly believes the Agencies should utilize current policies and examination procedures to better address the concerns of the Agencies.

However, if the Agencies decide to adopt the proposed guidance, WBA strongly suggests: (1) revision of the CRE definition to remove 1-4 family residential constructions; (2) increase the threshold percentage calculations if 1-4 family residential construction is to remain in the CRE definition; (3) clearly indicate when the proposed guidance is to be used; and (4) shorten the number of additional management oversight requirements to make the guidance easier to implement and less burdensome.

Once again, WBA appreciates the opportunity to submit comments on the proposed interagency guidance.

Sincerely,

Kurt R. Bauer
President/CEO