

TEL 770 805-2000  
800 277-2265



FAX 770 805-2121

2410 PACES FERRY ROAD  
600 PACES SUMMIT  
ATLANTA, GA 30339-4098

Ms. Jennifer J. Johnson  
Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> Street and Constitution Avenue, NW  
Washington, DC 20551

Office of the Comptroller of the Currency  
250 E Street, SW  
Mail Stop 1-5  
Washington, DC 20219

Mr. Robert E. Feldman  
Executive Secretary  
Attention: Comments  
Federal Deposit Insurance corporation  
550 17<sup>th</sup> Street, NW  
Washington, DC 20429

Regulation Comments  
Chief Counsel's Office  
Office of Thrift Supervision  
1700 G Street, NW  
Washington, DC 20552  
Attention: No. 2006-01

Ladies and Gentlemen:

The Bankers Bank appreciates the opportunity to comment on the Agencies' Proposed Guidance entitled "Concentrations in Commercial Real Estate Lending, sound Risk Management Practices" (the "Guidance"), published in the January 12, 2006 issue of the Federal Register. Our institution is a State of Georgia chartered financial institutional and a Federal Reserve member.

The Bankers Bank provides a full range of correspondent banking services to approximately 1100 financial institutions located primarily in the southeastern United States.

## Summary of our Comments:

We welcome that portion of the Guidance that addresses the importance of maintaining effective internal controls and risk management practices to safeguard financial institutions from excessive and highly leveraged credit exposure to the commercial real estate sector. We respectfully suggest, however, in light of the matters more fully discussed below, that the financial services industry would be better served if this guidance were distributed in the form of an Advisory Letter setting forth recommended "Best Practices" in respect to commercial real estate lending.

### **Formal rule-making proceeding is not appropriate**

Based upon experience, historical loss factors, and general state of capital throughout the banking sector, we are not persuaded that there is sufficient evidence to justify the Agencies in imposing, on all insured institutions, an arbitrary requirement that financial institutions maintain additional capital to support concentrations in commercial real estate loans. We view the Guidance to single out commercial real estate for no reason other than media coverage, inconsistent economic forecasts and isolated instances at a nominal number of banks.

Further, despite proven quality over time, documented improvement in underwriting practices, and record high capital positions throughout the industry, the Agencies have not elected to take a position in allowing banks to apply less than 100% Risk Based Capital to those asset classes (i.e. community bank financial institutions), that have exhibited historically low-to-nonexistent credit losses. Furthermore, in light of evidence suggesting Commercial and Industrial loans have exhibited higher absolute dollar losses over the last five years, the Agencies have not accounted for this fact in their application of the Proposed Guidance.

Although the proposed Guidance does not explicitly refer to the Basel Capital Accord, it is apparent that adoption of the Guidance would be a significant step toward imposing on all insured institutions the stricter capital standards that the Accord mandates in respect to the commercial real estate segment of institutions' loan portfolios. However, the Guidance does not provide the ability of the commercial bank to prove a Risk Based Capital allocation of less than 100% may be appropriate. We believe that, especially in respect to those domestic financial institutions that have less than \$20 billion in assets, subjecting them to requirements contained in the Accord would be neither necessary, nor beneficial for the institutions, their depositors, or their shareholders. In fact, if enforced, the proposed Guidance would have material adverse impact on the financial condition of community banks for no other reason other than an arbitrary ceiling was breached.

It is further our view that the widely varying conditions that may be found in the respective real estate markets in which such institutions operate mean that, in those instances in which such vulnerabilities do occur, they are more likely to be successfully rectified by more tightly focused supervision measures that are based upon, and tailored

to address, the particular institution involved and the local conditions from which its problem arise. If isolated instances of concern should arise from credit concentrations that have not been adequately addressed by the traditional supervision and examination processes, we suggest that the Agencies have available to them a wide range of other effective remedies and enforcement statues and strategies.

### **The Guidance fails to recognize existing controls**

We are concerned that the guidance fails to recognize the utility and effectiveness of existing controls, such as, but not limited to:

1. Policy
2. Underwriting Standards
3. Market Analysis
4. Stress Testing
5. Reporting
6. Loan Review
7. Safety and Soundness Exams,
8. External and Internal Audits
9. Historical Performance

A one-size-fits-all approach would impose potentially unnecessary and counterproductive mandates on institutions within the community banking group that have proven consistent risk management techniques over time.

Every community bank must be sensitive to, and must respond accordingly to, the credit needs of the community or communities it serves. We agree that the board of directors of each institution, through its formation and adoption of the institutions strategic direction, must determine how that institution will serve its community. Moreover, each board recognizes that it must assess the risks inherent in the various roles that the institution seeks to fulfill. There are a variety of methods and tools that institutions may employ to mitigate risk, although the Guidance focuses primarily on additional capital and monitoring.

A vital aspect of effective monitoring is the role played by both the internal and external audit functions. The Guidance fails to acknowledge the significant effects that have flowed from recent legislative and other measures designed to improve corporate record keeping, monitoring and governance.

### **The Guidance overemphasizes institutions vulnerability to commercial real estate**

While we share the Agencies' concern for the maintenance of safety and soundness in the operations of insured financial institutions, we believe that the proposed Guidance unreasonably exaggerates the potential exposure of those institutions to weaknesses in the commercial real estate sector, by essentially applying a liquidation of commitment approach, rather than a margined sales approach, to ultimate exposure calculations.

It is generally recognized for example that the recession of 1989-90 resulted in the failure of a number of financial institutions, both large and small, which held significant concentrations of commercial real estate loans. It is also generally recognized that the collapse of the real estate industry during that period was due in large measure to significant changes that had been enacted in federal tax laws in 1986, which resulted, among other things, in the reduction or complete abolition of substantial tax benefits that previously had been available to investors in commercial real estate projects.

We are unaware, however, of any financial institution failure over the past decade that has been attributable to a concentration of credit in real estate or in any other economic sector. To the contrary, it is our understanding that the principal underlying causes of bank failures over the past fifteen years have been fraud, abuse, or other unlawful conduct, on the part of bank management and, on occasion, bank customers.

Such deliberate wrongful conduct would be neither deterred nor prevented by the Guidance of by any other supervision measure. If there should be a threat to the safety and soundness of any financial institution that arises from weakness in real estate markets, it is our view that the best way to create an effective safeguard against such threats would be by seeking to ensure, through traditional supervisory processes, that every institution has in place, and consistently makes use of, effective management supervision, reliable internal controls, including reporting and monitoring mechanisms, and effective credit analysis and underwriting processes.

### **The proposed thresholds are arbitrary and would cause unnecessary corrective measures**

The propose Guidance would impose “heightened risk management practices” on any institution that has either (1) total reported loans for construction, land development, and other land that equal or exceed 100% of capital, or (2) total reported loans secured by multifamily and non-farm, nonresidential properties, together with construction and land development and other land, that equal or exceed 300% of capital

We believe that these thresholds are not commensurate with the levels of actual risk for institutions that adhere to the Agencies’ *existing regulations* and guidelines on real-estate lending, and that employ careful and consistent credit analysis and underwriting standards that are appropriately based upon knowledge of the real estate markets in which the institution, and its borrowers operate. Since these are loans that are secured by tangible, hard collateral, we believe that more appropriate threshold levels of exposure to commercial real estate, which would warrant enhanced attention. Approaches may include, but not be limited to:

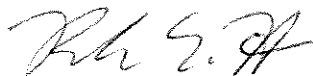
1. Targets based on stressed exposure to capital.
2. Concentration targets based on property type, markets, maturity, and LTV

### **Conclusion**

It is not our intention to deny or disregard the risks faced by financial institutions that engage to a significant degree in lending to the commercial real estate sector. We recognize and acknowledge that credit concentrations can impair and impede safe and sound operation and are a proper subject of supervisory concern. At the same time, the characteristics of commercial real estate markets vary widely throughout the nation, and management of risks attendant upon extending credits in those markets is particularly dependent upon thorough knowledge and understanding of, and experience in, those markets, as well as knowledge of the banks, businesses and individuals that do business in them.

For financial institutions that make use of their knowledge of the markets that they serve, and that exercise care to maintain effective management supervision, internal controls, and underwriting standards; adoption of the proposed Guidance would produce little if any benefit. For institutions that subject themselves to enhanced real-estate risk by poor underwriting practices, inattention to markets, or inadequate concentration reporting, or other undesirable practices, such weaknesses would be more properly, and more effectively, rectified through the traditional supervisory and examination process.

Respectfully Submitted,

A handwritten signature in dark ink, appearing to read "Brock E. Fredette". The signature is fluid and cursive, with the first letters of the first and last names being capitalized and prominent.

Brock E. Fredette  
Chief Credit Officer  
The Bankers Bank