

March 9, 2006

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G. Street, NW
Washington, DC 20552

Attn.: Docket No. 2006-01

Re: Proposed Guidance – Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices
71 FR 2302 (January 13, 2006)

Dear Sir or Madam:

First Niagara Bank (“First Niagara”) appreciates the opportunity to comment on the Proposed Guidance – Concentrations in Commercial Real Estate (“CRE”) Lending, Sound Risk Management Practices (“Proposed Guidance”) issued by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of Thrift Supervision (collectively, the “Agencies”).

Commercial real estate lending (which includes 1-4 family construction lending to local area builders within the geographic confines of our defined CRA assessment areas) has been both a core competency as well as an integral part of First Niagara’s successful community lending practices for at least the past 25 years.

As such, and given our bank’s continued strategic focus on this higher yielding and interest rate sensitive line of business, we certainly reinforce the Agencies’ position that “institutions should have in place risk management practices and capital levels appropriate to the risk associated with these concentrations” and further endorse the Agencies’ prudence in reinforcing the need for sound underwriting by issuing a compilation of previously issued guidelines for safe and sound commercial real estate programs.

First Niagara believes, however, that the proposed guidance of introducing threshold tests for assessing a bank’s commercial real estate concentration is arbitrary in nature and will not accomplish the Agencies’ goal of identifying banks that might be adversely impacted by their commercial real estate portfolios in an economic downturn.

Banks like First Niagara, which, through the careful and well designed implementation of Risk Management Principals, including Board and Management Oversight, Strategic Planning, Underwriting, Risk Assessment, and Monitoring of CRE loans, Portfolio Risk Management, Management Information System Concentrations, Market Analysis, Stress Testing, and Capital Adequacy, have already taken the necessary steps to implement and put into practice these sound risk management practices to properly insulate their commercial real estate portfolios from an economic downturn.

The proposal also calls for lenders with concentrations of commercial real estate loans to increase their capital levels above regulatory minimums. First Niagara believes that such increased levels, if any, should be imposed by regulations through the ongoing implementation of “Risk Based Capital” rules.

CRE Concentration Tests

First Niagara believes that the proposed CRE concentration thresholds are inappropriate and arbitrary, as they totally disregard differences in the compositions, credit histories, and other salient characteristics of each individual lender’s CRE portfolio. First Niagara believes that each individual bank should continue to be evaluated on a case-by-case basis as part of the ongoing annual Safety & Soundness Exam process where the current CAMEL rating analysis sufficiently addresses asset quality, management, and capital adequacy. The exam process already includes a thorough review of a bank’s commercial real estate lending policies and procedures, historical losses and delinquency trends, the composition of the CRE portfolio by product type and geography, borrower concentration exposure, including classified loans with appropriate risk ratings and loss allocations, the quality of underwriting, and the level of risk management controls already in place at each bank.

First Niagara believes that the Agencies have erred in their proposal to bundle all types of CRE lending into a single, uniform risk classification for purposes of threshold testing as each unique product type or segment of commercial real estate lending contains varying degrees of risk inherent to that particular product or market segment. As such, it is important to segregate the granting of loans for the acquisition of raw land or acquisition and development subdivision lending, speculative (“spec”) lending for both single-family home construction and commercial development, and the granting of unsecured “guidance” line facilities for commercial real estate developers as completely separate and distinct to the funding of permanent commercial real estate loans within the bank’s portfolio that have established cash flow debt service coverage ratio’s already in place, combined with satisfactory levels of personal guaranties from well established developers with proven property management track records, liquidity, adequate global cash flow, net worth, etc.

In analyzing historical risk profiles and loss history associated with commercial real estate and construction lending, First Niagara is firmly of the opinion that the proposed CRE definition should entirely exclude multi-family mortgages and pre-sold single-family residential

construction loans to builders with both non-contingent sales contracts and permanent lender take-out commitments already in place from the proposed threshold test. In their proposed guidance, the Agencies have completely disregarded the historical fact that, for community bank “relationship lenders” such as First Niagara, which primarily lend in their own CRA assessment areas to either well known local property owners or established developers on well seasoned multi-family or apartment projects with established performance for occupancy and operating expenses already in place, that these loans have significantly less risk than other traditional CRE product types such as office, retail, warehouses/industrial, hotels, etc.

In fact, at First Niagara, and I am convinced the following would hold true for the majority of community banks within both our respective New York Bankers Association and America’s Community Bankers trade associations, that multi-family charge-off losses have actually been below the level of losses experienced in our equally conservative and well underwritten 1-4 family loan portfolio.

To reinforce that position, please refer to Exhibit I which compares First Niagara’s historical loss experience of both multi-family and 1-4 family lending over the last five years. Additional loss experience data could be made available upon request. (Attachment)

Unless the Agencies can provide clear loss history to the contrary with respect to regional community banks such as First Niagara, which lend exclusively within their own state boundaries, there is absolutely no compelling reason to include multi-family loans as part of the proposed thresholds test. Our current real estate portfolio is \$1,882,500,000 and multi-family loans have historically comprised no less than 30-40% of First Niagara’s total CRE portfolio. Reinforcing our loss history over the last 15 years, First Niagara has had only one piece of owned real estate, resulting from a foreclosure on a multi-family property, which was over ten years ago in Lockport, New York. This was an eight-unit apartment complex loan with a balance of less than \$400,000 where the final charge-off was less than \$40,000. With respect to economic downturns, it is also important to note that multi-family housing has historically continued to perform very well in times of high interest rates, which results in increasing occupancy levels at apartment projects, as higher rates significantly decrease the pool of eligible homebuyers who then are more likely to rent than own as they become priced out of home ownership opportunities.

With respect to First Niagara’s similar historical loss experience in 1-4 family construction lending, the bank has, over the last 15 years, never suffered a loss on a single-family, residential construction loan to a bank-qualified builder where the bank had lent to the builder based on the existence of a non-contingent sales contract with a firm end-loan take-out commitment firmly in place. Over that same time period, there have been conservatively less than half a dozen instances where the borrower applicants defaulted under the terms of a new construction sales contract for a house under construction and financed by the bank. In all cases, the builder was able to resell the completed house to another buyer and repay the bank’s construction loan in

full. As such, this defined category of 1-4 family CRE construction loans should also be excluded from the threshold test.

In addition to these historical loss levels, which clearly demonstrate a compelling case for the exclusion of these two product lines, it is interesting to note that, by statute, the OTS has already conceded that the current risk-rating for these two product lines with a 50% risk weighting is equal to that of traditional 1-4 family residential loans.

It also seems incongruous that when the cornerstone of our original thrift chartered mission at First Niagara, was and still is to provide affordable housing and to make possible the American dream of home ownership to the communities we serve, (which has been further reinforced over time with Congress passing supporting CRA regulations to ensure that we are, in fact, providing both adequate levels of single-family and multi-family housing to our local communities), the Agencies would, in effect, now be looking to limit or restrict our ability to make these very loans we are required to make under the CRA lending test, when First Niagara has a proven credit-oriented track record of underwriting these product lines with resultant historical average loss ratios of just two basis points over the last 15-year period.

CRE Risk Management Principles

The proposed guidance very clearly and succinctly outlines the Agencies' view of what constitutes a "sound commercial real estate lending program". All of these underlying principles are, in fact, currently imbedded in First Niagara's Commercial Real Estate Policy, which is annually reviewed and approved by the Board of Directors, and is consistent with the Allowance for Loans and Leases Losses ("ALLL") Guidelines set forth on July 6, 2001 by the Federal Financial Institutions Examination Council "Policy Statement on Allowance for Loan and Leases Losses Methodologies and Documentation for Banks and Savings Institutions".

Given our ongoing adherence to these previously issued guidelines for safe and sound commercial real estate programs, when coupled with ongoing compliance with risk assessment programs, the requirement that community banks, such as First Niagara, routinely "stress test" their entire CRE portfolio is simply not practical. Again, community banks who lend in-state, within the geographic confines of their own local CRA assessment areas, know the economic demographics of their own areas and underwrite accordingly. There have been no recent commercial real estate bubbles in the Upstate New York geographic confines of Buffalo, Rochester, Syracuse, Rome, Schenectady, or Troy over the last 15-20 years, and First Niagara is selective in dealing in our local markets with borrowers and guarantors who have been successful in both developing and maintaining commercial real estate portfolios in their respective areas of expertise.

As part of sound risk management policy, First Niagara Bank at time of origination, as part of our standard loan approval underwriting process, stress-tests each individual real estate loan to quantify both the maximum interest rate and vacancy level exposure for each individual credit, in

addition to the thorough analysis of both the global cash flow and net worth of the borrower to quantify their capacity to provide supplemental cash flow to an individual credit.

Conclusion

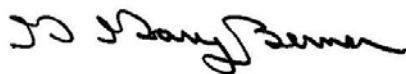
Commercial real estate lending is a critical component that plays a key role, not only to First Niagara's balance sheet and profit and loss statement, but to all community banks. Continuing our ongoing role in commercial real estate lending is an essential component to maintaining the health of our local economies, and continuing to provide the necessary extension of credit to the communities we serve, and will ensure a steady stream of capital to finance and maintain our respective local affordable housing markets.

Any guidance that imposes additional capital requirements in a purely arbitrary and mechanical manner could easily lead to major policy shifts in the lending patterns of community banks such as First Niagara, which could discourage the current critical role that CRE lending plays in the revitalization of our urban city centers throughout Upstate New York as well as having a detrimental impact on the replacement of our aging housing stock.

For the reasons described above, First Niagara recommends that the Agencies avoid imposing arbitrary threshold tests that, as proposed, would ignore the actual historical risk factors associated with each individual bank's loan portfolio.

First Niagara appreciates the opportunity to comment. If you have any questions, please contact the undersigned at 716/625-7504 or Gary.Berner@FNFG.com.

Sincerely,

A handwritten signature in black ink, appearing to read "G. Gary Berner". The signature is written in a cursive, flowing style.

G. Gary Berner
Executive Vice President & Chief Lending Officer

First Niagara Financial Group, Inc.
 Real Estate Charge Offs
 2001-2005

Exhibit I

| Year | 1-4 Family Chargeoffs | Average Portfolio Balance | Basis Points %/Port | Multi-Family Chargeoffs | Average Portfolio Balance | Basis Points %/Port |
|------|-----------------------|---------------------------|-------------------------------|-------------------------|---------------------------|-------------------------------|
| 2001 | 382,000 | 1,046,311,000 | 0.0004 | 65,100 | 122,553,500 | 0.0005 |
| 2002 | 370,000 | 929,411,000 | 0.0004 | 129,208 | 151,898,000 | 0.0009 |
| 2003 | 518,000 | 981,905,000 | 0.0005 | 13,710 | 234,205,000 | 0.0001 |
| 2004 | 49,000 | 1,152,504,000 | 0.0000 | 10,404 | 385,644,000 | 0.0000 |
| 2005 | 192,000 | 2,131,415,000 | 0.0001 | 34,432 | 555,795,000 | 0.0001 |
| | <u>1,511,000</u> | | 0.0002 | <u>252,855</u> | | 0.0002 |
| | | | 5 yr. Weighted Average | | | 5 yr. Weighted Average |