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Subject: Commercial Real Estate Lending

We would like to offer the following comments for your consideration in connection with the proposed guidance on commercial real estate concentrations (Docket OP-1248). We believe that the proposed guidance is not necessary or, if enacted, should be revised to consider the matters discussed below.

1. The category "Commercial Real Estate" is overly broad and so is not closely tailored to address the risks to be monitored under this regulation. The perception of heightened risk in commercial real estate concentration arises because of the interrelationship of the values of different commercial real estate properties; in other words, the concern is that problems in a few commercial real estate loans can cascade and cause problems in a much larger portfolio of loans. More specifically, if a few properties are foreclosed upon, these distress sales negatively impact the value of other commercial real estate. Because of this cascading effect, it is argued that a high concentration of commercial real estate loans can be riskier than one might otherwise think as compared to what one might conclude when reviewing loans on an individual basis.

We do not believe however that any cascading effect necessarily has a substantial cross over effect between different segments of commercial real estate loans. For example, if there is a glut of office buildings, this does not necessarily spill over and have a large impact on the rent for industrial space. In a city such as Los Angeles, even a glut of office space in one sub-market may not have much effect on the rents for office space in another sub-market. Similarly, changes in the value of hotels may not closely correlate with the value of strip shopping centers. The correlation, if any, would likely be no more than the general correlation between the overall health of an economy in a region and the credit worthiness of all businesses in the area.

We believe that the correlation between these different market segments should be studied more carefully before lumping all commercial real estate together. More meaningful risk management monitoring would we believe focus only on high concentrations in particular CRE segments, such as hotels.

2. Although the commentary on the proposed regulations states that banks are not being limited in making CRE loans or discouraged from doing so, this will be the inevitable although unintended effect of the regulations. The need to hold higher capital merely because one has a higher concentration of real estate loans will discourage banks from making these loans as it will be more costly for the bank to do so. The threat of this alone is enough to discourage lending.

One result of discouraging lending in commercial real estate is that the capital used by banks currently for this purpose will need to be deployed elsewhere. In order to use this capital and maintain profits, banks will feel pressure to expand lending in other areas where the risks might be even greater or the expertise of the bank not as great. There are only a limited number of safe and sound commercial loans. Accordingly, the unintended effect of these regulations may be to force banks to find new niches in perhaps factoring or "creative" home loans or other riskier areas where potential losses are much higher. Banks make real estate loans not because they are so profitable (the margins are not high compared to other commercial

loans) but because the loans are safe and there is a need for the loans. Pushing banks into finding new lending niches they do not want to be in is not a sound policy.

The regulations will also have the unintended effect of further marginalizing banks as financial intermediaries in the Untied States. Commercial real estate is an area where banks have been able to compete against the non-banks and at the same time to promote community development. Regulations that make it harder for banks to compete in this area may result in the conduit and Wall Street lenders becoming more dominant in this market place. These lenders are less patient and ready to support the community in economic downturns and their increased involvement and market share is likely to exacerbate fluctuations in real estate values and make worse one of the problems the regulations try to solve.

3. Many of the banks with high commercial real estate concentrations are in California. This is not an accident or because of a higher risk appetite by California banks. California banks have historically had a higher percentage of commercial real estate loans than banks in other parts of the country. There are many reasons for this. One reason is the high price of real estate in California, which in turn is related to the dynamic nature of the economy. Our economy is one of the main engines of economic growth in the country. Because real estate is relatively expensive, many businesses cannot afford to buy and so prefer to rent their space * one result of our dynamic small and new business oriented economy is accordingly that more property is rental as opposed to owner-user. The fact that many companies grow rapidly and find it hard to predict space needs, is another factor favoring renting. The proposed regulations view renting as a negative compares to the owner-user model, but do not seem to recognize that this is the nature of the California economy. By discouraging banks from making loans on rental commercial real estate property, the regulations are really trying to shift the basic business model that is part of the reason for California's success. This regulations to not seem to recognize this and do not distinguish between a rental industrial space in a large economy such as California where, even in downturns, a high rate of new business formation occurs, and rental industrial space in rust belt states where there are few new business start ups and filling up one space means luring a tenant out of another existing space. The proposed regulations should be reconsidered to evaluate these different circumstances and to recognize that a rule that makes sense for one area of the country may not make sense for another area of the country. California banks have historically had high CRE concentrations because there is a need for that in the local economy. Concentration is driven by local economic needs. Rather than trying to put all banks in country in the same mold, the regulations should recognize the success of the California economy and try to encourage what has been working well.

4. We believe that current safety and soundness and risk management guidance already adequately address any potential problems. As the commentary states, banks are already generally doing a good job underwriting and monitoring commercial real estate loans. Additional regulations to standardize monitoring and discourage such lending are, as discussed above, more likely to lead to unintended bad results than to solve any "problem."

5. Concentrations in other areas that are much larger that the CRE concentrations typical of many banks do not seem to be a concern. It seems unfair to penalize banks in this area and so, inadvertently, push other business models that are not as safe or as beneficial for the economy. The risk of CRE loan concentrations is said to be the cascading effect of defaults but similar situations arise for any bank that is specialized geographically (e.g., a one factory town in the mid-West), by industry (e.g., entertainment

or corporate trusts), or by customers (e.g., a bank owned by a brokerage firm or retailer). Rather than micro-managing specific risk management techniques and setting specific concentrations risks, it would seem worthwhile to consider letting existing regulations be used to allow a more risk focused assessment of each individual bank.

6. The regulations are not clear on how they relate to the risk management framework and capital ratio calculations of Basel II. Implementing specific requirements and practices for commercial real estate seems inconsistent with the general desire to put all banks worldwide on the same platform in terms of measuring capital and risk. For example, would a bank with a large concentration of real estate in Windsor, Canada have different capital and risk management requirements than a bank with the same concentration of real estate across the river in Detroit? Or if both banks had the same portfolio of real estate loans and concentrations in the United States, would they have different capital requirements because one is headquartered in the US and the other in Canada?

Thank you for your consideration.

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