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MARCH 8, 2006

To: Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System

From: Metropolitan National Bank, Little Rock, Arkansas
Submitted by Carl Roberts, SVP Loan Review

Subject: Comments on OCC Docket Number OP-1248 Proposed guidance on *Concentrations in Commercial Real Estate Lending, Sound Management Practices.*

Commenting on Background

The proposal states that the purpose of this guidance is to reinforce existing guidelines (i.e. 12 CFR 34) but does not state the underlying concern as to why reinforcement is suddenly necessary. One would assume that there is still a fear that lending practices which lead up to the crises in 1987-88 will be repeated. We do not believe this to be the case for the following reasons. First, Tax laws allowing heavy depreciation deductions on commercial real estate partnerships have changed removing the incentive for investors to borrow for unnecessary real estate ventures. Unlike many loans in the 80's, most loans now have valid purposes and fulfill a reasonable need in the economy. Also, given the strict enforcement of appraisal practices and loan to value limits, the *loss given default* is now generally much lower on CRE loans. Secondly, S& L's are now under the same regulations as banks, for this purpose, and if enforcement of the present regulation has been properly applied, a larger segment of the risk is now better monitored and controlled.

We think that the implementation of FIRREA and 12 CFR 34 (for national banks) has worked reasonably well over the past 12 years and will help avoid future crises of that magnitude.

The existing guidelines under 12 CFR 34 address the same issues as the proposed guidance. Supervision, risk management policies, policy tracking, board supervision, etc. are adequately covered in the present regulations. Another regulation to address the same issues is redundancy in its best form and would be confusing, at best, and potentially contradictory in interpretation.

Commenting on "Identification of Institutions with CRE Concentrations" p. 7:

We think that a commercial real estate loan, or for that matter, any type or size loan should receive the same conformity to *best practices* and good policies, whether or not it is officially a designated CRE loan. The proposal states that the "Guidance may be applied on a case by case basis" which implies that non-CRE loans or mixed collateral loans may be included, at will. This destroys the clarity of 12 CFR 34 and will result in further confusion in

identifying CRE loans as well as prohibit the uniform application of the guidance from bank to bank.

If it is determined that additional regulation is necessary for banks which truly have CRE concentrations, a much higher threshold would serve to better identify banks with true CRE concentrations and should be written *to supersede* 12 CFR 34.

***Commenting on "Strategic Planning"* the comparison of underwriting standards with those that exist in the secondary market." P.9**

Loans made in the secondary market are usually made with no reference to the borrower's total relationship. Funding sources are different and risk levels are intended to be different. Furthermore, secondary market terms change daily and are largely unavailable as a complete database. An occasional comparison is sometimes helpful but if this is made a requirement, banks would have lots of unavoidable, meaningless exceptions.

However, a practical way to lessen credit exposure is by selling participations in the primary market and this is not mentioned in the proposal.

Commenting on "Capital Adequacy" p. 5 and 12 para. 8

While we agree with the comments on capital adequacy, we question whether a discussion of capital adequacy belongs in additional guidance on CRE loans. This is already covered in guidance on risk-based capital and on the adequacy of the Allowance for Loan and Lease Losses (ALLL). The comment "an institution may need to maintain capital at levels exceeding the *well capitalized* standard to insure overall sound financial condition" implies an inadequate understanding of the purpose of risk-based capital and the ALLL. Our bank has a long history of providing adequate capital by recognizing the CRE concentrations as an integral part of the methodology in the ALLL. FAS5 indicates the need for this as does existing guidance from the regulators. A revision of the risk-rating method for CRE loans will be confusing, at best, and difficult to apply to existing ALLL methodologies. To have guidance on this, outside of that which is directly related to risk-based capital and the ALLL would be confusing and totally unnecessary. This comment seems to hint at having an extraordinary assessment of capital for an individual institution which would be unwarranted and unnecessary. The existing guidance on risk based capital and the ALLL is adequate.

Commenting on "Portfolio Stress Testing" p.12

The advisability of *portfolio* stress testing is already listed as a 'best practice" for CRE banks. The proposed guidelines give no more of a hint as to how this can be done with available information than do the existing guidelines.

In summary, our position is that the proposal is largely repetitive of *12 CFR 34* and existing Advisory letters on both Capital and ALLL methodologies which we think are still timely and effective in managing concentrations if applied correctly by both banks and regulators. This proposal would require an onerous change in management information systems and board reports which would be largely redundant. There is no single issue in the proposal that indicates that CRE risk would be better controlled.