March 2, 2018

The Honorable Mike Crapo
Chairman
Senate Banking, Housing, and Urban Affairs Committee
534 Dirksen Senate Office Building
Washington, DC 20510

The Honorable Sherrod Brown
Ranking Member
Senate Banking, Housing, and Urban Affairs Committee
534 Dirksen Senate Office Building
Washington, DC 20510

Subject: *Clarifying Commercial Real Estate Loans* – S. 2405

Dear Chairman Crapo and Ranking Member Brown:

The undersigned organizations are pleased to support your efforts to enact measures that will promote economic growth while maintaining a sound financial framework.

One such measure is the bipartisan *Clarifying Commercial Real Estate Loans* (S. 2405) co-sponsored by Senators Tom Cotton (R-AR) and Doug Jones (D-AL), which would reform the Basel III High Volatility Commercial Real Estate (HVCRE) Rule. Specifically, S. 2405 would amend the Federal Deposit Insurance Act to clarify specific requirements for acquisition, development, or construction (ADC) loans. An identical measure had nearly unanimous bipartisan support in the House Financial Services Committee and passed the U.S. House of Representatives by voice vote in November last year. We encourage the Senate Banking Committee to take the necessary steps to enact a similar measure.

The HVCRE Rule requires banks to hold higher capital levels against certain ADC loans. The problem with the current rule is that it is both unclear and overly broad. As a result, many stabilized loans without construction risk fall into the HVCRE category, unduly burdening stabilized loans with a higher capital charge designed to protect banks from heightened construction risks. This has deterred many banks, including small community financial institutions, from making this type of loan – which can represent up to 50 percent of some small bank loan portfolios.

A legislative measure like S. 2405 is necessary because banking regulators have not adequately addressed the issues with the HVCRE Rule. For example, several months after the Rule's effective date of January 1, 2015, the banking agencies issued 17 FAQs that did not adequately clarify key elements of the Rule, and they have not provided additional guidance in the ensuring three years despite ongoing requests.

More recently, the banking regulators proposed to replace the HVCRE Rule for standardized approach banks with a High Volatility Acquisition, Development or Construction (HVADC) Rule.[1] The HVADC Rule would be similar to the HVCRE Rule but would be less effective in tying capital to ADC lending risk and would remove incentives for banks to mitigate the risks of ADC lending. The proposal also would leave the current HVCRE Rule, with all its weaknesses, in place for advanced approach banks. In sum, it would not address the fundamental problems with the HVCRE Rule.

In contrast, S. 2405 would address key deficiencies in the agencies' regulations governing what is an HVCRE loan to ensure that they do not impede credit capacity or economic activity, while still promoting economically responsible commercial real estate lending. As such, the legislation would not eliminate the agencies' ability to require banks to hold higher capital for HVCRE loans. Rather, the bill would provide the transparency that the banking agencies have yet to provide, including clarifying which types of loans should and should not be classified as HVCRE loans.

[1] Notice of Proposed Rulemaking, Basel III High Volatility Acquisition Development or Construction (HVADC), "Simplifications to the Capital Rule Pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996," 82 Fed. Reg. 49984 (Oct. 27, 2017).

The capital treatment of bank lending matters because, of the $3.9 trillion in commercial real estate debt outstanding, commercial banks constitute our nation's largest source of commercial real estate financing. Moreover, this is not just a problem for commercial real estate owners and bank lenders; it is a problem for the broader economy. ADC lending is a critical component fueling the commercial and multifamily industry's production, and, in turn, the impact the commercial and multifamily real estate industry provides to the nation's GDP – employing millions of people and producing a significant amount of the taxes raised by local governments for essential public services. Regulations that can impair credit capacity for this important sector can have an adverse impact on jobs and tax revenue.

In sum, by carefully addressing the deficiencies of the current HVCRE rule, S. 2405 will help support job creation, economic growth and investment in the U.S. economy through a sensible financial regulatory framework that permits stable capital formation and balanced and disciplined lending.

The Banking Committee is to be commended for recognizing the important link between bank regulatory policy and economic growth and for taking concrete steps to enact measures that would foster job creation and economic activity.

In that same spirit, we encourage the Committee to move forward with *Clarifying Commercial Real Estate Loans* (S. 2405).

Thank you for the opportunity to comment on this important issue.

Sincerely,

American Land Title Association
Building Owners and Managers Association International
CCIM Institute
Institute of Real Estate Management
International Council of Shopping Centers
Mortgage Bankers Association
NAIOP, the Commercial Real Estate Development Association
National Association of Home Builders
National Association of Realtors®
Nareit®
National Apartment Association
National Multifamily Housing Council
The Real Estate Roundtable

cc: Members of the Senate Banking, Housing, and Urban Affairs Committee