November 7, 2017

Dear Representative:

On behalf of Americans for Financial Reform (AFR), we are writing to urge you to vote against H.R. 2148, which is being considered on the House floor today under suspension of the rules.[1] This legislation creates unjustified new statutory exemptions from bank capital requirements for risky commercial real estate loans.

Commercial real estate exposures played a significant role in the financial crisis, contributing to the failure of large banks like Lehman Brothers and also major losses for many small community banks. In fact, the Government Accounting Office has found a strong link between the failures of community banks during the financial crisis and their losses on commercial real estate loans.[2]

In response to this experience, both U.S. and international regulators created rules that require lending institutions making high risk commercial real estate loans to raise extra capital to absorb potential losses. This was a consensus measure passed by the Basel Committee in order to maintain adequate capitalization of financial institutions and more stable financial systems.

These regulations require banks to backstop High Volatility Commercial Real Estate (HVCRE) loans with more loss-absorbing capital than less risky loans. H.R. 2148 would relax those standards by creating a number of new exemptions to the capital standards for lenders making risky loans. The legislation significantly loosens the standard by which a commercial real estate project would be judged to be self-financing and therefore exempt from high-risk status and also creates other off-ramps and exemptions from high-risk status.

In response to criticism of excessive complexity in the current HVCRE regulation, the banking regulators have already proposed a new rule that aims at simplifies the HVCRE designation in multiple ways.[3] Additional Congressional intervention to loosen risk controls is not called for. Moreover, codifying lax capital standards into law would tie the hands of regulators to require higher capital reserves if it is needed in the future.

Proponents of H.R. 2148 mistakenly argue that burdensome capital rules related to HVCRE have slowed down lending in the commercial real estate market. However, a recent report from the Federal Reserve Bank of Richmond shows that commercial real estate lending by U.S. banks

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[1] Americans for Financial Reform is an unprecedented coalition of more than 200 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups. A list of coalition members is available at http://ourfinancialsecurity.org/about/our-coalition/.

[2] U.S. Government Accountability Office, "Causes and Consequences of Recent Community Bank Failures." Report to Congressional Committees, January 2013. Accessed November 6, 2017. Available at http://bit.ly/2ybRpAp.

[3] Federal Deposit Insurance Commission, "Simplifications to the Capital Rule Pursuant to EGRPPRA", FIL 45-2017, September 27, 2017. http://bit.ly/2yEFZc7

have surged in the past five years.[4] The report also suggest that the commercial real estate loan market may be overheated and regulators should carefully monitor excessive risk in this market. By loosening risk controls in commercial real estate, H.R. 2148 contradicts those findings and recommendations.

Relaxing risk controls in booming markets can lead to bank failures when inevitable downturns occur. This danger can be especially pronounced for small banks. The U.S. Government Accountability Office have found that the failures of small banks during the last financial crisis were largely driven by their losses on commercial real estate loans—in particular, by the same ADC loans targeted by the HVCRE rule.[5]

We urge you to reject this bill.

For more information please contact AFR's Policy Director, Marcus Stanley, at marcus@ourfinancialsecurity.org or 202-466-3672.

Sincerely,

Americans for Financial Reform

[4] Helen Fessenden and Catherine Muething, "Understanding the Surge in Commercial Real Estate Lending," Federal Reserve Bank of Richmond, *Economic Brief 17-08.* August 2017. Accessed November 6, 2017. Available at http://bit.ly/2xxClAE.

[5] U.S. Government Accountability Office, "Causes and Consequences of Recent Community Bank Failures." Report to Congressional Committees, January 2013. Accessed November 6, 2017. Available at http://bit.ly/2ybRpAp.