Response to questions from the Honorable Alan Grayson
by Martin J. Gruenberg, Vice Chairman,
Federal Deposit Insurance Corporation

Q1. How many new bank charters have you issued since January 1, 2009?

A1. While the Office of the Comptroller of the Currency, the Office of Thrift Supervision, and the various State Authorities hold the authority to grant bank or thrift charters, the FDIC is solely authorized to make determinations regarding deposit insurance. The table below presents the number of deposit insurance applications approved during 2006, 2007, 2008, and through March 31, 2009. The table also includes information regarding the number of approved applications that have consummated since approval; for ease of comparison, the number of applications consummated is attributed to the year the respective applications were approved rather than the year consummated.

	Deposit Insurance Applications			
	2006	2007	2008	3/31/2009
Approved	183	191	101	7
Consummated	183	186	79	2

Q2. What are you doing to make sure that developers who hold land loans and inventory and are current on all their interest charges are not forced to pay down principal before the properties are sold or developed?

A2. The FDIC understands the strain that builders and developers are under during this challenging environment, and we have encouraged banks to work with these borrowers given the sluggish demand for real estate at this time. Over the past year, we have issued guidance to FDIC-supervised institutions encouraging them to continue making loans available to creditworthy borrowers and to work with borrowers experiencing difficulty. The following directives issued to FDIC-supervised institutions are attached to this document:

FDIC Financial Institution Letter 128-08, *Interagency Statement on Meeting the Needs of Creditworthy Borrowers*
http://www.fdic.gov/news/news/financial/2008/fil08128.html

FDIC Financial Institution Letter 22-08, *Managing Commercial Real Estate Concentrations in a Challenging Environment*
http://www.fdic.gov/news/news/financial/2008/fil08022.html

Federal Deposit Insurance Corporation
550 17th Street NW, Washington, D.C. 20429-9990

Financial Institution Letter
FIL-128-2008
November 12, 2008

INTERAGENCY STATEMENT ON MEETING THE NEEDS OF CREDITWORTHY BORROWERS

Summary: The FDIC joined the other federal banking agencies in issuing the attached "Interagency Statement on Meeting the Needs of Creditworthy Borrowers" on November 12, 2008.

Distribution:
FDIC-Supervised Institutions

Suggested Routing:
Chief Executive Officer
Senior Credit Officer

Attachment:
"Interagency Statement on Meeting the Needs of Creditworthy Borrowers"

Contact:
Institution's contact person (Case Manager or Field Supervisor) at applicable FDIC Regional Office, or Associate Director Steven D. Fritts in Washington at 202-898-3723 and sfritts@fdic.gov

Note:
FDIC financial institution letters (FILs) may be accessed from the FDIC's Web site at www.fdic.gov/news/news/financial/2008/index.html.

To receive FILs electronically, please visit http://www.fdic.gov/about/subscriptions/fil.html.

Paper copies of FDIC financial institution letters may be obtained through the FDIC's Public Information Center, 3501 Fairfax Drive, E-1002, Arlington, VA 22226.

Highlights:

Several federal programs have recently been instituted to promote financial stability and mitigate the effects of current market conditions on insured depository institutions. These efforts are designed to improve the functioning of credit markets and strengthen capital in our financial system to improve banks' capacity to engage in prudent lending during these times of economic distress.

The agencies expect all banking organizations to fulfill their fundamental role in the economy as intermediaries of credit to businesses, consumers, and other creditworthy borrowers. Lending to creditworthy borrowers provides sustainable returns for the organization and is constructive for the economy as a whole.

The agencies urge all lenders and servicers to adopt systematic, proactive, and streamlined mortgage loan modification protocols and to review troubled loans using these protocols. Lenders and servicers should first determine whether a loan modification would enhance the net present value of the loan before proceeding to foreclosure, and they should ensure that loans currently in foreclosure have been subject to such analysis.

In implementing this Statement, the FDIC encourages institutions it supervises to:

- lend prudently and responsibly to creditworthy borrowers;
- work with borrowers to preserve homeownership and avoid preventable foreclosures;
- adjust dividend policies to preserve capital and lending capacity; and
- employ compensation structures that encourage prudent lending.

State nonmember institutions' adherence to these expectations will be reflected in examination ratings the FDIC assigns for purposes of assessing safety and soundness, their compliance with laws and regulations, and their performance in meeting the requirements of the Community Reinvestment Act (CRA).

Federal Deposit Insurance Corporation
550 17th Street NW, Washington, D.C. 20429-9990

Financial Institution Letter
FIL-22-2008
March 17, 2008

MANAGING COMMERCIAL REAL ESTATE CONCENTRATIONS IN A CHALLENGING ENVIRONMENT

Summary: The Federal Deposit Insurance Corporation (FDIC) is re-emphasizing the importance of strong capital and loan loss allowance levels, and robust credit risk-management practices for state nonmember institutions with significant commercial real estate (CRE) and construction and development (C&D) loan concentrations.

Distribution:
FDIC-Supervised Institutions (Commercial and Savings)

Suggested Routing:
Chief Executive Officer
Chief Lending Officer

Related Topics:
Guidance on Concentrations in CRE Lending
Interagency Statement on the ALLL

Attachment:
Appendix

Contact:
Sr. Examination Specialist William R. Baxter
wbaxter@fdic.gov, 202.898.8514

Note:
FDIC financial institution letters (FILs) may be accessed from the FDIC's Web site at www.fdic.gov/news/news/financial/2008/index.html.

To receive FILs electronically, please visit http://www.fdic.gov/about/subscriptions/fil.html.

Paper copies of FDIC financial institution letters may be obtained through the FDIC's Public Information Center, 3501 Fairfax Drive, E-1002, Arlington, VA 22226 (1-877-275-3342 or 703-562-2200).

Highlights:

- The FDIC is issuing this FIL to re-emphasize the importance of strong capital and loan loss allowance levels, and robust credit risk-management practices for institutions with concentrated CRE exposures, consistent with the December 6, 2006, interagency guidance on CRE lending and the December 13, 2006, interagency policy statement on the allowance for loan and lease losses (ALLL).
- Institutions with significant CRE concentrations should consult the 2006 CRE and ALLL guidance and should maintain or implement processes to:
  - Increase or maintain strong capital levels,
  - Ensure that loan loss allowances are appropriately strong ,
  - Manage C&D and CRE loan portfolios closely,
  - Maintain updated financial and analytical information, and
  - Bolster the loan workout infrastructure.
- Institutions are encouraged to continue making C&D and CRE credit available in their communities using prudent lending standards.

Financial Institution Letter
FIL-22-2008
March 17, 2008

Managing Commercial Real Estate Concentrations in a Challenging Environment

Recent weakness in the housing and the construction and development (C&D) markets have increased the FDIC's overall concern for state nonmember institutions with concentrations in commercial real estate (CRE) loans, and in particular, C&D loans. The purpose of this Financial Institution Letter is to re-emphasize the importance of strong capital and loan loss allowance levels, robust credit risk-management practices, and to recommend several key risk-management processes to help institutions manage CRE loan concentrations in this challenging environment.

On December 6, 2006, the FDIC joined the Federal Reserve Board and the Office of the Comptroller of the Currency (the agencies) in issuing final guidance on CRE entitled *Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices* (CRE Guidance). It was intended to help ensure that institutions pursuing a significant commercial real estate lending strategy remain healthy and profitable while continuing to serve the credit needs of the community. The CRE Guidance provided a framework for assessing CRE concentrations; risk management, including board and management oversight, portfolio management, management information systems, market analysis and stress testing, underwriting and credit risk review; and supervisory oversight, including CRE concentration management and an assessment of capital adequacy. The CRE Guidance was issued at a time when there was abundant liquidity in the credit markets, a strong global economy, and a number of what became known as "hot real estate markets" in major metropolitan areas. These factors led to a significant increase in CRE lending, especially in the C&D sector. The favorable market conditions led to relatively low borrowing costs, an overall boom in construction and sales activity, particularly in the residential and condominium sectors, and many institutions chose to relax loan terms and covenants to compete in the CRE mortgage market.

In addition, on December 13, 2006, the agencies and the Office of Thrift Supervision issued an *Interagency Policy Statement on the Allowance for Loan and Lease Losses* (ALLL Policy Statement) to revise and replace a 1993 policy statement on this subject. The ALLL Policy Statement reiterates key concepts and requirements pertaining to the allowance for loan and lease losses (ALLL) included in generally accepted accounting principles (GAAP) and existing supervisory guidance. It describes the nature and purpose of the ALLL; the responsibilities of boards of directors, management, and examiners; factors to be considered in the estimation of the ALLL; and the objectives and elements of an effective loan review system, including a sound credit grading system. The ALLL Policy Statement notes that determining the appropriate level for the ALLL is inevitably imprecise and requires a high degree of management judgment. An institution's process for determining the ALLL should be based on a comprehensive, well-documented, and consistently applied analysis of its loan portfolio that considers all significant factors that affect collectibility. That analysis should include an assessment of changes in economic conditions and collateral values and their direct impact on credit quality. If declining credit quality trends relevant to the types of loans in an institution's portfolio are evident, the ALLL level as a percentage of the portfolio should generally increase, barring unusual charge-off activity.

Since the CRE Guidance and ALLL Policy Statement were issued, market conditions have weakened, most notably in the C&D sector. The housing market is experiencing a slowdown, credit market liquidity has deteriorated, lending terms have tightened, and certain residential markets in the United States are overbuilt. While the vast majority of FDIC-insured institutions are well-capitalized, some institutions have significant CRE concentrations in areas with surplus housing units amid declining home prices. In addition, examiners have noted a few instances of potential underwriting weakness whereby institutions are inappropriately adding extra interest reserves on loans where the underlying real estate project is not performing as expected. This practice can erode collateral protection and mask loans that would otherwise be reported as delinquent.

The FDIC is increasingly concerned that institutions with concentrated CRE exposures may be vulnerable to a sustained downturn in real estate and should ensure that capital and ALLL levels are strong, and that credit risk management and workout processes are robust. It is strongly recommended that, as market conditions warrant, institutions with CRE concentrations (particularly in C&D lending) should increase capital to provide ample protection from unexpected losses if market conditions deteriorate further.

Recommendations for Managing CRE Concentrations

Institutions with significant CRE concentrations are reminded that strong capital and ALLL levels are needed, and that overall credit risk-management processes should reflect the principles of the 2006 CRE Guidance. Institutions with significant CRE concentrations are described in the CRE Guidance as those institutions reporting loans for construction, land development, and other land representing 100 percent or more of Total Capital; or institutions reporting total CRE loans representing 300 percent or more of Total Capital where the outstanding balance of CRE has increased by 50 percent or more during the prior 36 months.[1]

The FDIC suggests five key risk management processes to help institutions with significant C&D and CRE concentrations manage through changes in market conditions:

1. **Increase or Maintain Strong Capital Levels** – Capital provides institutions with protection against unexpected losses, particularly in stressed markets. Institutions with significant C&D and CRE exposures may require more capital because of uncertainty about market conditions, causing an elevated risk of unexpected losses. As market conditions warrant, directorates and management should take steps to increase capital levels to support significant CRE concentrations. Capital protection for C&D and CRE concentrations should be a strategic priority when contemplating the declaration of cash dividends.

2. **Ensure that Loan Loss Allowances are Appropriately Strong** – Institutions are expected to determine their ALLL in accordance with GAAP, their stated policies and procedures, management's best judgment, and relevant supervisory guidance. At least quarterly, institutions should analyze the collectibility of CRE and all other exposures and maintain an ALLL at a level that is appropriate to cover estimated credit losses on individually evaluated loans that are determined to be impaired as well as estimated credit losses in

[1] For the purposes of this FIL, C&D and CRE concentrations have the same meaning as stated in the CRE Guidance.

the remainder of the loan portfolio. In reviewing their ALLL methodology, institutions with significant C&D and CRE concentrations should consult recent supervisory guidance.[2]

3. **Manage C&D and CRE Loan Portfolios Closely** – Institutions should maintain prudent, time-tested lending policies and understand C&D and CRE concentrations. Management information systems should provide the board and management with effective data resources on concentrations levels and market conditions. A strong credit review and risk rating system that identifies deteriorating credit trends early should be enhanced or implemented. Institutions should also effectively manage interest reserve and loan extension accommodations, reflecting the borrower's condition accurately in loan ratings and documented reviews.

4. **Maintain Updated Financial and Analytical Information** – Institutions with CRE concentrations should maintain recent borrower financial statements, including property cash flow statements, rent rolls, guarantor personal statements, tax return data, global builder and other income property performance information. Global financial analysis of obligors should be emphasized, as well as the concentration of individual builders or developers in a loan portfolio. As real estate market conditions change, management should consider the continued relevance of appraisals performed during high growth periods, and update appraisal reports as necessary.[3]

5. **Bolster the Loan Workout Infrastructure** – Institutions should ensure they have sufficient staff and appropriate skill sets to properly manage an increase in problem loans and workouts. Management should develop a ready network of legal, appraisal, real estate brokerage, and property management professionals to handle additional prospective workouts.

The FDIC believes that CRE can be a profitable business line for institutions; however, as with any asset exposure, significant concentrations can lead to losses and capital deficiencies in a stressed environment. The Corporation's examiners recognize the challenges facing institutions in the current CRE environment, and will expect each board of directors and management team to strive for strong capital and loan loss allowance levels, and implement robust credit risk-management practices. Institutions are encouraged to continue making C&D and CRE credit available in their communities using prudent, time-tested lending standards that rely on strong underwriting and loan administration practices.

Sandra L. Thompson
Director
Division of Supervision and Consumer Protection

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[2] Institutions should refer to the ALLL Policy Statement, and the July 6, 2001, *Policy Statement on Allowance for Loan and Lease Losses Methodologies and Documentation for Institutions and Savings Institutions.*
[3] All appraisals should be consistent with the FDIC's appraisal rules in Part 323 of the FDIC's Rules and Regulations, 12 CFR 323.

APPENDIX

The following guidance and information should be consulted for additional details about matters discussed in this Financial Institution Letter.

Supervision

- *Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices*, December 6, 2006, http://www.fdic.gov/news/news/press/2006/pr06114.html
- *Interagency Policy Statement on the Allowance for Loan and Lease Losses*, December 13, 2006, http://www.fdic.gov/news/news/press/2006/pr06115.html
- *Policy Statement on Allowance for Loan and Lease Losses Methodologies and Documentation for Institutions and Savings Institutions*, July 6, 2001, http://www.fdic.gov/news/news/financial/2001/fil0163.html