



FEDERAL RESERVE BANK of KANSAS CITY

January 13, 2016

INTERAGENCY STATEMENT ON PRUDENT RISK MANAGEMENT FOR COMMERCIAL REAL ESTATE LENDING

Attention: Chief Executive Officer of Each Tenth District Bank, and Holding Company

In Brief: The Federal Reserve, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (the agencies) have jointly issued a statement to remind financial institutions of existing regulatory guidance on prudent risk management practices for commercial real estate (CRE) lending activity through economic cycles.

Highlights: The agencies have observed substantial growth in many CRE asset and lending markets as well as increased competitive pressures. While CRE market conditions and asset quality indicators do not currently indicate weaknesses in the quality of CRE portfolios, relaxed underwriting standards, increased levels of underwriting policy exceptions, and insufficient concentration monitoring have raised concern about the effectiveness of risk management practices at certain institutions engaged in this lending activity.

The statement offers examples of effective risk management practices undertaken by financial institutions that remained successful during historically difficult economic cycles. Furthermore, a list of all existing regulations and guidance related to CRE lending is included. Financial institutions are specifically encouraged to review the December 2006 interagency guidance entitled “Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices,” issued as an attachment to Federal Reserve Supervision and Regulation Letter SR 07-1.

Financial institutions should review their policies and practices related to CRE lending and exercise prudent risk management practices, including maintaining capital levels commensurate with the level and nature of their CRE concentration risk. During 2016, the agencies will continue to pay special attention to potential risks associated with CRE lending. The agencies will focus on those financial institutions that have recently experienced, or whose lending strategy plans for, substantial growth in CRE lending activity, or that operate in markets or loan segments with increasing risk fundamentals. The agencies may ask financial institutions found to have inadequate risk management practices and capital strategies to develop a plan to identify, measure, monitor, and manage CRE concentrations, to reduce risk tolerances in their underwriting standards, or to raise additional capital to mitigate the risk associated with their CRE strategies or exposures.

Contact: Please direct any questions concerning the new guidance to your Federal Reserve Bank of Kansas City central point of contact at (800) 333-1010.

Internet Link: A copy of the Federal Reserve Supervision and Regulation Letter SR 15-17 is available on the Board’s public web site at: <http://www.federalreserve.gov/bankinforeg/srletters/sr1517.htm>