TEMPLATE LETTER TO BANKING REGULATORS ON BUILDER FINANCING CONCERNS

The Honorable John C. Dugan
Comptroller of the Currency
250 E Street, SW
Washington, DC 20219

The Honorable Benjamin S. Bernanke
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

The Honorable Sheila Bair
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Mr. John E. Bowman
Acting Director
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552

Dear Madam and Sirs:

Turmoil in the housing credit and broader financial markets has spilled over into financing for housing production. Home builders are experiencing a significant adverse shift in terms and availability on land acquisition, land development and home construction (AD&C) loans, and builders with outstanding loans are facing mounting challenges. This rapidly spreading freeze in home building credit is causing severe harm to the small businesses that comprise the majority of the home building industry, and to a growing number of local economies already suffering job and revenue loss.

Portfolio lenders – commercial banks and thrifts – remain the predominant source of residential AD&C financing, accounting for over 90 percent of originations. There are no alternative sources of housing production credit for most firms in the home building industry. Thus, smaller builders have borne the brunt of the credit retraction.

I am hearing from my constituents in the home building industry that banks and thrifts are increasingly refusing to extend new AD&C credit or to modify outstanding AD&C loans in order to provide builders more time to complete their projects and pay off these loans. Lenders often cite regulatory requirements or examiner pressure that banks shrink their AD&C loan portfolios as the reasons for their actions. On outstanding loans, examiners are requiring banks to obtain new appraisals on properties for fully performing loans, which can result in the banks having to downgrade those loans, turning them into troubled “non-performing performing loans.” As a result, an increasing number of builders are being required to put up additional equity or collateral due to reappraisal of collateral or revaluation of their loan. Since most home building companies are small businesses and do not have the capacity to meet significant equity calls, the results are often foreclosure on a loan that had been performing and, in some cases, forcing builders into insolvency.

In many instances, banks that have received TARP funds are letting projects fail rather than pursuing workouts with the original developer and builders. This questionable action, which imposes serious hardship on home builders, often putting them out of business, should not be condoned or subsidized by the federal government.

As the nation's chief federal financial institution regulators, you are charged with ensuring sound lending practices are followed by regulated financial institutions. While I support prudent financial regulatory oversight, it seems that lenders are making demands on existing loans that are unrelated to sensible regulatory requirements. It is not in anyone's interest – not lenders, not builders, not the economy as a whole – to force sound and viable borrowers into insolvency.

Generally, a lender would be better off working with the borrower to extend the loan, rather than shutting off credit. Rather than calling loans, banks would be acting in their own self interest by extending loans for borrowers who are not in default or who have projects that are worthy of completion. This would allow borrowers to adjust their finances or to find other funding sources until they are able to complete and sell their homes.

As the home building industry is a major contributor to the economic vibrancy of the nation and its communities, I urge you to put a halt to these shortsighted practices that are adversely affecting the financial condition of the banking industry, as well as having devastating impacts on home building companies. Financial institutions should be encouraged to fund viable new projects and to take steps to avoid foreclosure on AD&C loans by accommodating loan modifications and workouts.

Further, banks that have received TARP funds should be required to account for how these funds are being used in lending on new AD&C projects. These banks must demonstrate how the institution is working out the restructuring of existing loans and providing more flexible terms to facilitate continued funding and eventual repayment of performing AD&C loans.

These actions would provide relief for a major sector of the economy that has suffered because of the inability of banks to provide the necessary funding and flexibility that would otherwise keep loans performing as scheduled. While it is not clear if lender demands are the result of regulatory excess, I hope that you, the nation's top federal financial institution regulators, recognize the effect that overly conservative lending standards have on credit availability. Americans benefit from a strong and fair financial regulatory system that balances prudent lending standards with the need for credit availability.

Thank you for your attention to this urgent matter.

Sincerely,

Member of Congress