OPENING STATEMENT OF CHAIRMAN SPENCER BACHUS
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER CREDIT
"A REVIEW OF REGULATORY PROPOSALS ON BASEL
CAPITAL AND COMMERCIAL REAL ESTATE"
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Good morning. Today the Subcommittee on Financial Institutions and Consumer Credit holds its sixth hearing on Basel Reform since the 106th Congress. Today's hearing will focus on the current status, recent developments, and potential impact of proposals from the financial regulators on Basel capital reform and commercial real estate lending guidance.

The goal of Basel is to develop a more flexible and forward-looking capital adequacy framework that better reflects the risks facing banks and encourages them to make ongoing improvements to their risk assessment capabilities. Over the past seven years, United States federal banking regulators have been engaged in negotiations with their foreign counterparts about improving the standards that govern the capital that depository institutions must hold against their assets.

The Federal Reserve Board, as the U.S. central bank, has taken the lead on this issue for the U.S. banking regulators. I would like to thank Governor Susan Bies for her dedication and hard work on the Basel Accord. Governor Bies has created an open dialogue with Members of Congress and the financial services industry. She understands the concerns that members of this Committee have raised with past proposals and has worked diligently to address those issues. Under Governor Bies' leadership, the banking regulators have worked to build consensus, and I would like to commend all of them for their efforts to improve the Basel framework.

We must ensure throughout this process that we do not include a framework that is too complex or costly to be followed. There are a wide variety of views expressed in the testimony that we will receive today. On the one hand, the federal banking regulators will testify that they have developed a Basel II rule that is intended to produce risk-based capital requirements that are more risk-sensitive than the existing rules. On the other hand, industry witnesses will tell us that the current U.S. version of the Basel II rule is less risk-sensitive than the internationally negotiated Basel II Accord, and that the differences between the U.S. rule and the Accord creates serious competitive issues, both within and outside the United States. This suggests that more work needs to be done on the rule. I was pleased this month that the regulators met and approved the notice of proposed rulemaking (NPR) on Basel II that requested comment on whether the so-called core banks and opt-in banks should be able to use the standardized approach. Alternative compliance options are a feature of the original Accord, and banks outside of the U.S. are provided this option.

In addition to the issues arising from Basel II, our hearing today addresses a January 2006 interagency Guidance on Concentrations in

Commercial Real Estate (CRE) proposal by the banking regulators. The proposal seeks to address high and increasing concentrations of commercial real estate loans at some banks and savings associations. The agencies suggest recent examinations show that risk management practices and capital levels of some institutions are not keeping pace with their increasing CRE loan concentrations. In turn, the Guidance sets forth thresholds for assessing whether an institution has a CRE concentration and should employ heightened risk management practices. The Guidance urges those institutions with elevated concentration risk to establish risk management practices and capital levels commensurate with the risk.

Some institutions have expressed the concern, however, that the proposed Guidance is too much of a "one size fits all" formulation and is effectively a cap on commercial real estate lending. They instead urge that the regulators utilize the examination process that identifies lending weaknesses in particular institutions. They contend that the data does not support the proposition that real estate lending *per se* is more risky than commercial and industrial lending, for example. Further, there is concern that the proposed Guidance is unfairly burdensome for community banks that do not have opportunities to raise capital or diversify their portfolios like larger banks. It is my hope that by the end of this hearing we may all be working from the same set of underlying facts with respect to how the real estate market works. In turn, I would hope that this will help ensure better regulation that will protect the taxpayer while not arbitrarily discouraging sound lending.

In closing, I want to thank Chairman Oxley, Ranking Member Frank and all of the Members of this Committee for their interest in working to ensure the Basel Accord is adopted in proper form. I look forward to hearing from our witnesses today and I am now pleased to recognize the Ranking Member, Mr. Sanders, for an opening statement.