

sensitivity of portfolio segments with common risk characteristics to potential market conditions. The sophistication of stress testing practices and sensitivity analysis should be consistent with the complexity of the institution and risk characteristics of its CRE loan portfolio. For example, well-margined and seasoned performing loans on multifamily housing normally would require significantly less robust stress testing than most acquisition, development, and construction loans.

Portfolio stress testing and sensitivity analysis may not necessarily require the use of a sophisticated portfolio model. Depending on the risk characteristics of the CRE portfolio, stress testing may be as simple as analyzing the potential effect of stressed loss rates on the CRE portfolio, capital, and earnings. The analysis should focus on the more vulnerable segments of an institution's CRE portfolio, taking into consideration the prevailing market environment and the institution's business strategy.

Credit Risk Review Function

A strong credit risk review function is critical for an institution's self-assessment of emerging risks. An effective, accurate, and timely risk-rating system provides a foundation for the institution's credit risk review function to assess credit quality and, ultimately, to identify problem loans. Risk ratings should also be risk sensitive, objective, and appropriate for the types of CRE loans underwritten by the institution. Further, risk ratings should be regularly reviewed for appropriateness.

Supervisory Oversight

As part of its ongoing supervisory monitoring processes, OTS uses certain criteria to identify savings associations that may have CRE concentration risk. These include savings associations that:

- Are approaching their HOLA investment limits.
- Have experienced rapid growth in CRE lending.
- Have notable exposure to a specific type of or high-risk CRE.
- Were subject to supervisory concern over CRE lending during preceding examinations.
- Have experienced significant levels of delinquencies or charge-offs in their CRE portfolio.

A savings association that exhibits any of the risk elements described above may receive further supervisory analysis to ascertain whether its internal concentration risk assessment and resulting risk management practices are commensurate with of the level and nature of its CRE exposure.

OTS will use the above criteria as a preliminary step to identify savings associations that may have CRE concentration risk.⁶ Because regulatory reports capture a broad range of CRE loans with varying risk characteristics, the supervisory monitoring criteria are intended to serve as high-level indicators to identify savings associations potentially exposed to CRE concentration risk.

For some types of CRE exposures, concentration risk may be present well before the statutory limit is reached. The statutory investment limit of 400 percent of total capital for non-residential real estate should not be considered a "safe harbor" for savings associations with smaller commercial real estate exposures. OTS expects all savings associations that are actively engaged in CRE lending to assess their concentration risk and maintain adequate risk management policies and procedures to control such risks.

Evaluation of CRE Concentration Risk

The effectiveness of an institution's risk management practices will be a key component of the supervisory evaluation of its CRE concentration risk. Examiners will evaluate an institution's internal CRE analysis and engage in a dialogue with the institution's management to assess CRE exposure levels and risk management practices. Savings associations that have experienced recent, significant growth in CRE lending will receive closer supervisory review than those that have demonstrated a successful track record of managing the risks in CRE concentrations.

In evaluating the level of risk, OTS will consider the institution's own analysis of its CRE portfolio including the presence of mitigating factors, such as:

- Portfolio diversification across property types
- Geographic dispersion of CRE loans
- Portfolio performance
- Underwriting standards
- Level of pre-sold units or other types of take-out commitments on construction loans
- Portfolio liquidity (ability to sell or securitize exposures on the secondary market)

Assessment of Capital Adequacy

OTS's existing capital adequacy guidelines note that an institution

⁶ Savings associations are reminded that this guidance does not affect the existing statutory investment limitations as set forth in 12 CFR 560.30. The statutory investment limit for loans secured by nonresidential properties is 400 percent of total capital.

should hold capital commensurate with the level and nature of the risks to which it is exposed. Accordingly, savings associations with CRE concentration risks are reminded that their capital levels should be commensurate with the risk profile of their CRE portfolios that includes both credit and concentration risks. In assessing the adequacy of an institution's capital, OTS will consider the level and nature of inherent risk in the CRE portfolio as well as management expertise, historical performance, underwriting standards, risk management practices, and market conditions. Most savings associations currently meet this expectation and will not be expected to increase their capital levels. However, an institution with inadequate capital to serve as a buffer against unexpected losses from a CRE concentration should develop a plan for reducing its CRE concentrations or for maintaining capital appropriate for the level and nature of its CRE concentration risk.

This concludes the text of the Guidance entitled, Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices.

Dated: December 7, 2006.

By the Office of Thrift Supervision.

John M. Reich,
Director.

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DEPARTMENT OF VETERANS AFFAIRS

Health Services Research and Development Service Merit Review Board; Notice of Meeting

The Department of Veterans Affairs (VA) gives notice under Public Law 92-463, Federal Advisory Committee Act, that a meeting of the Health Services Research and Development Service Merit Review Board will be held March 6-8, 2007, at the Sir Francis Drake Hotel, 450 Powell Street, San Francisco, CA. Various subcommittees of the Board will meet during that period. Each subcommittee meeting of the Merit Review Board will be open to the public the first day for approximately one half-hour from 8 a.m. until 8:30 a.m. to cover administrative matters and to discuss the general status of the program. The remaining portion of each meeting will be closed. The closed portion of each meeting will involve discussion, examination, reference to, and oral review of the research proposals and critiques.

The purpose of the Board is to review research and development applications concerned with the measurement and evaluation of health care services, the testing of new methods of health care delivery and management, and nursing research. Applications are reviewed for scientific and technical merit. Recommendations regarding funding are prepared for the Chief Research and Development Officer.

On Wednesday, March 7, six subcommittees will convene from 8 a.m. to 5 p.m. Those subcommittees are Implementation and Management Research Science, Chronic Disease Management & Long Term Aging, General Health Services Research, Special Populations, Equity/Women's Health and the Nursing Research Initiative (NRI). On Thursday, March 8, five subcommittees will convene from 8 a.m. to 5 p.m. Those subcommittees are Implementation and Management Research Science (continuation),

Special Populations (continuation), General Health Services Research (continuation), Chronic Disease Management (continuation) and Equity/Women's Health review group (continuation).

After the subcommittees meet there will be a debriefing provided to members of Health Services Research & Development Service Scientific Merit Review Board. This debriefing, by teleconference, will be to discuss the outcomes of the review sessions and to ensure the integrity and consistency of the review process.

During the closed portions of the meetings on March 7–8, discussion and recommendations will include qualifications of the personnel conducting the studies (the disclosure of which would constitute a clearly unwarranted invasion of personal privacy), as well as research information (the premature disclosure of which would be likely to compromise

significantly the implementation of proposed agency action regarding such research projects). As provided by subsection 10(d) of Public Law 92–463, as amended by Public Law 94–409, closing portions of these meetings is in accordance with 5 U.S.C. 552b(c)(6) and (9)(B).

Those who plan to attend the open session should contact the Scientific Merit Review Program Manager (124R), Health Services Research and Development Service, Department of Veterans Affairs, 1722 Eye Street, NW., Washington, DC 20006 at least five days before the meeting. For further information, call (202) 254–0207.

By Direction of the Secretary.

Dated: December 7, 2006.

E. Philip Riggins,

Committee Management Officer.

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