NAR Issue Summaries

Commercial / Basel Capital Standards for Banks and Thrifts

NAR Committee:

Commercial Federal Policy Committee

What is the fundamental issue?

International, voluntary regulatory capital standards for banks are developed by the Basel Committee on Banking Supervision. The most recent round of updates, referred to as Basel III, has been in an implementation cycle since 2013.

In 2015 a new risk-based capital category was created – High Volatility Commercial Real Estate Exposures (HVCRE) for commercial acquisition, development, and construction (ADC) loans, raising their risk-rate from 100% to 150%. These changes made commercial loans less attractive to lenders, and the lack of clarity around the new standard created confusion, resulting in different applications of the requirements by different lenders. In 2018 Congress passed S.2155, a regulatory relief package which clarified the definitions and exemptions in the HVCRE rule. Taken as a whole, it clarified and modified the HVCRE rule to ensure it is properly tailored while still promoting economically responsible commercial lending.

The Basel Committee published a final set of rules, known as "Basel III Endgame," and in 2023 the U.S. Federal Reserve, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation released proposed changes to bank capital rules in the U.S. to bring them into accordance with Basel III. Some of the proposed changes include increasing the banks held to the highest capital standard (those with $100B or more in assets; currently they are applied only to banks with $700B or more in assets) and reducing the ability of banks to use their own models for calculating capital requirements for loans by requiring a standardized calculation. These proposed rules have been critiqued by many as being too harsh and having the potential to discourage lending, with banking industry groups, Members of Congress, and even members of the agencies (the FED, OCC, and FDIC) voicing concerns. An updated proposal is expected in 2024.

I am a real estate professional. What does this mean for my business?

The Basel III capital standards and the proposed rules to align with the "Endgame" rules will require banks to hold more capital. The changes could significantly reduce lending, push borrowers outside of the traditional banking system, curtail the flow of capital to real estate and harm the commercial and residential property market and property values. Policymakers and trade groups alike have criticized the U.S. proposed rule, and a new proposal is expected in 2024. Even if the final rule is an improvement, borrowers and banks alike should ultimately prepare for higher capital standard requirements.

NAR Policy:

While NAR supports the Basel Committee's objective to prevent another financial crisis, NAR is concerned that requiring banks to hold far more capital could further exacerbate credit challenges for real estate and broader credit capacity. Furthermore, NAR seeks to protect and enhance the flow of capital to commercial and residential real estate by making sure that the capital rules do not require excessive capital to be held by banks.

Opposition Arguments:

Proponents of Basel III argue that by requiring banks to hold more capital, they improve their ability to absorb shocks arising from financial and economic stress, and improve their risk managment. These proponents also believe that the heightened capital requirements strenghten banks' transparency and their disclosures.

Legislative/Regulatory Status/Outlook

The Federal Reserve, Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation issued proposed rules to align with Basel III Endgame in July 2023, and has been taking comments since. A new proposal is expected by the end of 2024.

Current Legislation/Regulation (bill number or regulation)

Basel III Final Rule

Basel III Endgame Proposed Rule (July 2023)

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