ZIONS BANCORPORATION

HARRIS H. SIMMONS
Chairman, President and Chief Executive Officer

November 3, 2003

Office of the Comptroller of the Currency
250 E Street, SW
Public Information Room, Mailstop 1-5
Washington, D. C. 20219
Attention: Docket No. 03-14
Fax: (202) 874-4448
Email: regs.comments@occ.treas.gov

Ms. Jennifer J. Johnson
Secretary, Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, D. C. 20551
Attention: Docket No. R-1154
Fax: (202) 452-3819 or (202) 452-3102
Email: regs.comments@federalreserve.gov

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, D. C. 20429
Attention: Comments
Fax: (202) 898-3838
Email: Comments@FDIC.gov

Re: Risk-Based Capital Guidelines; Implementation of New Basel Capital Accord

Ladies and Gentlemen:

Zions Bancorporation ("Zions") is pleased to submit its comments on the proposals relating to the New Basel Capital Accord (the "New Accord"). Zions is a $28 billion (assets) regional financial services company, with six bank subsidiaries and several non-bank subsidiaries operating over 400 offices in Arizona, California, Colorado, Idaho, Nevada, New Mexico, Utah and Washington.

While Zions fully supports the concept that capital should properly reflect economic risks, we are concerned about some of the specific approaches chosen, the costs entailed relative to the potential benefits, and the future implications for the banking industry. Specifically, we believe that the New Accord will have adverse effects in terms of creating biases that favor large banks, deleterious industry concentration trends, and decreased safety and soundness.

Our detailed comments are as follows:

Competitive Effects: There are two forms of potentially anti-competitive implications for midsize and smaller banks. First, the capital requirements could become an additional anti-competitive factor relative to non-bank competitors that are not subject to these regulations. Examples would include finance companies and credit unions. Second, there could be adverse effects on the structure of the banking industry itself. If it is true that only the largest banks can realistically avail themselves of the technology and expertise required to implement the Advanced Internal Ratings Based (A-IRB) approach and Advanced Measurement Approach (AMA), then only these larger banks will have access to potentially lower capital requirements. Over time, this could harm the competitiveness of smaller and mid-sized banks and stimulate further aggressive consolidations into larger banks.

We cite the following QIS3 statistics about how the A-IRB methods changed capital requirements compared to current rules for 20 large U.S. banks:

Corporate Loans	26% reduction
Small- to Medium-sized Enterprise Loans	39% reduction
Residential Mortgages	56% reduction
Credit Card Receivables	16% increase
Other Consumer Loans	25% reduction

In general, these results suggest that A-IRB banks would have significant competitive advantages over other banks in that their loan officers would be able to allocate significantly less capital to most categories of loans. Such lower capital allocations translate into lower rates to potential borrowers, and hence, clear competitive advantages. Over time, such advantages would lead to declining market share for community and regional banks and would increase the rate of mergers with larger banks.

Safety and Soundness Implications: Some senior regulatory officials have stated that smaller banks are not as concerned about capital management as larger banks. They cite as evidence the fact that regional and community banks already maintain higher capital ratios. We disagree with this view. Among the reasons that smaller banks hold more capital are: (a) they are often encouraged to do so by examiners, and (b) some rating agencies require smaller banks to hold more capital to achieve a comparable debt rating to larger banks, all else being equal. Hence, *de facto* capital penalties already exist for smaller banks. The New Accord proposal would exacerbate this economic penalty for the reasons cited above.

The stock market would, in turn, reinforce this adverse effect. Under the Capital Assets Pricing Model, there are two main drivers of stock valuations: expected return on equity and expected growth rate. Requiring smaller banks to hold more capital than larger banks for the same assets will lower both ROE and growth rate. This will lower stock valuations for these institutions and drive them to consider selling their franchises to larger banks.

Such a trend would lead to accelerated concentration of the banking industry. More assets will be owned by fewer and fewer banking companies. This violates one of the fundamental tenets of risk management: diversification. The consolidation of the banking industry in the U.S. over the past two two decades has resulted in the creation of mammoth institutions that are generally more diversified by geography and product line than was previously the case. It might be true that the risk of any one of these very large banks failing has been reduced; at the same time, regulators have acknowledged that the consequence and cost of a large bank failure has been dramatically increased. We believe the implementation of the New Accord will result in accelerating the further consolidation of the industry into fewer, larger banks – banks that are already *de facto* too big to fail. In the end, the federal government and the taxpayers are forced to cover any adverse risk consequences, whereas today, that portion of risk is diversified and non-systemic. We believe that such biases in capital rules would be at odds with the notion of improving bank safety and soundness.

International Parity: It is widely recognized that the United States has the strongest regulatory supervisory system in the world. Even Comptroller Hawke has publicly acknowledged that Basel II will be more intensely enforced in the U.S. than anywhere else in the world, thereby putting U.S. banks at a disadvantage. We urge U.S. regulatory agencies to make all efforts in working with foreign counterparts to insure parity of treatment in all substantive matters.

Effect on the Economy: The current proposals would have an adverse effect on the economy in that it will exacerbate cyclical downturns by requiring banks to charge more for credit risk just when the economy weakens. This effect is known as "pro-cyclicality". Zions suggests that any new capital proposals should guard against such effects. To do so requires that any new capital standards reflect the entire economic cycle, rather than focus on or weight analyses based on portions of business cycles.

Cost to Implement: The cost of implementing the advanced approaches (A-IRB and AMA) can be staggering. Zions will spend over ten million dollars over the next several years, in large part to develop the data needed for economic capital analyses related to Basel II. The banking industry may well spend billions of dollars in aggregate for a very structured framework that may actually turn out to be less effective than either current, simpler approaches to economic profitability or more sophisticated approaches to value-at-risk. The New Accord will literally force most banking companies to abandon their current procedures in deference to the detailed prescriptions of Basel II. This will represent an unprecedented coercion of risk management practices for the entire banking

industry and will impede further development of new risk management practices that do not fit the strictures of the New Accord. Again, this can be construed as contrary to banking safety and soundness.

Simpler Approaches: The New Accord proposals mandate that only the most complicated and costly approaches to risk assessment are undertaken. However, Zions management believes that there are legitimate, simpler analyses that can yield important quantitative insights into relative risk levels among banks. One example would be measurement of earnings volatilities over economic cycles. Such volatilities can be dissected into the portions attributable to credit risk, interest rate risk, and operating risk simply by analyzing the volatilities of net charge-offs, net interest income, and net non-interest expense, respectively. While we do not claim that such measures are superior to the proposed framework, we believe that such simple approaches may serve as a stepping stone to more complicated approaches. They offer the advantage of being intuitively understandable and easily implemented by small and mid-sized banks just as effectively as by large banks. Indeed, it may be advantageous to allow smaller institutions to rely entirely on such simpler techniques.

Another simple alternative would be to allow all banks to adopt capital standards that are a blend of current standards and the A-IRB standards as determined from a representative sampling of large banks. In this way, all banks could avail themselves of at least a portion of the benefits of A-IRB, as well as maintaining an incentive to work toward full A-IRB implementation.

Commercial Real Estate Treatment: We reviewed with great interest the White Paper entitled "Loss Characteristics of Commercial Real Estate Loan Portfolios" dated June 2003. That analysis suggests that the late 80s and early 90s were an outlier period regarding commercial real estate losses. As such, we believe that no special treatment of commercial real estate loans is warranted. Indeed, Zions suggests that under A-IRB, no special weightings or factors should be applied to any type of loan. A-IRB should reflect the risk dynamics from the data. To insure that no biases exist in the data analyzed, it is fair to require that a broad sample of external data gathered from full business cycles be used as a representative benchmark. The external data should be weighted no less than equally with internal data.

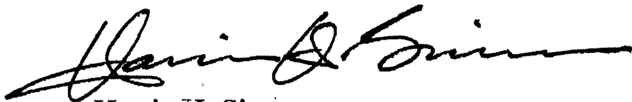
Operating Risk: Zions has grave concerns about the treatment of operating risk as a Pillar 1 category. There is no consensus about the analytical methods; nor is there availability of historical national or international data (such as rating agency data for credit risk). Finally, there are no recognized standards for translating operating risk components into capital standards. Such risk does not follow standard statistical distributions. It does not have conventional size correlations. In light of this situation, it only seems prudent to classify operating risk as a Pillar 2 category until the techniques and data are better developed. It would be perverse to have interest rate risk be treated as Pillar 2 and operating risk as Pillar 1 when the techniques for interest rate risk definition, analysis, monitoring, and hedging are far better established and practiced than anything related to operating risk.

Unexpected Loss Issue: We applaud the announcement by the BIS that the New Accord will be redirected to focus on unexpected losses, rather than both expected and unexpected losses. We understand that this will necessitate adjustments and simplifications relating to the treatment of Future Margin Income, partial charge-offs, and the treatment of the loan loss allowance in capital.

In closing, we emphasize our concern about the adverse effects of the New Accord on small and medium-sized banks, the costs required to implement the A-IRB and AMA methods, and the strain on banking safety and soundness.

We are grateful for this opportunity to express our concerns. If any of your staff wish to discuss any of the views expressed here in greater detail, I invite them to contact Doyle Arnold, our chief financial officer, at (801) 524-2210.

Sincerely,



Harris H. Simmons
Chairman and Chief Executive Officer