# *INDEPENDENCE BANK*

October 22, 2012

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W Washington, D.C. 20551
*regs.comments@federalreserve.gov*
Docket R-1430 and R-1442; RIN No. 7100-AD 87

Office of the Comptroller of the Currency
250 E Street, SW Mail Stop 2-3
Washington, DC 20219
*regs.comments@occ.treas.gov*
Docket ID OCC-2012-0008 and OCC-2012-0009; RIN 1557-AD46

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation,
550 17th Street, N.W.
Washington, D.C. 20429
*comments@fdic.gov*
RIN 3064-AD95 and RIN 3064-AD96

***Re: Exempt Community Banks from Basel III Capital Proposals***

Dear Sirs and Madam:

Independence Bank appreciates the opportunity to provide our comments on the Basel III proposals (the "Proposals") entitled:

Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, and Transition Provisions; Regulatory Capital Rules: Standardized Approach for Risk-weighted Assets; Market Discipline and Disclosure Requirements; and Regulatory Capital Rules: Advanced Approaches Risk-based Capital Rules; Market Risk Capital Rule.

As you know, these proposed rules were recently approved by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (collectively the "Banking Agencies").

***Independence Bank strongly believes that community banks should be EXEMPT from the Basel III Capital Proposals.***

As a consequence of the Financial Crisis of 2008, Basel III was originally intended to apply to large, internationally-active, and systemically important financial institutions. Clearly, it is important that these large financial institutions are closely monitored by the Banking Agencies to insure that they at all times



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maintain strong capital and liquidity ratios, so our economy does not experience a repeat of the Financial Crisis.

However, community banks operate on a much different, and much simpler, business model than the large institutions that Basel III was intended for. Community banks engage in traditional banking: gathering deposits from local individuals, business, and municipalities in our community; make loans to local small business and consumers in our community, and processing transactions for our local customers through the Federal Reserve payment system.

Moreover, most community banks do not engage in investment banking, derivatives trading, and other high-risk financial activities. Basel III will harm community banks in the following ways:

1. **Basel III is overly complex**. In general, community banks do not have the in-house expertise to meet the overwhelmingly complex Basel III proposed capital standards, resulting in an increased compliance burden and cost for community banks.

2. **Basel III requires excessive risk-weights**. Under Basel I, the highest risk-weight is 100%. This is appropriate for community banks, since we do not generally have exposure beyond our balance sheet. Basel III requires risk-weights of up to 200% form some assets, such as non-qualified mortgages, C&I, and CRE loans. These excessive risk-weights are greater than the loan amount.

3. **Basel III will reduce risk-based capital ratios**. By requiring punitive risk-weights in excess of 100% of the loan amount, Basel III, when calculated, will result in substantially lower risk-based capital ratios for community banks. At this time, it is extremely difficult for community banks to access the capital markets. It has been estimated that roughly 700 community banks could be undercapitalized if Basel III is applied to them.

4. **Basel III will reduce lending**. Community banks forced to shore up their capital as a result of Basel III will have no choice other than to deleverage their balance sheets. This will have the adverse, unintended consequence of reducing lending to homeowners and small business in the communities they serve, at precisely the time it is needed.

5. **Basel III will result in excessive capital volatility**. By requiring the gains and losses on Available for Sale ("AFS") investment securities to flow through the Accumulated Other Comprehensive Income ("AOCI") equity account, Basel III will cause undue and excessive capital volatility from the mark-to-market of these investment securities.

6. **Basel III will undercut ALLL methodology**. By limiting Allowance for Loan and Lease Losses ("ALLL") to 1.25% of risk-weighted assets, Basel III has the unintended consequence of reducing reserves against losses. All banks should be encouraged to build their reserves as an additional capital buffer, not to reduce them.

7. **Basel III will impair Mortgage Servicing Assets**. For those community banks that sell but continue to service their mortgage loans, Basel III will have a devastating impact on Mortgage Servicing Assets ("MSA"). Under Basel III, community banks will be required deduct a large portion of their MSA from the Tier 1 Capital calculation, further decreasing capital. This will have the unintended consequence of forcing community banks to reevaluate their "sell and service" loan model, and exit mortgage lending.

8. **Basel III will hurt SBA lenders**. Independence Bank, like many community banks, originates U.S. Small Business Administration ("SBA") loans to small business. SBA lending has been a key driver of employment growth, since small business is responsible for 2 out of every three new hires. SBA lenders also utilize the "sell and service" business model that mortgage lenders use. We are also required to book a Servicing Asset relating to guaranteed portions of the SBA loans we sell. Like mortgage lenders, SBA lenders will be required to take a substantial write-down of this Servicing Asset. SBA lenders will experience a dramatic reduction in capital if Basel III is applied to community banks.

For the reasons outlined above, it is imperative that community banks be granted an exemption from Basel III, and be allowed to continue with the Basel I standard risk-weight methodology that has been employed successfully for many years.

Thank you for the opportunity to comment on the Basel III Capital Proposals.

Very truly yours,
INDEPENDENCE BANK

By: Robert A. Catanzaro, Pres.
Robert A. Catanzaro, President



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