# Alpine Banks of Colorado

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September 27, 2012

Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street N.W.
Washington, DC 20429
**Delivered via email comments@FDIC.gov**

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, DC 20551
**Delivered via email regs.comments@federalreserve.gov**

Officer of the Comptroller of the Currency
250 E Street SE
Mail Stop 2-3
Washington, DC 20219
**Delivered via email regs.comments@occ.treas.gov**

Re: Basel III Capital Proposals
OCC: Docket ID OCC-2012-0008
OCC: Docket ID OCC-2012-0009
FRB: Docket No. R-1430; RIN No. 7100-AD87
FRB: Docket No. R-1442; RIN No. 7100-AD87
FDIC: RIN 3064-AD95
FDIC: RIN 3064-AD96

Ladies and Gentlemen:

Thank you for the opportunity to provide comment on the Basel III proposals[1] (Proposals) that 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").

[1] The proposals are titled: *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.*

The proposals as currently written will have a profoundly negative impact on our ability to serve our communities.

I am the Chief Financial Officer for Alpine Bank (Alpine). Alpine is an employee owned community bank headquartered in Glenwood Springs, Colorado. We operate in eleven counties in Western Colorado through thirty seven full service branch locations. Formed in Carbondale, CO forty years ago, we've grown to be the second largest bank serving our eleven county market area. We serve a wide range of communities in Western Colorado from high end resort towns to rural areas to smaller cities. As the second largest financial institution in our market, our ability to lend and the lending terms we are able to offer can have a major impact on the economic health of Western Colorado.

I would like to comment on a few of the major issues raised by the Basel III Capital Proposals and how they will impact our bank and communities.

Phase Out of Trust Preferred Securities

The Proposals call for a ten year phase out of Trust Preferred Securities (TRUPs) as Tier 1 capital. This is in direct conflict with the intent of Congress. The Collins Amendment of the Dodd-Frank Act grandfathered TRUPs as Tier 1 capital for banks under $15 million in total assets. I fail to see how removing a form of capital will add to the safety and soundness of the banking system.

In the past, some banks may have used funding from TRUPs to grow faster and larger than was prudent. However, new issues of TRUPs were banned by the Dodd-Frank Act. The misuse of new TRUPs financing is not a concern for the future. I would contend that removing TRUPs as Tier 1 capital actually adds risk to the system. Most smaller banks will have difficulty replacing TRUPs with new capital at a reasonable price. As a result, they will need to work within a smaller capital base. Growth and lending will be restricted and there will be pressure to increase earnings to augment capital levels. This could lead to risky behavior as banks reach for riskier but more profitable business lines.

In Alpine's case, TRUPs are a large part of the capital base for our holding company (Alpine Banks of Colorado). Both the bank and holding company are extremely well capitalized at this time. As a stand-alone issue, we can manage the phase out of TRUPs as Tier 1 capital without significant changes to our business plan. However, when combined with other aspects of the Proposals, Alpine will either need to raise additional Tier 1 capital at unreasonably high costs or restrict growth. We estimate on a conservative basis that over $600 million in loans will not be made in our communities due to the phase out of TRUPs.

In my opinion, continuing to grandfather existing TRUPs is the best decision. It is consistent with Congressional intent and does not add risk to the financial system.

Unrealized Gains and Losses Flowing Through Capital

The Proposals call for the inclusion of all Unrealized Gains and Losses on Available for Sale securities in Common Equity Tier 1 capital. This is a change from current regulations in which Unrealized Gains and Losses on AFS debt securities are not included in Tier 1 capital. This change appears to be risky and will likely lead to many unintended and unwanted consequences.

Particularly considering the low interest rate environment now, this proposal will add extreme volatility to regulatory capital calculations. Most banks are subject to very large unrealized losses in their AFS portfolio given 300 and 400 basis point rises in interest rates. A simple rise in rates could move banks into the Adequately and Undercapitalized categories even without any additional credit risk. It is likely that banks will shorten the duration of security portfolios, resulting in much less return. A shift to Held to Maturity is also likely, resulting in fewer liquidity options for banks. I am also concerned about the impact on the municipal financing market. Most muni financings are longer term. Banks will be much more reluctant to purchase these long term bonds if they are subject to large swings in unrealized gains and losses. The resulting impact on public entities' ability to finance operations could be severe.

The impacts of this proposal cannot be fully evaluated without knowing what FASB will eventually decide on the accounting treatment for investment securities. There has been talk over the last few years that FASB may eliminate the Held to Maturity category. If this were to occur, banks would have no "safe harbor" from the whims of interest rates and their impact on regulatory capital levels.

For Alpine, the proposed change is not an immediate concern. The majority of our security portfolio is Held to Maturity. We have been booking more securities as AFS for liquidity reasons, but this will likely stop if the proposal goes through as written.

I would suggest the treatment of Unrealized Gains and Losses on AFS securities remain unchanged from current regulations. Changes in values due to credit quality issues are adequately covered by existing regulations. Including changes in value due to interest rate fluctuations adds unnecessary volatility to regulatory capital calculations.

Risk Weighting of Assets

The Proposals outline much more stringent risk-weightings for mortgage loans, some commercial real estate loans and past due loans.

Mortgage loans are broken down into Category 1 and Category 2 loans. Risk weights for Category 2 loans are at least double that for Category 1. The risk weighting of Category 2 loans are much higher than current regulations require. Although more granular breakdown of risk weighting may be sensible, the proposed rules are very complicated and time consuming to implement. Currently, we at Alpine do not have access to this data without reviewing each and every file on our books. That has made it very difficult to model the impact of the proposed changes. In our particular case, we have not found mortgage lending to be a high risk area. Over the last few years we have seen relatively few losses in our mortgage portfolio. That would indicate in our case that the complicated new proposal is not necessary.

I also find it unusual that the Proposals have a complicated formula for determining the risk weighting of mortgage loans, while at the same time leaving risk weighting on owner occupied and non-owner occupied real estate at 100% (excluding HVCRE). Although I don't encourage more complicated regulations, it appears inconsistent to break down mortgage lending to a more granular level and leave commercial real estate unchanged.

For Alpine, the new risk weightings for mortgage lending will lead us to redesign many of our products to meet the Category 1 definitions. This may be to the detriment of our customers, as they enjoy many of the existing terms. As a result, pricing on any loan deemed Category 2 will increase substantially.

I believe the new category of High Volatility Commercial Real Estate (HVCRE) has some merit. It is definitely the area of lending where Alpine took the largest losses over the past years. There is a need for more clear definition of what HVCRE actually includes. Many people I've talked with think it includes potentially ALL commercial real estate. I believe it only includes a subset of loans that would be classified on lines 1.a.1 and 1.a.2 of Schedule RC-C of the Call Report. Regardless, I believe the definition is unnecessarily complicated to monitor. I would suggest basing the definition solely on Loan to Value. Additionally, a 150% risk weight on performing loans is too high; I suggest it be set at 125%.

The increased risk weightings on past due and non-accrual loans appear to be unnecessary and redundant. Rules for Allowance for Loan and Lease Losses (ALLL) already require banks to hold more capital in the form of ALLL for past due, impaired and non-accrual loans. Layering this additional capital burden on serves no purpose.

At Alpine, I've estimated the increase in our Risk Weighted Assets at 15% once the proposed changes are implemented in 2015. This will have a very dramatic impact on our regulatory capital ratios. It will lead us to curtail lending until our regulatory capital ratios rise to our desired levels.

My overall recommendation is to leave risk weighting unchanged from current regulation. It is best to deal with the capital issues by adjusting the required capital levels as is also in the Proposals.

<u>Summary</u>

We have spent many hours attempting to model the impact of the Proposals on our organization. It is difficult to accomplish this without quick and easy access to the detailed information we will need for the new risk weighting rules. Under the existing risk based capital rules, Alpine anticipates we can grow by seven percent annually. That equates to hundreds of millions in loans made in our communities. Under the terms of the Proposals, Alpine will need to cut growth back to three percent annually over the next ten years. In 2022, that equates to a loan portfolio which is smaller by $1 billion. When you factor in all the loans that will be originated in the interim and either paid down or paid off, well over $2 billion in loans will not be made in our communities. Add to that all the reduced lending by other community banks in our market, and the economic impact to Western Colorado could be devastating.

Many of the items addressed within the Proposals seem to make sense on a stand-alone basis. However, when the proposals are taken as a whole, they create a dramatic change in the "rules" of banking. Many organizations, Alpine included, will need to drastically alter their business plans and operations. Changes of this magnitude will be detrimental to communities, employees and shareholders of community banks.

I urge the banking agencies to take a second look at the Proposals and their impact on community banks and the communities we serve. One size does not fit all. We need a regulatory framework that is tailored to the characteristics, needs and requirements of community banks.

Thank you for the opportunity to comment on the Proposals.

Sincerely,

Eric A. Gardey
Chief Financial Officer
Alpine Bank and
Alpine Banks of Colorado

cc:

The Honorable Michael Bennet
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