PREMIER
VALLEY BANK

July 9, 2011

Department of the Treasury, Office of the Comptroller of the Currency
regs.comments@occ.treas.gov
Subject: Margin and Capital Requirements for Covered Swap Entities
Docket ID OCC-2011-0008 and RIN 1557-AS43

Board of Governors of the Federal Reserve System
regs.comments@federalreserve.gov
Subject: Margin and Capital Requirements for Covered Swap Entities
Docket No. R-1415 and RIN 7100 AD74

Federal Deposit Insurance Corporation
comments@fdic.gov
Subject: Margin and Capital Requirements for Covered Swap Entities
Docket No. RIN 3064-AD79

Farm Credit Administration
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Subject: Margin and Capital Requirements for Covered Swap Entities
Docket No. RIN 3052-AC69

Federal Housing Finance Agency
regcomments@fhfa.gov
Subject: Margin and Capital Requirements for Covered Swap Entities
Docket No. RIN 2590-AA-45

To Whom it May Concern:

Premier Valley Bank is a community Bank that lends to businesses and consumers in the communities of the Greater Fresno and Sierras in California.

Premier Valley Bank, using simple swaps, has loaned more than $45 million in fixed rate loans to local businesses that, without the ability to hedge our interest rate risk by swapping to floating rates, likely would not have been made.

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As a community Bank, Premier Valley utilizes one of the simplest forms of swaps; we know our counter party and have agreements in place whereby collateral is pledged in the case of default. In the case of Premier Valley Bank, we have been utilizing this tool since 2006 and have experienced no losses in the program. In addition to minimizing the Bank's risk, this form of lending also minimizes credit risk with our borrowers who are able to efficiently obtain fixed rate terms which allows for predictable cash flows related to the debt.

Premier Valley Bank agrees with the views expressed by Pacific Coast Bankers' Bank in its June 22, 2011 letter(attached) submitted to the Agencies regarding the margin and capital requirements for covered swap entities.

Sincerely,

Premier Valley Bank, Fresno, California

Encl: PCBB Letter of June 22, 2011

PACIFIC COAST BANKERS' BANCSHARES

June 22, 2011

Mr. John Walsh
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Mr. Alfred M. Pollard
General Counsel, Attention Comments
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Ms. Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
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Mr. Gary K. Van Meter
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Mr. Robert E. Feldman
Executive Secretary, Attention: Comments
Federal Deposit Insurance Corporation
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Mr. David A.Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Center
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Via Electronic Submission

RE: Docket No. R-1415 and RIN 7100; Margin and Capital Requirements for Covered Swap Entities

RIN 3038—AC97; Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants

Pacific Coast Bankers' Bancshares (PCBB) appreciates the opportunity to provide comments on: (1) Notice of Proposed Rulemaking[1] by the Office of the Comptroller of the Currency (OCC), Treasury (Treasury), Board of Governors of the Federal Reserve System (Board), Federal Deposit Insurance Corporation (FDIC), Farm Credit Administration (FCA), and the Federal Housing Finance Agency (FHFA) (collectively, the Agencies) pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA) governing margin requirement for covered swap entities; and (2) the Notice of Proposed Rulemaking[2] by the Commodity Futures Trading Commission (CFTC) governing margin requirements for uncleared swaps for swap dealers and major swap participants.

[1] Margin Requirements for Covered Swap Entities, 76 FR 27564 (May 11, 2011)

[2] Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 76 FR 23732 (April 28, 2011)

Background: Community Banks Are Critical to Small Businesses and Consumers

PCBB provides correspondent banking services to over 500 community banks and savings associations (together community banks) throughout the United States[3]. We offer a range of services to our community bank clients which help them address their risk management, liquidity and operational needs. In total, our community bank clients lend billions of dollars – largely to small businesses and consumers.

Community banks are also the key provider of financial services to small businesses and thereby serve a critical role in the economy. Indeed, the regulatory burdens that impact community banks directly affect the small businesses that they serve. Our comments are intended to provide the CFTC and the Agencies with a small financial institution's perspective in an effort to support final rules that protect the interests of all market participants.

The Application of Dodd-Frank's Margin Requirements to Community Banks Will Harm Small Businesses and Consumers – Margin Requirements for Small Financial Institutions and Nonfinancial End-User Should Be Similar

The Dodd-Frank Act (the DFA) mandates that margin requirements apply to all non-cleared swaps and security-based swaps into which a covered swap entity enters, regardless of the type of transaction, except where the counterparty is a commercial end user. The Agencies and the CFTC are seeking comments on the appropriate application of the margin requirements to small financial institutions (i.e., depository institutions with total assets of $10 billion or less). Specifically, the relevant notices of proposed rulemaking ask the following question:

> *Should counterparties that are small financial institutions using derivatives to hedge their risks be treated in the same manner as nonfinancial end users for purposes of the margin requirements?*[4]

We believe that the answer to this question is "Yes" - small financial institutions should be treated as nonfinancial end users for purposes of the margin requirements.

Small financial institutions primarily use swaps for two reasons. First, small financial institutions use swaps to mitigate risks that they face as a result of their ordinary lending activities. In short, much of this lending activity directly benefits "Main Street" small businesses without creating the systemic risks that the DFA margin requirements are intended to manage. The imposition of margin requirements on hedging and risk mitigation transactions entered into by small financial institutions could adversely affect

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[3] All of PCBB's clients would be considered a "small financial institution"; which is to say that these clients have total assets less than $10 billion and as defined under End-User Exception to Mandatory Clearing of Swaps, 75 FR 80747 (December 23, 2010).

[4] 76 FR at 27570; 76 FR at 23740.

the efficiency of such institutions, increase risk, reduce performance and, by extension, their ability to provide financing to small businesses.

Second, small financial institutions use swaps to accommodate customer requests for specific loan structures that are longer-term in nature. For example, a small financial institution may offer its customer a fixed rate loan coupled with an interest rate swap. For the small business, this structure lets the small business lock in a longer-term fixed rate, protecting it against rising future interest rates. For the bank, the interest rate swap transforms the loan into a floating rate instrument, aligning its funding and interest rate risk structure and thereby reducing the risk of rising interest rates. This allows the customer to hedge against a rise in the relevant market level interest rate (the Customer Swap). Small financial institutions typically allow nonfinancial end user customers to pledge noncash collateral (lien on real estate or personal property) to secure obligations owed to the small financial institution in connection with the Customer Swap. Currently, most small financial institutions enter into an offsetting swap in order to lay off the market risk faced by the small financial institution under the Customer Swap. Current industry standard collateral arrangements do not typically require small financial institutions to pledge security (i.e., initial margin) to other financial institutions, although daily mark-to-market gains/losses in excess of a certain level (*e.g.*, $100,000) may be pledged in respect of such offsetting swaps. All of these community banks are also regulated by a banking regulator, such as the FDIC, state banking departments, OCC or Federal Reserve.

If small financial institutions are required to post initial margin for uncleared swaps the cost and complexity of doing business for community banks will increase. This could lead them to take additional risk, remain mis-matched in funding and lending activities, or not offer small business clients loans due to an unbalanced interest rate structure. We believe that this greater cost and complexity will jeopardize community banks' effectiveness in providing banking services and in particular, prudently structure many types of loans to their small business and consumer clients. It will also leave them at a competitive disadvantage relative to larger financial institutions. Yet, despite such increased costs and complexity, the imposition of initial margin requirements on small financial institutions will do little if anything to further DFA's key policy objective: implement margin requirements to reduce systemic risk and could, in fact, exacerbate that issue.

Increased Systemic Risk in the Financial System If Margin Requirement for Small Financial Institutions Is Not Similar to Nonfinancial End-User

Small financial institutions will be particularly disadvantaged against their larger financial institution competitors. Unlike small financial institutions, larger financial institutions do not need to offset swaps with a nonfinancial end user because larger financial institutions have the ability to manage a matched book of offsetting swaps on their own balance sheet without the use of a clearing house, a futures exchange or entering into an offsetting swap with another swap dealer. Larger financial institutions will realize a cost advantage because of lower margin costs versus smaller financial institutions. This would most

likely result in fewer loans being made to small business and consumer clients by community banks, and/or increase the concentration of such loans in a small number of larger financial institutions – an outcome that could have the unintended consequence of increasing systemic risk in the financial system.

Conclusion

We urge the CFTC and the Agencies to treat small financial institutions using derivatives to hedge their risks in the same manner as nonfinancial end users for purposes of the margin requirements. If small financial institutions are required to pledge additional initial collateral to support their lending activities (i.e., if initial margin requirements are imposed on swaps entered into by small financial institutions), then small businesses and consumers that so heavily rely on community banks in their own locality will have fewer options for borrowing. These small financial institutions did nothing to create the credit crisis driven by the larger banks and we believe that these unintended consequences are directly counter to the objectives of the DFA.

By comparison, we believe that our recommendations serve to further the intent of DFA, and will help community banks uphold the safety and soundness of the financial system and increase small business job creation and overall economic activity.

We thank the CFTC and the Agencies for their willingness to consider our suggestions and views.

Yours Truly,

Steve Brown
President & Chief Executive Officer
Pacific Coast Bankers' Bancshares