Gorham
SAVINGS BANK

October 17, 2012

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

Dear Ms. Johnson:

I would like to bring to light a few important points about Basel III which will likely affect the future of Gorham Savings Bank, and community banks in general.

I believe strongly, and trust that you agree, that community banks have been a tremendous asset to the banking system. We have served important community needs for centuries with local knowledge that simply does not exist in large regional, national, or international banks. Gorham Savings Bank has 144 successful years of serving individuals, families and businesses in Southern Maine during many economic difficulties from post Civil War to the Great Depression. We have been conservative to the point of being a bright spot in the otherwise risky sub-prime lending practice that led to the recent housing crisis and recession. GSB has provided jobs in Maine communities at a time when bigger institutions have closed offices and moved these jobs out of state or overseas.

I fear that Basel III's efforts could dilute, if not dislodge, the community bank's place. At the least, it will restrict our ability to lend to our communities. At most, it could create an environment where we can no longer survive. This runs counter to our efforts to prevent "too big to fail" where the riskiest entities had the least amount to lose.

We know our markets and our borrowers. We apply our expertise carefully, based partly on banking skills reminiscent of an earlier day. This does not mean we record decisions on the back of napkins. Our audit results and regulatory examinations will show, we are a well run institution. But some of the restrictions proposed under Basel III could force us to merge, acquire, or be acquired, until community banking disappears. Mutual Banks in particular, do not have the tools to create capital as easily as stock banks or large banks, giving us even less room to accommodate requirements for additional capital. It is troubling to note that if requiring more capital is the solution, and for many this results in mergers/acquisitions, doesn't this fuel the "too big to fail" concern?

In banking, balance sheet risks are often mitigated by creating an equal and opposite transaction that would, when added together, reduce risk. There are a number of places in the Basel III proposal where there are new regulations impacting one side only. Here are two examples:

1. The requirement for banks to recognize changes in investment portfolio value in capital. Basel III writers need to understand that in a community bank, the Investment Portfolio is part of our asset/liability gap management, and we use it to hedge our loan and deposit portfolio interest rate risk. If we put on a long term deposit, we may buy a long term security. If we only pass value changes to capital on the investment side, and not the deposit side, then we are only

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2. The second example is demonstrated when Private Mortgage Insurance (PMI) is removed as a way to hedge mortgage losses, and thus reduce the capital required. Reducing risk is exactly what PMI is designed to do, and is the most often used method for Community Banks to manage mortgage risk. This regulation has the appearance of penalizing us because of the debacle in credit default swaps owned by insurance companies, and the feeling that insurance cannot be trusted. That is unfair and "asymmetric" to banks. It will require us to only lend to the very best borrowers, at the expense of an important part of the fabric of home ownership across a broad constituency in our small rural state.

While Basel III's motives make sense, and much of it is welcome in a world needing help to protect us from unsafe credit practices, we hope our regulatory bodies don't inadvertently push community banks out of the picture in the process. We have earned our place as prudent managers of risk, and healthy contributors to the economy, especially here in Maine.

Sincerely,

Chris Emmons

Christopher W. Emmons
President & CEO

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