Bank of American Fork
BIG CITY BANKING - SMALL TOWN SERVICE

October 19, 2012

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

Office of the Comptroller of the Currency
250 E Street, S.W.
Mail Stop 2-3
Washington, DC 20219

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, DC 20429

Re: Basel III Capital Proposals

Ladies and Gentlemen:

Thank you for the opportunity to provide comment on the Basel III Proposal ("the Proposal") that was recently issued for public comment by your respective agencies. While its motives may be noble, the Proposal is worthy of no praise.

If the Proposal is adopted, the Basel Committee on Banking Supervision ("BCBS") will have set the rules for bank capital, stress testing, and liquidity standards in the United States. If the Proposal is adopted, there will no longer be any need for you as U.S. banking regulators to have a role in setting standards in those areas. You will have abdicated U.S. sovereign power to a multinational committee without a treaty or other authority from Congress to do so. You will have neglected your duty to craft regulatory solutions specifically designed for the very unique nature of the U.S. banking system. By adopting Basel III, insofar as those areas are concerned, you will have rendered yourselves unnecessary. If the Proposal is adopted, then your budgets and staff should be reduced accordingly. You will have effectively said to the world that the U.S. banking system should be regulated the same as banks in Turkey, Luxemburg, Russia, and the other countries participating in BCBS. A single model, no matter how absurdly complex it is, cannot possibly account for the diversity of 27 countries' banking systems and in particular, community banks.

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It is clear that as the complexity of regulation increases, its effectiveness decreases. The Proposal is hyper complicated. It will require the addition of countless highly paid employees at banks in order to manage, and it will take resources that could have been used to enhance capital. It will stifle lending. It is not designed for small banks, community banks, or for industrial banks with unique business models. It is not designed for the U.S. banking system and should not be imposed on it.

The Proposal comes at the same time as two other great threats to the health of the U.S. banking system: (1) the massive new regulatory burdens imposed on banks by the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"); and (2) interest rates that have been held too low for too long by the Federal Reserve, putting unprecedented pressure on banks' margins, and coupled with out-of-control federal deficits which must eventually lead to high inflation.

Increasing the risk weights for residential balloon loans, interest-only loans, and second liens will penalize banks that offer these loan products to their customers and deprive customers of many financing options for residential property. Additionally, higher risk weights for balloon loans will further penalize banks for mitigating interest-rate risk in their asset-liability management. Banks will be forced to originate only 15- or 30-year mortgages with durations that will make their balance sheets more sensitive to changes in long-term interest rates. Many banks will either exit the residential loan market entirely or only originate those loans that can be sold to a GSE. Second liens will either become more expensive for borrowers or disappear altogether as banks will choose not to allocate additional capital to these balance-sheet exposures.

Higher down payment requirements in residential lending and fewer outside-the-box loans will clearly impact lower-income and protected classes to a greater degree than other groups. Have you considered the *disparate impact* that your Proposal will likely create? Will your agencies be referred to the Justice Department for investigation if that happens?

When the true costs to banks and to the economy of these two great threats and of Basel III are realized, the potential macroeconomic consequences are frightening. Dodd-Frank by itself is already stifling the economic recovery because banks are unsure about what constitutes safe mortgage lending under Dodd-Frank. Now with the Proposal's increased risk weights, the economic recovery will be stifled even further.

We applaud and agree with the thoughtful comments of the following respected individuals and groups, each of whom has voiced concerns with Basel III and suggested either major modifications to it or starting over altogether:

- The Conference of State Bank Supervisors
- FDIC Director Thomas Hoenig

- Andrew G Haldane, Executive Director, Financial Stability and member of the Financial Policy Committee and Vasileios Madouros, Economist, Bank of England
- Former FDIC Chairman William M. Isaac
- 53 U.S. senators: Kelly Ayotte (R-N.H.), John Barrasso (R-Wyo.), Max Baucus (D-Mont.), Michael Bennet (D-Colo.), Roy Blunt (R-Mo.), John Boozman (R-Ark.), Scott Brown (R-Mass.), Richard Burr (R-N.C.), Saxby Chambliss (R-Ga.), Dan Coats (R-Ind.), Tom Coburn (R-Okla.), Susan Collins (R-Maine), Kent Conrad (D-N.D.), John Cornyn (R-Texas), Mike Crapo (R-Idaho), Mike Enzi (R-Wyo.), Lindsey Graham (R-S.C.), Chuck Grassley (R-Iowa), Kay Hagan (D-N.C.), Orrin Hatch (R-Utah), John Hoeven (R-N.D.), Kay Bailey Hutchison (R-Texas), James Inhofe (R. Okla.), Johnny Isakson (R-Ga.), Mike Johanns (R-Neb.), Ron Johnson (R-Wis.), John Kerry (D-Mass.), Amy Klobuchar (D-Minn.), Herb Kohl (D-Wis.), Jon Kyl (R-Ariz.), Mary Landrieu (D-La.), Mike Lee (R-Utah), Joe Manchin (D-W.V.), Mitch McConnell (R-Ky.), Bob Menendez (D-N.J.), Jerry Moran (R-Kan.), Lisa Murkowski (R-Alaska), Ben Nelson (D-Neb.), Bill Nelson (D-Fla.), Rob Portman (R-Ohio), Mark Pryor (D-Ark.), James Risch (R-Idaho), Pat Roberts (R-Kan.), Marco Rubio (R-Fla.), Jeanne Shaheen (D-N.H.), Olympia Snowe (R-Maine), Debbie Stabenow (D-Mich.), Jon Tester (R-Mont.), John Thune (R-S.D.), Pat Toomey (R-Pa.), Mark Warner (D-Va.), Roger Wicker (R-Miss.), and Ron Wyden (D-Ore.).
- Spencer Bachus, Chairman, U.S. House Committee on Financial Services
- Jeb Hensarling, Vice Chairman, U.S. House Committee on Financial Services
- Shelley Moore Capito, Chairman, U.S. House Subcommittee on Financial Institutions and Consumer Credit
- Randy Neugebauer, Chairman, U.S. House Subcommittee on Oversight and Investigations
- 15 members of the Pennsylvania delegation to the U.S. Congress
- Numerous state and national banking associations
- Numerous banks

Community banks should not be held to the same capital standards as the largest banks in the country. Community banks did not engage in the highly leveraged activities that severely depleted the capital levels of the largest banks and created panic in the financial markets. Community banks operate on a relationship-based business model that is specifically designed to serve their customers on a long-term basis. This model contributes to the success of community banks all over the United States through practical, common-sense approaches to managing risk. The largest banks operate purely on transaction volume and pay little attention to the customer relationship. This difference in banking models demonstrates the need to place tougher capital standards exclusively on the largest banks to better manage the ability to absorb losses. These obvious disparities in the Proposal will inevitably favor the largest banks. This will exacerbate the problem of "too big to fail."

Inclusion of accumulated other comprehensive income ("AOCI") in capital for banks will result in increased volatility in regulatory capital balances and could rapidly deplete capital levels under certain economic conditions. AOCI commonly represents unrealized gains and losses on investment securities held available-for-sale.

In the case of our bank, the intent of holding investment securities as available-for-sale is to allow us flexibility to manage the changes in loan and deposit balances on our balance sheet by selling these available-for-sale securities as needed. Our bank has historically purchased investment securities held-for-sale in maturities based on a laddered approach and asset-liability interest-rate-risk planning, resulting in rational yields. If the AOCI is included in the capital calculation, I believe our bank will be forced to purchase investment securities with shorter-term maturities and thereby reduce our yields.

Because these securities are held at fair value, any gains or losses due to changes in interest rates are captured in the valuation. Recently, both short-term and long-term interest rates have fallen to historic lows, generating unprecedented unrealized gains for most investment securities. Additionally, demand for many implicitly and explicitly government-guaranteed securities has risen due to a flight to safety and government intervention in the capital markets. This increased demand has caused credit spreads to tighten, further increasing bond valuations. Interest rates have fallen to levels that are unsustainable long-term once an economic recovery accelerates. As interest rates rise fair values will fall, causing the balance of AOCI to decline and become negative. This decline will have a direct, immediate impact on common equity, tier 1, and total capital as the unrealized losses will reduce capital.

Additionally, penalizing the existing mortgage-servicing assets under the Proposal is unreasonable for those banks that have large portfolios of mortgage-servicing rights. Any mortgage-servicing rights existing on bank balance sheets should be allowed to continue to follow the current risk-weight and deduction methodologies.

For these reasons I would argue for the complete rejection of the Proposal in favor of a radically simpler solution that is tailored to the needs of U.S. banks. Let's find a simpler, American solution. Call it "America I" instead of "Basel III."

Sincerely,

Richard T. Beard
President & CEO