October 15, 2012

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

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

Re: Basel III Capital Proposals

Ladies and Gentlemen:

Thank you for the opportunity to provide comments on the Basel III proposals that were issued for public comment by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation.

As CFO of our $545 million community bank in Kentucky, I have followed the numerous comments made by bankers, banking lobby groups and now Congressmen on the new Basel III proposals. Months prior, in a board meeting, a member who is a doctor asked me if the new Basel III proposals would impact our bank and holding company. Instead of saying "I don't know", I made the assumption that the proposal should only impact the largest of banks, as the Basel group is only concerned about international banking and not community banking. Boy was I wrong and after doing considerable reading on the topic, I had to admit how wrong I was at the next board meeting.

Are the current capital standards adequate for banks? I would say not, so I see the worthiness of attempting to re-work them. The main issue for me is if "one size fits all" in capital standards. I would say definitely not. The largest banks, those $50 billion and up, operate in a totally different world of banking than a bank 1/100ths their size and likely needs a more sophisticated set of rules. I have run the Basel III models on our bank and holding company and outside of including the AOCI as a part of regulatory capital; we could handle the new rules just fine. But don't like all the complexity and expense it will cause us as I don't see the benefit to our customers. Surely a less complex system to measure capital needs for non-agency bonds and residential loans could be applied for community banks and the AOCI inclusion is setting up for another banking "crisis" when rates rise down the road.

Our bank could adapt to the new rules because we already have a strong "capital" mentality, but the new rules will hamper us from taking on as many new loan opportunities created when other banks in our market have to slow or stop lending in order to comply with the new rules. A stress test conducted by Trepp LLC claims that nearly 13% (784 of 6151 tested banks) would fail the new rules under their existing dividend policy and 615 of them would fail even if all dividends were stopped. This is pretty alarming as the test was done under current low interest rates, so a much greater number could fail under a rates-up scenario. If 615 plus smaller banks fail and have to be sold, who will buy them? Will the TBIF banks and larger regional banks continue to absorb these smaller banks? Will the other community banks be in the position to take in some under the new rules?

The Trepp study indicated that $26.7 billion in additional capital in aggregate would be needed to raise the 784 banks that "failed" to minimum thresholds under the new rules. In the lending world, that used to be $267 billion in loans, but under the proposals, it would be closer to $300 billion in loans that these banks would have to shrink by to avoid raising capital, which is increasing difficult to do today.

I can see why a bi-partisan group of 53 Senators has come out against applying the new rules to community banks. The rules appear to be a job-killing proposal at a time when the "recovery" is still very weak.

It seems to me that the easy solution is to exempt all banks under a threshold of $10 to $50 billion in total assets, then come back later with a new improved set of standards for the smaller banks. That way the largest banks, including the few TBIF banks, would have to play by the global standards while smaller domestic banks can continue to operate under existing capital rules until a less complex new set of standards can be developed for community banks.

I appreciate you extending the comment period.

Sincerely,

John H. Durbin, CFO

Paducah Bank & Trust Company,

Paducah, KY