NORTH DAKOTA
BANKERS
ASSOCIATION

October 15, 2012

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

RE: Basel III FDIC RIN 3064-AD95, RIN 3064-AD96, and RIN 3064-D97

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

RE: Basel III Docket No. 1442

Office of the Comptroller of the Currency
250 E Street SW
Mail Stop 2-3
Washington, DC 20219
regs.comments@occ.treas.gov

RE: Basel III OCC Docket ID OCC-2012-0008, 0009, and 0010

Ladies and Gentlemen:

The North Dakota Bankers Association ("NDBA") appreciates this opportunity to comment upon the referenced capital proposals. NDBA is a trade association for banks and thrifts that operate offices in North Dakota. Our 81 state and national bank and federal savings bank members serve the financial needs of North Dakotans from more than 300 North Dakota offices. We also want to state our appreciation for agency undertakings to educate bankers about the substance of the proposals and for the development of a calculator to help banks measure the impact of the proposals on their individual institutions. Without those efforts bankers, would have found it vastly more difficult to assess the proposals. We urge the agency to continue to provide bankers with practical tools to evaluate future proposals. That said, **NDBA opposes adoption of both the proposed capital rules and risk-based guidelines. We and our banks implore you to withdraw them and re-work the proposals to**

reflect both the need for a strong, but not impenetrable, capital base and the pivotal role that banks, as lenders, play in U.S. economic recovery and sustenance.

NDBA and its member banks believe the proposed rules and guidelines will actually stifle banks' abilities to meet their customers' legitimate financial needs, particularly for affordable housing (which is critically needed in North Dakota) and for the loans that fuel economic activity and development. We also fully expect that adoption and implementation of the proposed rules and guidelines will drive many committed, independent community bankers out of the business because they simply do not have cost effective access to either the human or capital resources that are required to comply with rules and guidelines that are so complex and "granular" that they must be reviewed and assessed for virtually every loan a community bank will consider making. **Truly, we cannot overstate our misgivings. The adoption of the proposed rules and guidelines will mean there will be fewer good loans made in North Dakota and fewer banks to make them. How ironic. Every North Dakota bank survived the recession; now many are jeopardized by the regulatory "cure".**

Some, but not all of the major issues are discussed below.

Overall, the proposals divert resources from and actively discourage lending precisely when loans are needed to support economic growth.

Unsubstantiated Risk Weights
We participated in agency sponsored educational forums concerning the proposals. From them it is clear that the risk weighting proposals lack a credible research foundation. Indeed, based on regulator comments during those forums, it appears most if not all new risk weights were based on regulatory intuition instead of research. This is irresponsible. Risk weighting affects how community banks operate and what products they offer by encouraging investments in lower risk weight assets and discouraging investments in higher risk weight assets. Many describe the risk weighting proposals to be draconian or punitive for community banks because they impose unsubstantiated risk weights for loans that are the economic lifeblood of community banks, their customers and their communities and they apply them to all banks in a one size fits all approach that is harmful to individual banks and the industry as a whole.

Contraction in Residential Mortgage Lending
Housing is a prime example. North Dakota did not have a housing bust and is now experiencing substantial economic growth. Providing housing for needed workers and their families and for persons displaced by development-related, high housing costs is a critical concern and is a recognized key to maintaining economic prosperity over time. We need and want our community banks to be able to make profitable housing loans and have been working diligently to develop ways to help them be able to expand their residential real estate lending. Our bankers have been honest about the impediments they face and fear they cannot afford the resources that are required to comply with a quagmire of new mortgage loan regulations. Now, they face capital risk weight rules that discourage residential mortgage loans by making the bank have to set aside more capital because a federal agency has decided, years after the fact, that house loans are risky. This, even though no North Dakota bank has been shown to have been placed at risk by making local housing loans. We are aware of no community bank expert who does not conclude that the combined effect

of the recent flood of mortgage loan regulations and increased risk weights for residential mortgage loans will be a demonstrable reduction in residential mortgage lending by community banks. Federal regulators, well-intended as they may be, are simply making that business too complicated and too expensive for many community banks.

The standardized approach for risk weighting residential real estate loans that have a balloon payment feature is particularly destructive to community banks and, again, is not supported by any empirical evidence of abuse by those banks. Community banks use balloon payment loans to manage interest rate risk, not to abuse their customers. A loan is paid based on a 30 year amortization. When a loan comes due, typically in five years, it is refinanced as a matter of course at then current interest rates. The proposal risk weights balloon payment loans at 200% until their loan to value is under 80% and at 100% after that. The likely result for rural, community banks and their customers is that a profitable source of residential mortgage lending will be eliminated and interest rate risk will be more difficult to manage.

The proposed treatment of mortgage servicing rights will cause banks to reassess and reduce their mortgage lending activities and support. Why would they not when the federal regulatory agencies are making it so crystal clear that in their view the way to address a housing crisis that was not caused at all by community banks is to make it so expensive and complicated that many community banks will opt out of housing loans rather than risk the compliance and supervisory sanctions that are now being proposed?

The standardized approach similarly discourages lending for what it categorizes as "high volatility" commercial real estate which includes multifamily residential properties by imposing a risk weight of 150%. North Dakota desperately needs multifamily housing. Increasing the amount of capital a bank must devote to multifamily housing means less of it will be financed and built just as we need it and cannot do anything other than impede North Dakota's economic development.

Complexity and Compliance
Basel III capital requirements were not developed for community banks. They were developed for financial institutions that have international operations and complex investment strategies. Applying Basel III concepts to community banks harms them and is absolutely not required for their proper supervision. FDIC board member Hoenig is right: it's time to start over.

Community banks do not pose systemic risk and should not be treated by Basel III based rules and guidelines as though they do. According to the Comptroller of the Currency, most community banks maintain capital levels that meet or exceed those now proposed. Publicity about this OCC insight is apparently intended to ease fears that the proposed rules and guidelines will drive community banks to raise capital even though (as it is generally acknowledged) they do not have access to capital markets. If community banks as a group do not need to raise more capital, what is the point of requiring them to track, measure, re-measure and report capital adequacy under multiple, ever more complex systems and imposing multiple capital standards that appear to act to impede even well capitalized banks from making distributions for such things as even the payment of taxes in the case of Sub S banks? **Have community bank operations changed over the past few years such that regulatory agencies are suddenly incapable of assessing the capital adequacy of a community bank for its types of operations under the current leverage and risk based capital rules?** We think not and we hope you, as bank supervisors, will consider whether the benefits of implementing the proposed rules and guidelines for community banks are really worth the costs. North Dakota's and other states' community banks do not have endless financial and human resources to expend trying to figure out and comply with make-work regulations that were developed in the contexts of international banking business models that do not apply to community banks. **Current leverage and risk -based capital rules work well for community banks and their supervisors and should be retained.**

Additional Critical Problems
Our community banks have expressed their concern about other aspects of the standardized approach:

Trust Preferred Securities
Community banks and their holding companies have not been shown to have abused trust preferred securities. Accordingly, we oppose the early elimination of trust preferred securities as a component of capital; the phase out of trust preferred securities should be left at 15 years as provided by the Dodd Frank Act.

Capitalizing Unrealized Gains and Losses
Capitalizing unrealized gains and losses do nothing more than inject harmful volatility. We do not dispute that information about unrealized gains and losses may be important to the assessment of a bank's financial condition. However, that information is already available to regulators and investors. Community bankers cannot control market fluctuations. The only way they will be able to manage the unpredictability is to set aside capital to cushion against it. Capital that is set aside is not available for loans.

Access to Capital/ Shrinking the Bank
Community banks lack of access to capital markets is axiomatic. When a community bank needs to raise its capital levels it has two realistic choices: ask its shareholders or local citizens for more money or shrink the bank. Since the overall effect of the proposed rules is to make traditional banking activities less profitable and more expensive for shareholders, we think it is predictable that, in the future, there will be less interest in providing new capital for small banks and that banks will actively seek to shrink in order to be compliant with capital requirements. Because they lack access to capital markets, community banks will be hit first and hardest.

Conclusion
Most of North Dakota's banks are well under $ 1 billion in assets. We have focused our comments on community banks because the Basel III rules and standardized approach endanger these banks' future vitality, the future vitality of their communities, and thus the future vitality of North Dakota. (The economic vitality and contributions of larger banks will also be impeded by the proposed rules, but others can speak to that.) **But, capital standards must realistically reflect the variety of types of banks and banking operations that exist in the United States. Here, the proposed rules do not.** Additionally, their development appears to have no consideration of the longer term consequences beyond higher capital. As small banks are forced to live under rules that were

originally designed for big banks, the small banks will have to become bigger by consolidation in order to survive. And, because the resulting banks will be fewer, bigger, and less diversified, these bigger banks will pose increased risk to the system.

The bank regulatory agencies can do better. Capital rules can distinguish between banks and types of bank operations. Capital rules can support a diversified banking system. We are asking you to withdraw the proposed rules and reassess how to support the U.S. banking system of small to world class banks. Our diversity in banks has served the U.S. well and is a major contributor to our comparative economic strength even in difficult times. Capital requirements should be a backstop of support for that system. The Basel III and standardized approach proposals are not. As such they should be withdrawn and the process re-evaluated with a clear consideration for community banks and the effect of the rules on bank operations of all sizes and on the economic recovery and future of the U.S.

Sincerely yours,
NORTH DAKOTA BANKERS ASSOCIATION

Rick Clayburgh\
President and CEO