December 18, 2017

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street SW
Suite 3E-218, Mail Stop 9W-11
Washington, DC 20219

Ms. Ann E. Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

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

Re: Simplifications to the Capital Rule Pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996

Dear Ladies and Gentlemen:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to provide comment on the proposed rulemaking to simplify the current regulatory capital treatment related to certain capital deductions for mortgage servicing assets, certain

[1] The Independent Community Bankers of America®, the nation's voice for more than 5,700 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services. With 52,000 locations nationwide, community banks employ 765,000 Americans, hold $4.9 trillion in assets, $3.9 trillion in deposits, and $3.3 trillion in loans to consumers, small businesses, and the agricultural community. For more information, visit ICBA's website at www.icba.org.

investments in other financial institutions, certain deferred tax assets (DTAs), and the current high volatility commercial real estate (HVCRE) designation applicable to certain acquisition, development, and construction (AD&C) loans.

ICBA and community bankers across the country are excited at the prospect of curbing some of the damaging effects of Basel III and its contribution to the regulatory burden currently faced by community banks. ICBA supports the work of the banking agencies to take these initial steps to provide regulatory relief and views the changes proposed herein as a necessary first step in a much larger regulatory burden reduction effort. The economic harm brought about by Basel III, particularly the unwarranted criticism levied on quality core banking assets like mortgage servicing rights and AD&C loans, stems from international capital accords that were never intended to apply to small banking organizations like community banks in the United States. As we have stated repeatedly in past meetings, letters, and other communications, community banks are key job creators in urban, suburban, and rural locales and continue to act as a pillar of strength for those consumers and small businesses that make up the diverse fabric of our great nation.

Although the regulatory agencies have proposed amendments to Basel III that provide much needed help to community banks mired in regulatory stress, the agencies must move further down the path of meaningful regulatory relief. Therefore, ICBA requests that the current prospective suspension of HVCRE assets be finalized with no implementation of the high volatility acquisition, development, and construction loan (HVADC) exposure requirement. For banking organizations with total consolidated assets of $50 billion or less, all prudently underwritten AD&C loans should carry the 100% risk weight regardless of the type of project sourcing the loan and the level of investment by the borrower.

The proposed lifting of the common equity tier 1 capital deduction threshold from 10% to 25% for mortgage servicing assets, temporary difference deferred tax assets (DTA), and investments in the capital of unconsolidated financial institutions should be further raised to a threshold of 50% for banking organizations with total consolidated assets of $50 billion or less. The proposed removal of the aggregate 15% common equity tier 1 capital deduction threshold should be finalized. Finally, the risk weight applied to mortgage servicing assets, temporary difference DTAs and investments in the capital of unconsolidated financial institutions not deducted from common equity tier 1 capital should be reduced to 100% for those banks.

The Proposed Rulemaking

The Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, and the Federal Deposit Insurance Corporation are proposing to amend the Basel III capital rule by altering significantly certain risk weights and threshold

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deductions on key bank assets. These alterations are being proposed in response to repeated calls by ICBA and community banks that small banking organizations, none of which possess the ability to threaten the viability of the deposit insurance fund, are facing a significant regulatory burden when trying to comply with the agencies' new capital rules. In addition, through Basel III, regulators have flagged certain quality community bank assets as degrading community bank balance sheets. This proposal aims to correct some of those misinterpretations by regulators.

The proposal aims to eliminate the classification of AD&C exposures as HVCRE on a prospective basis for banks that use the standardized approach under Basel III. HVCRE classification would continue for banks that use the advanced approaches under Basel III. HVCRE loans currently represent certain AD&C loans where the borrower has not contributed at least 15% of the as-completed value of the project in cash or readily marketable assets with the total investment remaining in the project throughout its construction phase. These loans currently carry a punitive risk weight of 150% until they achieve permanent financing. One-to-four family residential properties, community development projects, and agricultural exposures are exempt.

The HVCRE classification would be replaced on a prospective basis with a more broadly defined HVADC classification. HVADC exposures would be those that primarily finance acquisition, development, or construction activities. Loans where 50% or more of the loan proceeds are used for these activities would be classified as HVADC exposures. Loans that meet the HVADC criteria would be considered HVADC exposures regardless of the amount of contributed capital by the borrower. One-to-four family residential properties, community development projects, and agricultural exposures would continue to be exempt. Permanent loans where the borrower has clearly identified an ongoing source of payment sufficient to service the principal and interest payments aside from the sale of the property would also be exempt. HVADC exposures would carry a risk weight of 130%, an improvement over the current risk weight of 150% for HVCRE exposures.

The proposal is also designed to simplify and improve the regulatory burden associated with deductions from common equity tier 1 capital for mortgage servicing assets, temporary difference DTAs, and significant investments in the capital of unconsolidated financial institutions in the form of common stock. These assets are currently deducted from common equity tier 1 capital when they individually exceed 10 percent or collectively exceed 15% of common equity tier 1 capital. Amounts that are not deducted will be risk weighted at 250% starting on January 1, 2018. In addition, non-significant investments in the capital of an unconsolidated financial institution above certain thresholds and significant investments in the capital of an unconsolidated financial institution that are not in the form of common stock are deducted from common equity tier 1 capital when they exceed 10% of the bank's common equity tier 1 capital under the corresponding deduction approach.

Under the proposal, banks that use the standardized approach under Basel III would deduct from common equity tier 1 capital MSAs, temporary difference DTAs, and investments in the capital of unconsolidated financial institutions that individually exceed 25% of the banking organization's common equity tier 1 capital. MSAs and temporary difference DTAs that are not deducted would continue to be risk weighted at 250%. Investments in the capital of unconsolidated financial institutions that are not deducted would be risk weighted based on the applicable treatment for that instrument according to the current Basel III risk weights for equity instruments, which are currently dependent on the type of instrument in question.

The proposal also simplifies current minority interest calculations. Currently minority interest is limited as a component of regulatory capital based on the amount of capital held by the consolidated subsidiary relative to the amount of capital the subsidiary would need to hold to avoid any restrictions on capital distributions and discretionary bonus payments. Under the proposal, banks that use the standardized approach under Basel III would include common equity tier 1 minority interest up to 10% of the parent banking organization's common equity tier 1 capital, tier 1 minority interest up to 10% of the parent banking organization's tier 1 capital, and total capital minority interest up to 10% of the parent banking organization's total capital.

ICBA's Comments

ICBA supports this proposed rulemaking as a strong message from the prudential bank regulators that their focus should be on maintaining high quality safety and soundness standards for community banks while understanding that community banks are not at risk of compromising the global financial system, the very risk that Basel III was created to protect against. This proposal, if implemented, would improve the regulatory capital framework for community banks by allowing these institutions to continue to originate or otherwise acquire quality bank assets like mortgage servicing rights, AD&C loans, and investments in other financial institutions.

The capital requirements surrounding HVCRE have been problematic from the inception of Basel III and simplification of the criteria for identifying those AD&C loans needing a higher risk weight are long overdue. Community bankers have been confused from the very beginning about which loans meet the criteria for inclusion in the HVCRE risk weight category. The process of evaluating particular loan attributes that might give rise to HVCRE designation is expensive, time consuming, and diverts community bank resources from key management activities.

However, the proposed amendment to assign a 130% risk weight to all AD&C loans on a default basis penalizes quality construction and development loans while correcting the pitfalls of the HVCRE identification burden. Through this proposed change, regulators are essentially trading one poor capital decision for another. AD&C loans originated at community banks do not automatically subject the bank to increased credit risk simply because they involve property improvement projects. Community banks are in the best position to understand the underlying economics behind a specific construction project, the viability of the project, and the ability of the borrower and any security interest to protect the bank against future credit losses.

ICBA has concerns that otherwise common-sense construction projects that should be financed by community banks will either not be started at all or financed through nonbank lenders at unfavorable terms to the borrower. The AD&C loans that finance many construction projects are important job creators in local communities across the country that provide both temporary and permanent employment opportunities in many rural and underserved areas. Regulators should revisit the 130% risk weight for all AD&C loans and propose a common-sense alternative to the punitive capital treatment that more fairly acknowledges the value that these loans provide to community bank borrowers and their communities. **ICBA recommends that for banking organizations with total consolidated assets of $50 billion or less, regulators allow for all prudently underwritten AD&C loans to be risk weighted at 100% without limitations on the borrower's investment or the debt service coverage ratio associated with the borrowing arrangement.**

ICBA welcomes the proposed increased deduction thresholds for MSAs, temporary difference DTAs, and investments in the capital of other financial institutions as a step in the right direction. The current 10% individual deduction threshold and 15% aggregate deduction threshold for these items penalizes community banks who have held high quality banking assets like MSAs and trust preferred securities for many years. The original introduction of punitive caps on these assets depressed prices and decreased demand for them in financial markets, making their disposition difficult and costly when trying to maintain healthy capital levels under the Basel III framework.

While the elimination of the aggregate deduction threshold and the raising of the individual deduction threshold to 25% provides regulatory relief, ICBA is concerned that regulators have not gone far enough to ensure that these quality banking assets are not unfairly criticized when they provide quality future earnings for community banks. **In order to better reflect the earning potential for these assets, ICBA believes the individual cap should be raised not to 25% but to 50% of common equity tier 1 capital for banking organizations with total consolidated assets of $50 billion or less. In addition, the risk weight assigned to these assets when they are not deducted be lowered to a 100% risk weight.**

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ICBA appreciates the opportunity to comment on the proposed rulemaking. If you have any questions or would like additional information, please do not hesitate to contact James Kendrick at james.kendrick@icba.org.

Sincerely,

/s/

James Kendrick
First Vice President, Accounting and Capital Policy

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