Bank of the Pacific

Real Values. Real Solutions.

October 16, 2012

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

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

Dear Mr. Feldman:

I am troubled by the Basel III's implications to community banks. Designed for the largest banks, applying Basel III capital requirements to small banks, given their absence of access to capital markets, presents several problems:

- Increasing capital for loans secured by primary residences will mean making less such loans as community banks cannot easily raise more capital to fund them. Meanwhile, the FDIC estimates 40% of small business lending is made by small banks, and those loans are often secured by primary residences. During the recent economy, we did not experience material deterioration of foreclosures of loans in this category as they were not underwritten the way sub-prime loans were that created the financial crisis.

- Basel III also requires marking public securities held by community banks to market. Without ease of raising capital, small banks will simply ensure all such securities are short term and therefore with less risk of mark-down. That will increase rates municipalities will have to pay for longer issues and thereby further burden tax payers.

- My bank is one of the few holders of Trust Preferred Securities. As the rules currently state, phasing out TPS in a period shorter than such securities are allowed to be repaid will result in penalties to be paid by the bank that will further reduce capital.

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Safety and soundness in our industry is essential. Among recent failures, asset concentration and participation in subprime mortgage assets and derivatives were dominant factors. The resulting economic crash caused losses for some of us who did not participate in such practices. But by continued sound banking practices, community banks are profitably contributing to the growth of our communities. Basel III would do nothing to promote such sound practices and instead hamper lending among small banks, and would unnecessarily burden community banks unfairly relative to their competition from the largest banks.

Sincerely,

G. Walker Evans
SVP, Manager Commercial Banking

October 17, 2012

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

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

Dear Mr. Feldman:

I am writing you to express my concerns relative to the adverse impact that will most certainly result from the Interagency Risk-Based Capital Proposals, more commonly referred to as Basel III. Ironically, the adverse impact of these proposed changes (which were designed primarily for the largest banks) to capital will be far more punitive for banks less than $5.0 billion in assets, largely because of their difficulty to access capital markets.

Many of these smaller community banks are the very fiber of rural America's small business and labor force. In fact, according to the acting Chairman for the FDIC, Martin Gruenberg, community banks with less than $1 billion in assets account for 40% of the small business lending in the US. For many years we have made loans to small businesses secured by personal residences that we hold within our loan portfolios. During the recent economic downturn we did not experience any significant increase in past-dues or foreclosures. Because of the increased capital requirements, and its related costs associated with loans secured by primary residences, we will either lose out to the "too big to fail" banks or, borrowers that traditionally qualified well before the subprime era will be left without reasonable financing options.

In addition, marking the investment portfolio to market is counterintuitive to safe and sound banking practices. The very nature of the investment portfolio is to provide both a source of liquidity as well as a reasonable hedge against a falling rate environment. If we begin marking this portfolio to market, it will cause community banks to substantially shorten the duration of their investment portfolio, giving rise to interest rate risk in a falling-rate environment, which is generally a time when banks need all the help they can get. (A down-rate environment generally signals a weaker economy.)

Furthermore this will be like another tax upon the already burdened taxpayers. Why? Community banks have traditionally been very active purchasers of locally originated tax exempt bonds. If we substantially reduce our participation in these longer term investments, municipalities will be forced to pay up on the interest rates in order to pull in new investors. This is an unreasonable (and I suspect unintended) consequence that no one wants to have happen to taxpayers.

Lastly, our bank is one of a few holding Trust Preferred Securities (TPS) in support of Tier 1 capital. Most likely you will not receive much in the way of comments related to TPS since few community banks hold TPS. While eliminating this for the "too big to fail" banks was ok, the accelerated elimination of the TPS over 10 years for smaller community banks is far more burdensome. It is easy for the largest banks to replace capital...not so for us. This will only serve to reduce loan growth over the next several years while TPS is eliminated. If it must be eliminated, allow the principal to amortize over the remaining life of the TPS. While this in and of itself will be burdensome, it would be more manageable and, unlike the present proposal, the principal balance would, in fact, be extinguished over time. Even as the proposal is written today, we would be penalized for paying back any TPS principal until 10 years have passed. In other words, if we had $10 million in TPS, and paid $1 million toward principal during the first year, the way it is proposed today, we would now have $8.1 million in tier 1 capital, not $9 million from allowable TPS. Under this scenario we lose an additional $900 thousand of tier 1 capital.

In closing, I have the highest regard for what is needed to shape and improve the safety and soundness for our industry. As I reflect back upon the reason for most of the recent bank failures, asset concentration dealt by far the greatest death knell for the failed institutions, followed by ineffective boards. Those of us still standing managed our way through this by adhering to sound banking practices, coupled with sound board oversight. The Great Recession did cause many of us to lose some money during this very difficult economic time; however, it is important to remember that many of us also came through it and are once again profitably contributing to the growth of our communities. Please be thoughtful before taking knee-jerk actions that detract from our ability to serve the important needs of our communities.

Sincerely,

Dennis A. Long
CEO

The Bank OF THE PACIFIC

October 18, 2012

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

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

Dear Mr. Feldman:

I am writing you to express my concerns relative to the adverse impact that will most certainly result from the Interagency Risk-Based Capital Proposals, more commonly referred to as Basel III. Ironically, the adverse impact of these proposed changes (which were designed primarily for the largest banks) to capital will be far more punitive for banks less than $5.0 billion in assets, largely because of their difficulty to access capital markets.

I have been in banking since 1974, starting as a messenger with a local community bank in Vancouver, Washington. Along my banking career I have held several key management positions with several community banks. My eyes have seen numerous changes in the bank world, but none so draconian to community banking world as the Basel III proposal. I understand the concept of the Basel III; however, the proposal tears at the fibers of many smaller community banks of rural America's small business and labor force. In fact, according to the acting Chairman for the FDIC, Martin Gruenberg, community banks with less than $1 billion in assets account for 40% of the small business lending in the US. For many years we have made loans to small businesses secured by personal residences that we hold within our loan portfolios. During the recent economic downturn we did not experience any significant increase in past-dues or foreclosures. Because of the increased capital requirements, and its related costs associated with loans secured by primary residences, we will either lose out to the "too big to fail" banks or borrowers that traditionally qualified well before the subprime era will be left without reasonable financing options.

In addition, marking the investment portfolio to market is counterintuitive to safe and sound banking practices. The very nature of the investment portfolio is to provide both a source of liquidity as well as a reasonable hedge against a falling rate environment. If we begin marking this portfolio to market, it will cause community banks to substantially shorten the duration of their investment portfolio, giving rise to interest rate risk in a falling-rate environment, which is generally a time when banks need all the help they can get. (A down-rate environment generally signals a weaker economy.)

Furthermore this will be like another tax upon the already burdened taxpayers. Why? Community banks have traditionally been very active purchasers of locally originated tax exempt bonds. If we substantially reduce our participation in these longer term investments, municipalities will be forced to pay up on the interest rates in order to pull in new investors. This is an unreasonable (and I suspect unintended) consequence that no one wants to have happen to taxpayers.

Lastly, the bank that I currently work for is one of a few holding Trust Preferred Securities (TPS) in support of Tier 1 capital. Most likely you will not receive much in the way of comments related to TPS since few community banks hold TPS. While eliminating this for the "too big to fail" banks was ok, the accelerated elimination of the TPS over 10 years for smaller community banks is far more burdensome. It is easy for the largest banks to replace capital...not so for us. This will only serve to reduce loan growth over the next several years while TPS is eliminated. If it must be eliminated, allow the principal to amortize over the remaining life of the TPS. While this in and of itself will be burdensome, it would be more manageable and, unlike the present proposal, the principal balance would, in fact, be extinguished over time. Even as the proposal is written today, we would be penalized for paying back any TPS principal until 10 years have passed. In other words, if we had $10 million in TPS, and paid $1 million toward principal during the first year, the way it is proposed today, we would now have $8.1 million in tier 1 capital, not $9 million from allowable TPS. Under this scenario we lose an additional $900 thousand of tier 1 capital.

In closing, I have the highest regard for what is needed to shape and improve the safety and soundness for our industry. Please be thoughtful before taking knee-jerk actions that detract from our ability to serve the important needs of our communities.

Respectfully submitted,

Wayne R. Kepfer
SVP – Credit Risk Officer

Bank of the Pacific
Real Values. Real Solutions.

October 19, 2012

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

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, D.C. 20219

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

RE: Basel III notice of proposed rule making

Ladies and Gentlemen:

Thank you for the opportunity to comment on proposed capital standards commonly known as Basel III. While we appreciate the Agencies efforts to address perceived weaknesses in the banking industry's capital framework, I believe the proposals as written will negatively impact community banks and our ability to serve the needs of small businesses and consumers.

Bank of the Pacific is a $644 million community bank headquartered in Aberdeen, WA. The Bank was founded in 1971 and is located in three distinct market areas in western Washington and the Oregon coast. We are primarily a business bank servicing small to medium size businesses in rural areas. Additionally, we serve many individuals through our mortgage department which provides nearly $200 million in home loans annually to people within our communities.

The areas of concern in the Basel III proposals are as follows:

Mark to market on investments

The proposal as written would require all unrealized gains and losses on available for sale securities to flow through to regulatory capital. Most banks today have large gains in the portfolio due to the historic low rate environment. However, when interest rates rise, this capital will quickly erode if banks are forced to recognize unrealized gains in their capital ratios. As of September 30, 2012, our Bank held $51.7 million in AFS securities. Based on our most recent quarterly interest rate shock analysis, if rates were to increase 400 basis points, our AFS

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portfolio and our capital would decrease by approximately $5 million or 1% of capital. The unintended consequence is that our Bank will then be forced to maintain excess capital to allow for unknown fluctuations which would directly correlate to a decrease in credit that will no longer be available in our communities.

Furthermore, the change in unrealized gains or losses is primarily related to interest rates, NOT credit risk. We use our investment portfolio as a natural hedge to our loan portfolio whereby we offset some of the variable rate loans with fixed rate longer term bonds which has been an effective way to manage net interest margin through varying interest rate cycles. To avoid inclusion in capital, we most likely will be required to make shorter-term investment decisions with significantly reduced yields which could conflict with other CAMEL components such as earnings and liquidity and weaken our asset-liability management.

We strongly recommend that AFS mark-to-market adjustments be excluded from regulatory capital.

Elimination of Trust Preferred Securities

Our Bank has $13 million in trust preferred securities which has been included in capital for nearly eight years. This is not a significant portion of our capital, but is a low cost and effective source of capital that has allowed us to provide loans and meet the funding needs of our customers. The elimination of trust preferred securities for community banks previously exempt under Dodd-Frank, will reduce our ability to grow our balance sheet by approximately $130 million thereby, reducing the availability of credit to the exact small business customers that are necessary to support job growth to get our local economies back on track. Additionally, while large banks have access to capital markets to replace trust preferred securities, community banks do not have that same luxury. This proposal has a much deeper adverse impact on community banks than on "too big to fail" banks.

Non-accrual loans

The agencies have proposed that loans 90 days or more past due or on non-accrual should be assigned a risk weighting of 150%. Currently, risks associated with problem credits are already captured through the Allowance for Loan Losses (ALLL) and in most cases assigned a specific reserve. Because the ALLL is reflective of the risk of loss in the loan portfolio, there is no need to create an additional charge to capital. Essentially, the Bank would be double counting for the same risk. Additionally, this rule would discourage banks from working with borrowers in order to move the loan off the balance sheet, and reduce our willingness to resolve credit issues during times of economic stress.

Capital Conservation Buffer

The proposed rules introduce a capital conservation buffer of 2.5%. I do not object to the proposed common equity tier 1 ratio or the increase in the tier 1 risk based ratio. However, to avoid confusion and better align the proposed capital guidelines to the existing "well-capitalized" standards under the prompt corrective action, we recommend that the capital conservation be adjusted to 2.0%.

Risk weightings for residential mortgage loans

The proposal assigns risk weightings for residential mortgages ranging from 35% to 200%. Our losses on home loans to individuals held on our balance sheet have been minimal during the last five years. The new risk weightings on 1-4 family residential loans are higher in many cases than other types of loans that would be considered riskier based on our loss experience. Additionally, as proposed any balloon payment automatically places the home loan into a Category 2 which increases the risk weighting rom 50% to 100%. I strongly recommend that Category 2 loans be redefined to exclude loans with balloon payments and not lump balloon payment loans in with negative amortizing loans. These two provisions alone would greatly reduce our ability to provide mortgage loans and limit the population of potential homebuyers that will be eligible to buy homes.

In conclusion, the above proposals as written would greatly harm our bank and the communities we serve. I strongly urge you to reconsider the Basel III proposals as they are not geared to the community banking industry.

Sincerely,

Denise Portmann

Denise Portmann
EVP & Chief Financial Officer