CARVER
FEDERAL SAVINGS BANK

deborah.wright@carverbank.com

DEBORAH C. WRIGHT
President & CEO

October 22, 2012

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

Office of the Comptroller of the Currency
250 E Street, SW
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, D.C. 20429

Re: Basel III Capital Proposals
OCC: "Basel III OCC Docket ID OCC-2012-0008, 0009, and 0010"
Federal Reserve Board: "Basel III Docket No. R-1442"
FDIC: "Basel III FDIC RIN 3064-AD95, RIN 3064-AD96, and RIN 3064-D97"

Ladies and Gentlemen:

This comment letter is in response to the Basel III proposals[1] (the "Proposed Rules") that the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (collectively the "Agencies") approved. Carver Federal Savings Bank ("Carver") is very concerned about the probable negative, and possible fatal, impact Basel III will have on community banks, especially Community Development Capital Initiative ("CDFI") banks, the customers we serve and the economic health of the United States.

Carver fully concurs with the Agencies' goals of helping ensure the United States maintains a prosperous banking system that provides valuable financial services in a safe and prudent

[1] The proposals are titled: *Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, and Transition Provisions; and Regulatory Capital Rules: Standardized Approach for Risk-weighted Assets; Market Discipline and Disclosure Requirements.*

manner during prosperous and challenging economic periods. Carver also recognizes and supports the Agencies' goal to establish capital requirements that are appropriately sensitive to different risk profiles. Unfortunately, Basel III, as drafted, does not accomplish these goals.

About Carver

Founded on November 5, 1948, and named for agricultural researcher and scientist George Washington Carver, Carver Federal Savings Bank formally began operations on 125th Street in Harlem, providing local residents a place to save and obtain mortgages to buy homes in their own communities on January 5, 1949.

Today, Carver is the largest African- and Caribbean-American operated bank in the United States ($640 million in assets) and channels its resources into underserved neighborhoods, including reinvesting over 80% of its deposits locally ("Outstanding" CRA rating). The Bank remains rooted in expanding wealth enhancing opportunities in the communities it serves, by expanding access to capital and financial advice, to consumers, businesses and non-profit organizations, including faith-based institutions. Carver remains headquartered in Harlem, and predominantly all of its nine branches and stand-alone 24/7 ATM Centers are located in low-to-moderate income neighborhoods. Carver will be opening its tenth branch later this month in East Harlem, a largely Hispanic neighborhood.

Carver's product mix includes not only traditional banking products vital to local communities, but Carver is one of the only banks in the nation that also offers a full array of products and services tailored to the unbanked (i.e., check cashing, money transfers, bill payment and reloadable prepaid cards). Approximately 65% of customers surrounding Carver's branch network are unbanked or underbanked, making Carver's services vital.

The U.S. Treasury Department has designated Carver as a Community Development Financial Institutions (CDFI) because of our community focused banking services and our dedication to the economic viability and revitalization of underserved neighborhoods. This is both a unique mission and a statutory directive that must be fostered for the benefit of the inner-city neighborhoods we serve.

National Bankers Association

We respectively refer the Agencies to the National Bankers Association ("NBA") comment letter that contains compelling reasons why Basel III should not be applied to minority banks and CDFIs. The NBA is a trade organization formed in 1927 representing the interests of minority depository institutions, including African American, Asian American, Hispanic, Indian American, Native American and women-owned financial institutions. Their comment letter includes the following:

1. By their very nature, minority banks are at a competitive disadvantage from peer banks and thus have difficulty maintaining earnings and capital levels near those of other peer banks. This is due in part to the fact that minority banks operate predominately in low- to moderate-income communities, without the ability to utilize highly profitable

products or services. Minority banks have accepted this reality in pursuit of their higher social mission.

2. Minority banks are clearly needed in the communities we serve. The U.S. Government Accountability Office, GAO Report 07-6, *Minority Banks: Regulators Need to Better Assess Effectiveness of Support Efforts (2006)* documents this need.

3. The Proposed Rules are designed from a global perspective, much of which is inapplicable to inner-city communities. Minority banks and CDFIs, by definition, engage almost exclusively in local activities, providing credit and services to communities that need them most. None of these activities led to the international crisis that gave birth to Basel III.

4. The Agencies are compelled to consider the impact the Proposed Rules would have on the viability of inner-city banks, which have successfully been fulfilling their mission for years without the Proposed Rules. Section 308 of the Financial Institutions Reform, Recovery and Enforcement Act ("FIRREA") explicitly recognizes the need for strong minority banks, directing the applicable regulatory bodies to achieve the following five goals:

    (*1*) Preserve the present number of minority banks;
    (*2*) Preserve their minority character in cases involving merger or acquisition of a minority bank by using general preference guidelines;
    (*3*) Provide technical assistance to prevent insolvency of minority banks not now insolvent;
    (*4*) Promote and encourage creation of new minority banks; and
    (*5*) Provide for training, technical assistance, and educational programs.

5. Raising capital is difficult for all community banks, and even more difficult for minority banks and CFDIs, that do not have the same income opportunities of non-CDFI institutions. Applying the Proposed Rules would require CDFIs to raise more capital, threatening their viability. Special consideration is therefore required to develop and apply capital requirements appropriate to the nature and risk profile of CFDIs.

6. In summary, because Basel III was not designed to apply to small, local banking organizations that do not engage in international activities, and because FIRREA requires the Agencies to give special consideration to minority banks, the Proposed Rules should not apply to minority banks and CDFIs.

Impact on Community Banks

In addition to the valid arguments posited by the National Bankers Association, other evidence continues to emerge that the Proposed Rules will have a detrimental impact on community banks. Recently, Trepp LLC, applying Basel III standards, conducted a capital stress test utilizing second-quarter 2012 call report data of 6,151 banks and found that 10% of the banks would need to raise additional capital to maintain ratios at the minimum levels established under Basel III, with big banks performing much better than midsize and small banks. As is documented in the NBA comment letter and discussed below, it is very difficult for community banks, especially CDFIs, to raise new capital. The proposed new capital requirements on community banks is not in the best interests of ensuring a network of healthy vibrant local community banks, but rather encourages further consolidation and demise of the community banking structure, the group that extends 40% of the small business lending in the United States.

Phase out of Trust Preferred Securities as Capital Instruments

Carver is extremely concerned that the Proposed Rules eliminate Trust Preferred Securities as a form of core capital for institutions between $500 million and $15 billion. This is directly contrary to the intent of Dodd-Frank, specifically the Collins amendment, and does not advance safety and soundness for this group of banks. Rather, it places many financial institutions in peril as the three alternatives to this are to: (l) raise more capital, (ii) shrink the bank or (iii) merge.

Raising capital for this entire segment of the industry is not realistic. To the extent there is access to capital for a community bank, investors are focused on investing funds for growth opportunities, not to fill capital holes caused by changes in regulation. In 2011, Carver was successful in a capital raise (discussed below) and knows firsthand how difficult it can be. Carver also knows many banks unable to raise capital, and like Carver would be at peril should trust preferred securities be disallowed. It is important to recognize that, in reliance upon the capital rules, in 2003 Carver raised $14.1 million through issuance of trust preferred securities which have a thirty year life. Assuming the Basel III elimination phase in were complete Carver's June 30, 2012 Tier 1 core capital would decrease by 288 basis points from 9.72% to 6.84%, which is a shocking 29.6% reduction. The ten percent phase out in 2013 would reduce Carver's Tier 1 core capital by 22 basis points.

Shrinking a bank's size to meet capital ratios is counterproductive, as it generally leads to lower income without a proportional decrease in expenses. There are base costs every bank must face, and as these base costs continue to increase, a bank's size and earnings must also increase. Further, to the extent there is a decrease in expenses, it will most likely include a reduction in staff and a reduction in customer products and services, neither of which benefit society.

Faced with the difficult prospect of raising capital and the unpalatable option of shrinking the bank, many banks will likely choose to merge out of existence, assuming this is an option. Carver could easily be one of these casualties given the limited interest of large industry participants in poor communities. Further industry consolidation will destroy many of the unique contributions local community banks bring to their communities. Rather, fewer banks means risks are aggregated into fewer hands and customers have fewer choices.

Carver's Capital Structure

Carver also has concerns about how its common stock and Series D preferred stock may be treated under the Proposed Rules. Carver believes its common stock and Series D preferred stock are structured such that they both would be treated as Common Equity Tier 1 under the Proposed Rules. However, review of the Proposed Rules and conversations with a representative from the FDIC has left Carver unsure. In connection with a $55 million capital raise that occurred on June 30, 2011, Carver issued approximately 3.5 million shares of common stock and 45,115 shares of Series D preferred stock. The 3.5 million shares of common stock were issued to the United States Department of the Treasury ("Treasury) in connection with conversion of their Series B preferred stock into common stock (2.3 million shares, valued at approximately $19 million) and seven independent investors ("Investors") (1.2 million shares, valued at approximately $10 million). Carver issued the Series B preferred stock in connection with our participation in the Troubled Asset Relief Program ("TARP"). The Treasury currently owns approximately 63% of the common stock and the Investors currently own approximately 33% of the common stock. As part of the capital raise, Carver also issued the 45,115 shares of Series D preferred stock, valued at approximately $45 million, to the Investors. The Series D preferred stock has a liquidation preference of $0.01 per share, is non-voting, non-redeemable, has no expectation of redemption and has no entitlement to dividends unless a common dividend is paid. The Series D preferred stock also has a conversion feature, converting it into common stock at a set conversion rate upon its sale to a third person.

Carver is concerned that there may be two grounds for eliminating the Series D preferred stock from Common Equity Tier 1. The first is the $0.01 per share liquidation preference over common stock, which appears to be a technical basis to disqualify the Series D preferred stock as common stock. The second stems from slide 9 of the FDIC's "Notice of Proposed Rulemaking: Regulatory Capital" presentation. This slide provides that the Proposed Rules "[e]xpect the majority of Common Equity Tier 1 to be **voting** shares." Since the Series D preferred stock is designed to be treated as Common Equity Tier 1, it could be excluded from capital due to its non-voting nature. Excluding the Series D preferred stock, on a pro forma basis, would be devastating, reducing Carver's June 30, 2012 Tier 1 Capital ratio from 9.72% to 2.74%.

Carver also has concern, based upon discussion with a representative of the FDIC, that the Proposed Rules expect the U.S. government to hold less than a majority of common stock in any financial institution. Carver could not locate anything explicit on this, but believes it prudent to at least bring up the point in this comment letter. As stated above, U.S. Treasury holds the majority of voting common stock. Excluding the Treasury's holdings would, on a pro forma basis, reduce Carver's June 30, 2012 Tier 1 Capital ratio from 9.72% to 6.77%.

Clarification that the above situations would not negatively impact Carver's capital ratios is important.

<u>**Other Concerns**</u>

Complexity and uncertainty. The Proposed Rules add unnecessary complexity and uncertainty to community banks' ability to operate in a safe and sound manner. The Proposed Rules will first require Carver, and all other community banks, to expend great resources understanding and applying the new capital rules. Next the new capital rules will require banks to expend resources addressing the impact the rules will have, including addressing the unintended consequences, such as reducing products and services offered to customers and reducing a bank's ability to grow earnings and in turn capital. It is clear to everyone involved (bankers, legislators, regulators, investors and even customers) that banking continues to become more difficult and operating efficiencies continue to become more critical. The regulatory burden of the Proposed Rules will only add to this challenge without apparent commensurate benefits.

Unrealized gains and losses flowing through capital. Allowing unrealized gains and losses on available for sale securities to flow through to regulatory capital would bring interest rate risk into the regulatory capital standards, greatly increase the volatility of banks' capital ratios, and undermine prudent risk management. Carver currently has approximately $114 million in available for sale securities (approximately 18% of Carver's total assets). The vast majority of Carver's securities are in agencies and the remainder is in AAA or AA rated investments. Changes in interest rates, which are inevitable, can and will dramatically impact a bank's, including Carver's capital ratios. In a rising rate environment, portfolio losses could easily exceed a bank's annual income. This exposure is too great and would limit banks' ability to invest in securities, reducing the ability to effectively utilize excess cash and mange liquidity. The better method of measuring the potential impact of changes in security values is through interest rate risk modeling both on a Gap and economic value of equity basis. Adding the additional complexity and burden contained in the Proposed Rules hinders, rather than helps, safe and sound banking practices.

Risk weighting on structured securities. Carver recognizes the trend is away from rating agencies, but providing a 1,250% risk weighting option has no relation to the actual risk in the security and is punitive. Carver has approximately $15 million of securities that fall into this category. Carver is capable of utilizing the Gross Up approach, but even that approach appears too conservative. Since the securities are a relatively small portion of Carver's balance sheet, under the Gross Up approach, they have a small impact on capital. However, under the 1,250% approach, on a pro forma basis, the securities would reduce Carver's Total Risk-based Capital Ratio at June 30, 2012 by a staggering 294 basis points from 17.63% to 14.69%, which is a 17% reduction. We believe the risk weighting requirements for structured securities in the Proposed Rules should be reviewed and adjusted to appropriate levels.

Increased risk ratings on residential loans, commercial real estate loans and delinquent loans. Carver believes that increasing risk ratings on residential loans, commercial real estate loans and delinquent loans is redundant, distorts a bank's strength and will likely lead to banks reducing certain lending activity to the detriment of customers and certain communities. Carver takes very seriously its risk weighting process and loan loss allowance preparation. As such, Carver believes it appropriately accounts for risks in its loan portfolio through the allowance preparation process. Having an appropriate loan loss allowance takes into consideration all the factors that an increased risk weighting process would add, making this section of the Proposed Rules redundant.

Mortgage servicing capital requirements. Although Carver has a very small mortgage servicing portfolio at this time, we may determine it is appropriate to pursue this service. However, the proposed capital requirements increasing risk weightings for off balance sheet exposure, which appear excessive relative to the level of exposure, could eliminate this potential source of income. Carver requests the proposed capital requirements be reevaluated for appropriateness.

In summary, the Agencies' goal to enhance the capital assessment process is laudable. However, the proposals contained in Basel III, in many instances, do not appear to accomplish this goal and would have a material adverse impact on community banks' ability to serve customers and continue our role in strengthening local economies.

Thank you for your consideration.

Regards,

Deborah C. Wright

Deborah C. Wright
Chairman & CEO