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 comment on the Basel III proposals that were recently issued for public comment by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation.

Applicability of Basel III to Community Banks

Community banks should be allowed to continue using the current Basel I framework for computing their capital requirements. Basel III was designed to apply to the largest, internationally active, banks and not community banks. Basel III is overly complex, would create volatility in regulatory capital (i.e. due to normal market fluctuations) and would impair various forms of lending (i.e. single family residential). Community banks operate on a relationship-based business model that is specifically designed to serve customers in their respective communities on a long-term basis. This volatility and complexity would impair our ability to bank our customers' relationships and would not add significantly to our Bank's risk management.

Incorporating AOCI as Part of Regulatory Capital

Inclusion of accumulated other comprehensive income (AOCI) in capital for community banks will result in increased volatility in regulatory capital balances and could rapidly deplete capital levels under certain economic conditions. AOCI for most community banks represents unrealized gains and losses on investment securities held available-for-sale. Because these securities are held at fair value, any gains or losses due to changes in interest rates are captured in the valuation. Recently, both short-term and long-term interest rates have fallen to historic lows generating unprecedented unrealized gains for most investment securities. Additionally, demand for many implicitly and explicitly government guaranteed securities has risen due to a flight to safety and government intervention in the capital markets. This increased demand has caused credit spreads to tighten further increasing bond valuations. Interest rates have fallen to levels that are unsustainable long-term once an economic recovery accelerates. As interest rates rise, fair values will fall causing the balance of AOCI to decline and become negative. This decline will have a direct, immediate impact on common equity, tier 1, and total capital as the unrealized losses will reduce capital balances.

At my bank, for instance, if interest rates increased by 200 basis points, Century Bank’s bond portfolio would go from a $3.8 million gain to a $9.5 million loss. Our tier one leverage capital ratio would change from 10.8% current to 11.5% (including unrealized gain) to 9.8% (with a 200 b.p. shock).

New Risk Weights

The proposed risk weight framework under Basel III is too complicated, would force significant software upgrades, and will be an onerous regulatory burden that will penalize community banks. In addition, I would anticipate that banks such as ourselves would consider exiting the residential mortgage origination market which could potentially jeopardize the housing recovery.

Increasing the risk weights for residential balloon loans, interest-only loans, and second liens will penalize community banks who offer these loan products to their customers and deprive customers of many financing options for residential property. Additionally, higher risk weights for balloon loans will further penalize community banks for mitigating interest rate risk in their asset-liability management. Community banks will be forced to originate (or will not originate) only 15 or 30 year mortgages with durations that will make their balance sheets more sensitive to changes in long-term interest rates. Many community banks will either exit the residential loan market entirely or only originate those loans that can be sold to a GSE. Second liens will either become more expensive for borrowers or disappear altogether as banks will choose not to allocate additional capital to these balance sheet exposures.

Community banks should be allowed to stay with the current Basel I risk weight framework for residential loans.

Proposed Phase - out of Trust Preferred Securities

We object to the proposed ten year phase-out of the tier one treatment of instruments like trust preferred securities (TRUPS) because it is reliable source of capital for community banks that would be very difficult to replace. We believe it was the intent of the Collins amendment of the Dodd-Frank Act to permanently grandfather tier one treatment of TRUPS issued by bank holding companies between $500 million and $15 billion. Phasing out this important source of capital would be a particular burden for many privately-held banks and bank holding companies that are facing greatly reduced alternatives in raising capital. Century Bank's Parent (Century Financial) currently has $12 million in Trust Preferred Securities. The Bank and Century Financial's assets are marginally above $500 million.

We urge the banking regulators to continue the current tier one treatment of TRUPS issued by those bank holding companies with consolidated assets between $500 million and $15 billion in assets.

Subchapter S Community Banks

Imposing distribution prohibitions on community banks with a Subchapter S corporate structure conflicts with the requirement that shareholders pay income taxes on earned income. Those banks with a Subchapter S capital structure would need to be exempt from the capital conservation buffers to ensure that their shareholders do not violate the provisions of the Internal Revenue Code. We recommend that the capital conservation buffers be suspended during those periods where the bank generates taxable income for the shareholder.

Sincerely yours

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