PINNACLE BANK

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

Dear Mr. Feldman:

We are writing to comment on the proposed Basel III capital requirements issued in June 2012. We appreciate the opportunity to provide input on this most important issue. We are a community bank that began operations in Greenville, South Carolina in 2006 and have grown modestly and are approaching $150 million in assets. We have always maintained a "well capitalized" rating and have Tier 1 capital of over 12%. We have been profitable for a number of years and obtained cumulative profitability in our fifth year of operation despite a very difficult economic environment the last three years. Like most banks, we are struggling with the never ending new regulations and balancing maintaining profitability and compliance with these new regulations.

Before dealing with any of the specific proposals, we will state we are most concerned by the opinion that Basel capital requirements should be applied to community banks (we understand the term community banks can have varied definitions but we believe this group should, at a minimum, include all banks less than $10 billion in assets). While the Basel accords and guidelines have been in place for many years, we believe the regulatory agencies have historically shown much wisdom by not including community banks within those requirements. Including community banks for the first time under these guidelines does not seem to be logical and ignores a fundamental banking difference that exists in the United States. The dual banking system used in this county is unique compared to most other modern banking systems and it has served us well. Previous regulators have recognized those differences and that the capital requirements established for the rest of the world dominated by a small number of large, global financial institution in each country should not apply to smaller banks. We respectfully request that the regulatory bodies reconsider the need to apply these regulations to community banks as it is not necessary to add this level of complexity to smaller institution that have no national or international impact.

We recognize the need, as the world continues to deal with financial challenges, to address capital requirements. We believe increases in required levels of capital could be more easily obtained by adjusting the existing regulations. Why should we feel a need to adopt Basel guidelines which have obviously not worked in the past by now adopting them for all community banks? Widening the scope of flawed regulations is not the answer. We suggest that the existing capital regulations be reviewed and adjusted to ultimately achieve the increased capital levels that bankers and regulators can agree are necessary. We agree with FDIC Director Hoenig that capital rules must be simple, understandable, and enforceable. These proposed regulations fall far short of the first two requirements. Finally, we caution that dramatic increases in capital levels, no matter the type of measurement used, will continue to make additional capital infusions into the community banking industry difficult. All investors require a reasonable return and nothing is accomplished by creating such high regulatory capital levels that obtaining a market rate of return by investors is impossible. The desire for capital levels that are excessively high serve, in theory, to protect regulators and the public; they realisticly result in an unattractive investment option that decreases the capital raising ability of the industry.

We believe the 1.25% of risk weighted assets limit to add to Tier 1 capital to obtain Tier 2 capital should be revisited. We are uncertain how that percentage was ever chosen but are guessing there is no real statistical basis for its selection. Much as been written about the counter cyclical nature of loan loss reserves as a result of the recent recession. We believe one realistic fact is that higher reserves would have been established by community banks in "the good times" if more of the allowance was included in capital. We do not believe it is a coincidence that very few community banks had more than 1.25% ALLL during these good times. Everyone understands that establishing the allowance is as much art as science. Including more of the allowance in Tier 2 capital would serve as a secondary incentive for banks to maintain higher levels of reserves during the good economic times.

We have several concerns about the specifics of the proposal. The most significant concern is including accumulated other comprehensive income (AOCI) as a component of Tier 1 capital. The agencies have concluded that recognizing this component could "introduce substantial volatility in a banking organization's regulatory capital ratios." Knowingly adding volatility to capital is the last thing this industry needs. While the change is positive for banks in the current low interest rate environment, ultimately interest rates will increase, resulting in unrealized losses. Including these losses in capital is not productive. You have received numerous other letters detailing these risks, which include: causing banks to make poor economic decisions by reducing the market value risk and lowering yields on bonds by purchasing very short term/low return bonds; hurting bank liquidity by placing bonds in held to maturity, eliminating the chance to sale bonds for liquidity needs just to avoid an accounting rule; ignoring the funding side of the balance sheet which will have built in gains on long term liabilities just because accounting rules do not recognize that benefit; the rules would disproportionately impact community banks given their limited access to the capital markets. Of all the items in the proposal, we find this to be the most glaring weakness.

Second, the regulations proposed a wider range of capital for residential mortgages. There can be little argument that the last few years have resulted in greater losses on mortgage loans that anticipated. We believe it should be recognized that the failure of the industry (and that is primarily the mega banks) to underwrite and the failure of the regulators to insist on proper underwriting standards should not result in an after-the-fact change in regulation that impacts thousands of banks that have not significantly changed underwriting standards. Inclusion of balloon payment loans and home equity loans as requiring additional capital does not agree with our experience or, we believe, the experience of most community banks. Capital requirements can be monitored by the loss experience and the ALLL required for community banks. On a somewhat separate note, we find that the combination of regulations being issued from both a safety and soundness and a compliance perspective are making it more difficult for community banks to originate and retain any residential mortgages. The press often discusses that more than 50% of all residential mortgage are issued by two large financial organizations. We believe the regulatory world that discourages mortgage lending by enactment of very difficult rules that benefit the consumer very little is a primary reason for this industry consolidation.

Third, the inclusion of additional capital requirements for delinquent loans seems to be redundant. All banks consider delinquencies in the calculation of the ALLL and to add additional capital on top of additions to the ALLL seems to be double counting.

We appreciate the opportunity to comment on the proposals. There are other areas of concern to us but these document the primary items as they apply to our organization. Thank you for your consideration.

Sincerely,

David G. Barnett
President and CEO