Massachusetts Bankers Association

December 19, 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

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 2055

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:

On behalf of our 150 commercial, cooperative and savings banks and federal savings banks and savings and loan associations with more than 69,000 employees throughout the Commonwealth and New England, the Massachusetts Bankers Association (MBA) appreciates the opportunity to provide comment on the proposed rulemaking titled, **"Simplifications to the Capital Rule Pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996"**. This proposal addresses potential simplifications to the definition for High Volatility Commercial Real Estate (HVCRE), the treatment of certain capital deductions for mortgage servicing assets, investments in other financial institutions, and deferred tax assets.

The Proposed Alterations to HVCRE

The proposal attempts to curb some of the effects of Basel III and lessen the regulatory burden facing our members each day. Simplifications to capital rules are always welcomed, but in order to understand the net effects, the new treatments require context as proposed. The proposal attempts to simplify the HVCRE definition by creating an entirely new definition, High Volatility Acquisition, Development or Construction (HVADC). HVADC is defined within the proposal as credit that *primarily* finances or refinances acquisition, development and construction (ADC) activities. Furthermore, the proposal clarifies that *primarily* finances means credit activities where more than 50% of the loan proceeds will be used for ADC purposes.

The proposal also adjusts risk weights for these loans from 150% to 130%. This is a welcome change as it provides needed relief from the Basel III capital structures. Nevertheless, in the attempt to simplify the capital rule, the proposal eliminates previous exemptions on certain HVCRE exposures for loan-to-value (LTV), and contributed capital amounts. In the desire to simplify treatment of these loans, it is very plausible that additional loan balances would be covered under the new umbrella of the HVADC definition. As a result, this would actually increase the risk weights for these balances from

100% to 130%. MBA has serious concerns with this portion of the proposal and the potential policy outcomes. Credit underwriting standards throughout the Commonwealth and New England are already quite strict, and generally conform or surpass supervisory standards.

The elimination of previous exemptions for capital contributions or LTV coupled with an increased risk weighting factor of 130% would certainly hurt the ability to lend. It would require careful analysis of all underwriting criteria to appropriately assess the net effect, and could potentially result in harmful consequences to regulatory capital. One such recommendation to resolve this tension would be a reduction in the risk weighting of these balances to 100% regardless of type of lending project, loan characteristic or the level of investment by the borrower. We also request that the elimination of previous exemptions be reconsidered, particularly as it relates to LTV or debt-service-coverage ratio.

The Future Treatment of Common Equity Tier 1 Threshold Deductions

MBA applauds the revised treatment of exposures subject to common equity tier 1 capital threshold deductions, such as mortgage servicing assets (MSAs) and deferred tax assets (DTA). Most specifically, increasing the deduction threshold from 10% to 25% for MSAs and DTA is a welcome change that provides regulatory relief from complex regulatory requirements. MSAs are quality assets, and the previous capital treatments depressed values and unnecessarily penalized the market and, by default, banks for holding onto these and other assets such as trust preferred securities. We would expect that raising the threshold for deductions to 25% would increase demand to a proper level and provide for healthy capital levels as the industry moves away from the more onerous Basel III framework.

One piece of criticism that we have within the proposal is the treatment of the assets that are not subject to deduction (i.e., capped). The risk weight for non-deducted amounts of MSAs and DTA will remain 250% under the new proposal. We strongly recommend that this risk weight be lowered to 100% for these assets in the final proposal. This would be consistent with the intent of the proposal and would ensure that quality banking assets are not unfairly criticized during regulatory exams as they continue to provide future quality earnings.

Finally, we note that the proposed treatment for investments in the capital of unconsolidated financial institutions (which includes common stock) appears commensurate with industry recommendations and concerns of the last several years. Nevertheless, the risk weights for non-deducted amounts for banks that do not use advanced approaches continue to be overly burdensome. 300 and 400% risk weights for equities in excess of 10% of total capital should be capped at 150%. These securities are generally very conservative, composed of Fortune 100 firms and have a historical track record of success.

Conclusion

In closing, MBA appreciates the ability to provide feedback on this crucial proposal as regulatory capital levels remain a significant concern for our members and the banking industry on the whole. The proposed changes are a positive step forward for the treatment of capital levels, and the revised definition of HVADC shows promise. Nevertheless, we urge that consideration be given to the

HVADC risk weights as well as which future loan originations and development projects will fall subject to risk weighting. The impact of the revised definition will differ from bank to bank, and any significant impact due to an expanded and broad umbrella of defined loans could lead to a restriction in lending supply. Community banks have the necessary expertise to determine the viability of development projects, and MBA has serious concerns that certain new construction projects may not be started or move to nonbank lenders under the broad HVADC definition. MBA welcomes many of the proposed changes to risk weighting and recommends lowering weights in the final rule where appropriate.

Thank you again for the opportunity to comment on the proposed rule. If you have any questions or need additional information, please contact me at (617) 523-7595 or via email: bcraigie@massbankers.org.

Sincerely,

[redacted]

Ben Craigie
Director of Compliance and Training