ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA

October 28, 2008

Office of the Comptroller of the Currency
250 E Street, SW
Mailstop 1-5
Washington, DC 20219

Attention: Docket No.OCC-2008-0006

Robert E. Feldman, Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Attention: Comments/Legal ESS

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street an Constitution Avenue, NW
Washington, DC 20551
Docket No. R-1318

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attn: No. 2008-0002

Re: Risk-Based Capital Guidelines; Capital Adequacy Guidelines: Standardized Framework

Dear Sir or Madam:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to offer comments on the proposal by the banking agencies for a new risk-based capital framework (the "Standardized Framework) based on the standardized approach for credit risk and the basic indicator approach for

[1] [1]*The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 20,000 locations nationwide and employing nearly 300,000 Americans, ICBA members hold $1 trillion in assets, $800 billion in deposits, and $700 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

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operational risk described in the capital adequacy framework titled "International Convergence of Capital Measurement and Capital Standards: A Revised Framework" released by the Basel Committee on Banking Supervision. The proposed new Standardized Framework would be available on an optional basis for all domestic banks, bank holding companies, and savings associations that are not "Core Banks." The Core Banks, those large financial institutions with $250 billion or more in consolidated assets or $10 billion or more in on-balance sheet foreign exposures, would be subject to the Basel II Advanced Approaches.

Summary of ICBA's Position

Although ICBA generally supports the Standardized Framework, we still remain very concerned about the implementation of Basel II Advanced Approaches in the United States. The current banking crisis and the failures of our largest investment banks that were subject to Basel II-like, risk-based capital requirements have demonstrated the inadequacies of a capital framework that allows a large financial institution to determine its own minimum capital requirements subject to supervisory review.

ICBA believes that the banking agencies should postpone the Basel II transition period for the Core Banks which is to begin next year and immediately begin a reappraisal of the Basel II Advanced Approaches as well as the idea of implementing a bifurcated capital framework in the United States. The largest financial institutions in the United States that are now considered "too big to fail" need to be subject to a rigorous standard of risk-based capital requirements that are established by the banking agencies. These capital requirements should not determined by the institutions based on internal risk-based formulas that are only reviewed by the agencies. **Furthermore, ICBA remains very concerned about implementing any type of bifurcated risk-based capital framework that may disadvantage community banks from other sized financial institutions**.

ICBA commends the agencies for proposing to allow non-Core Banks the option to opt-in to the Standardized Framework. However, ICBA remains concerned about the complexity of the Standardized Framework and the regulatory burden that would be imposed on community banks that want to opt-in to the new framework. **For this reason, ICBA urges the agencies to allow community banks the flexibility to opt-in to certain sections of the Standardized Framework.** This flexibility to opt-in to certain sections would substantially reduce the regulatory burden of having to track on a community bank's balance sheet sixteen different risk weight categories and comply with the complex rules that apply to each category.

ICBA has a number of recommendations for improving the Standardized Framework including:

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Operational risk. ICBA believes that the proposed Standardized Framework over weights operational risk. Although we like the simplicity of the Basic Indicator Approach (BIA) and would not recommend using a different approach, we recommend that operational risk be based on no more than 10 percent of a bank's positive gross income. Otherwise, we believe few community banks will use the Standardized Framework because the operational risk charge will negate any benefit of using the more risk-sensitive framework. Furthermore, we believe that a lower percentage such as 10 percent would more accurately calculate a community bank's operational risk.

Residential Mortgage Exposures. Although we agree with most of the proposed risk weights for first-lien residential mortgage exposures listed in Table 7 of the proposal, we recommend a 10 percent risk weight category for those residential mortgage loans with loan to value ratios (LTVs) of less than or equal to 30 percent. We also believe that the risk weight should be capped at 100 percent for all first-lien residential mortgage loans with LTVs of 100 percent or less.

However, we believe that it would be too complicated for community banks to have to calculate a separate loan amount and LTV ratio for the unfunded portion of a residential mortgage exposure. Instead, we recommend that the agencies adopt the proposed alternative LTV ratio calculation that would require only the calculation of a single LTV ratio representing a combined funded and unfunded amount when calculating the LTV ratio for a given exposure.

Stand-alone Junior Lien Mortgages. For stand-alone junior mortgages, we also agree with the agencies that a banking organization should use the combined LTV of that loan and all senior loans to determine the appropriate risk weight for the junior lien. However, we disagree with the proposed risk weight designations in proposed Table 8 for these stand-alone junior mortgages. In our opinion, the proposed risk weights for stand-alone junior mortgages should be significantly reduced to accurately reflect the credit risk of these types of loans. We recommend substituting 50 percent for the 75 percent risk weight category, 75 percent for the 100 percent category, and capping the highest risk weight category for these loans at 100 percent instead of at 150 percent.

Regulatory Retail Exposures. We agree with the proposed risk weight of 75 percent for regulatory retail exposures that meet certain criteria including that the exposure is part of a well diversified portfolio and is not an acquisition, development and construction loan. However, we recommend that the aggregate amount of the exposure to a single obligor be raised from $1 million to $2 million. This would cover more of the typical, low-risk, small business loans that community banks make and would minimize the capital differences between the Standardized Framework and the Basel II Advanced Approach for credit risks.

Loans 90 Days or More Past Due. ICBA disagrees with the proposal to assign loans that are 90 days or more past due (or that are in non-accrual status) to a higher than 100 percent risk weight category. We believe that the more appropriate way to deal with the risk involved in these kinds of loans is by providing adequate reserve amounts through the bank's loan loss reserve account. As long as they are adequately reserved for, there is no need to risk weight them higher then 100 percent.

Use of External Credit Ratings. ICBA generally agrees with the concept of using external credit ratings to enhance the risk-sensitivity of the Basel I risk-based capital rules. Using the external credit ratings that are publicly issued by the Nationally Recognized Statistical Rating Organizations (NRSROs) to assign risk weights for securities held by banks is a reasonable approach to assessing the risk exposure of a bank's securities portfolio. Furthermore, the risk-weight categories in Tables 1-6 of the Standardized Framework are an appropriate way to assess a bank securities portfolio

Core Deposit Intangibles. ICBA continues to believe that the agencies should include a revision to the regulatory capital treatment of identifiable, intangible assets. In past comments made during the Basel 1A rulemaking period, we requested that the agencies include, subject to limitations, contractually protected core deposit intangible assets in the calculation of core capital.

Allowing Core Banks to Use the Standardized Framework. To reduce the costs and complexity of Basel II Advanced Approaches, ICBA supports allowing the Core Banks the option of using the Standardized Framework in lieu of the Basel II Advanced Approaches. ICBA believes that the use of the Standardized Framework by the Core Banks would mitigate to some extent, the potential competitive disparity between Core Banks and non-Core Banks.

Background Concerning the Standardized Framework

Adopted in 1989, the current U.S. risk-based capitals rules are based on the "International Convergence of Capital Measurement and Capital Standards" which is known as Basel I. Under the Basel I framework, banking organizations are required to assign balance sheet exposures to one of five categories of credit risk, which carry minimum capital charges ranging from zero to eight percent. Almost all exposures to individuals and companies, other than residential mortgages, are assigned to the standard risk weight category (i.e., the 100 percent risk weight category), limiting the extent to which the Basel I rules recognize risk differentials among different credit exposures.

In response to concerns that Basel I was not sufficiently a broad indicator of risk for many exposures held by the large banking institutions, the Basel Committee on Bank Supervision launched an effort to fundamentally revise Basel I. These efforts culminated in the Committee's release in June 2004 of a revised capital framework known as Basel II. On August 2003, the banking agencies issued an advance notice of proposed rulemaking for the implementation of Basel II in the United States which indicated that Basel II would only apply only to the ten to

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twelve largest U.S. banking organizations that have total assets of $250 billion or more or total on-balance sheet foreign exposure of $10 billion or more. Other institutions would have the opportunity to opt-in to Basel II provided they meet very strict eligibility standards. ICBA commented on the Basel II ANPR and expressed our concerns about the complexity of Basel II and the competitive inequities that would result if Basel II were implemented. ICBA also recommended further changes to Basel I to make that accord more risk-sensitive and address the competitive inequities presented by Basel II. ICBA also recommended allowing non-Core Banks to remain subject to current Basel I rules at their option.

On September 6, 2006, the agencies issued a notice of proposed rulemaking to implement the Basel II Advanced Approaches in the United States. ICBA commented on the proposal and commended the agencies for adopting a three year transitional period to phase in the Advanced Approaches beginning on January 1, 2009 with appropriate capital floors.

ICBA also commended banking agencies for proposing to retain the Tier 1 leverage ratio as part of Basel II and said that the retention of the leverage ratio is essential to maintaining the safety and soundness of our banking system and is a needed complement to the risk-sensitive Basel II framework that is based only on internal bank inputs and risk parameters. ICBA pointed out that capital requirements under Basel II depend heavily on the answers to questions that vary from bank to bank and have no objectively best answer. No matter how refined a risk-based capital framework the regulators come up with, it cannot capture all risks. Accordingly, there will always be a need for minimum capital requirements to ensure adequate minimum capital levels and a base level of capital for safety and soundness in all economic conditions.

ICBA also said that it was very important to our economy that regulators maintain a minimum capital cushion for our largest financial institutions that pose the greatest risks to our financial system. "If a trillion dollar financial institution were to become significantly undercapitalized or fail, the consequences to the Deposit Insurance Fund, the rest of the banking industry, and our economy would be enormous," ICBA warned. "The agencies should never consider putting our entire banking system in jeopardy because a few banks claim that they need lower capital requirements to compete internationally. "

On December 26, 2006, the agencies issued a notice of proposed rulemaking (Basel IA NPR) which proposed modifications to the general risk-based capital rules for banks not required to adopt the Basel II advanced approach. Specifically, the agencies proposed to increase the number of risk-weight categories from five to eight, expand the use of external ratings for assigning risk weights, broaden recognition of collateral and guarantors, use loan-to-value ratios (LTV ratios) to risk weight most residential mortgages, and increase the credit conversion factor for various short-term commitments. ICBA generally supported the Basel IA proposal but recommended additional risk weights for mortgages and small business loans. ICBA strongly supported the right of community banks to have the option to continue using the existing Basel I risk-based capital rules.

In testimony before the House Financial Services Subcommittee on September 14, 2006[2] and in a written statement to the Senate Banking Committee on September 26, 2006[3], ICBA also said that despite the safeguards incorporated into Basel II mentioned above and the efforts by the regulators to revise Basel I, that ICBA remained concerned that Basel II may place community banks at a competitive disadvantage. The Advanced Approaches of Basel II will yield lower capital charges for residential mortgage, retail and small business loans for Basel II adopters, the very credits where community banks compete with large institutions. ICBA also expressed fears that Basel II will further accelerate the consolidation in the banking industry. Lower capital levels that large banks obtain under Basel II will likely result in more acquisitions of community banks by the larger banks seeking to lever capital efficiencies. As more of the larger banks opt-in to Basel II over the long-term, this may eventually threaten the viability of community banking.

ICBA's Comments Regarding the Basel II Process

Although ICBA generally supports the Standardized Framework, we still remain very concerned about the implementation of Basel II Advanced Approaches in the United States. The current banking crisis and the failures of our largest investment banks that were subject to Basel II-like risk-based capital requirements have demonstrated the inadequacies of a capital framework that allows a large financial institution to determine its own minimum capital requirements subject to supervisory review.

ICBA believes that the U.S. banking agencies should postpone the Basel II transition period for the Core Banks which is to begin next year and immediately begin a reappraisal of the Basel II Advanced Approaches as well as the idea of implementing a bifurcated capital framework in the United States. The largest financial institutions in the United States that are now considered "too big to fail" need to be subject to a rigorous set of risk-based capital requirements that are imposed by the banking agencies and that are not determined by the institutions themselves based on internal risk-based formulas. Even with the retention of the capital leverage ratio, minimum risk-based capital requirements for the Core Banks should be as high under the Basel II Advanced Approaches as they would be under the Standardized Approach and/or Basel I. The failures of Bear Stearns and Lehman Brothers have taught us the advantages of regulator imposed, risk-based capital framework that is robust

[2] See testimony of James H. McKillop before the House Subcommittee on Financial Institutions and Consumer Credit dated September 14, 2006.
[3] See ICBA's Statement before the Senate Banking Committee dated September 26, 2006 entitled "Basel Capital Accord Update."

enough to provide a capital cushion for all types of risks including credit, liquidity, reputational, or operational risks.

In previous letters on Basel II, ICBA also has criticized the complexity of the Basel II Advanced Approaches and the risks that regulators would not be able to spot the intentional or unintentional errors or omissions in the formulas that are used. Any minimum capital requirements for credit risk should be simple enough that bank directors can monitor its implementation and auditors can certify to them as part of their internal control audits. **ICBA believes that only a less complex, regulator-imposed, risk-based framework would allow the regulators, the institution, and the institution's directors and auditors to adequately track whether an institution was complying with its capital requirements.**

Furthermore, ICBA remains very concerned about implementing any type of bifurcated risk-based capital framework that may disadvantage community banks from other sized financial institutions. As noted above, the Core Banks which include the largest financial institutions in the United States should be subject to capital standards that are at least as rigorous as those that are imposed on the rest of the industry. Although implementing the Standardized Framework may mitigate to some extent the competitive disparities between the Basel II Advanced Approaches and Basel I, potentially there will always be differences between the two approaches with respect to certain credit exposures that will disadvantage one sized institution over another.

ICBA's General Comments Regarding the Standardized Framework

ICBA generally supports the proposed Standardized Framework. ICBA has long advocated revising Basel I to make it more risk sensitive and to address any competitive issues with using a bifurcated capital system. Just like with Basel IA, the Basel II Standardized Framework would make capital requirements more risk-sensitive than the current Basel I capital rules. This is accomplished in large measure through modification of the risk weighting of various asset classes. The risk weighting process would yield risk-adjusted asset amounts for general credit risk, unsettled transactions, securitization exposures, and equity exposures. Total risk assets would be the sum of these amounts, plus operational risk.

ICBA also commends the agencies for proposing to allow non-Core Banks the option to opt-in to the Standardized Framework. As we stated in our comment letter concerning the Basel IA, many community banks have excess capital and would prefer to remain under Basel I without revision to avoid unnecessary burden. This is particularly true for smaller banks that are management-owned, otherwise closely held, or not publicly traded, or banks in rural or other smaller markets. These banks generally hold higher amounts of capital than regulatory minimums for a variety of reasons including a

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conservative philosophy or lack of ready access to raise capital in the capital markets.

For instance, the average total risk-based capital ratio for banks under $100 million in assets is approximately 25% and for banks between $100 million and $1 billion, the ratio is15-16%.[4] For these banks, computing risk-based capital minimums and ratios using the Standardized Framework could present a significant regulatory burden with no corresponding benefit. These community banks will likely choose not to opt-in to the Standardized Framework.

However, ICBA is also concerned about the complexity of the Standardized Approach and the regulatory burden to comply with the entire framework. For instance, the proposal increases the number of risk weight categories from the current five under Basel I to a total of sixteen to allow for greater risk differentiation across risk exposures. Risk weights would range from zero to 1250%, which makes the proposal much more complex than Basel IA which would have expanded the number of risk weight categories from five to eight and the risk weights from zero to 200%. As noted below, most community banks would find many of the new risk weight categories inapplicable but will still need to adopt a system to track exposures for sixteen different risk weight categories.

For this reason, ICBA urges the agencies to allow community banks (e.g., those institutions with less than $10 billion in consolidated assets) to have the ability to opt in to only certain sections of the Standardized Framework that would most apply to their balance sheet. For instance, some community banks would be interested in opting in to only that part of the Standardized Framework that deals with mortgage exposures, since those exposures would be subject to a more risk-sensitive risk weight system than under the current Basel I framework. This flexibility to opt-in to certain sections of the Standardized Framework would substantially reduce the regulatory burden of having to track on a typical community bank's balance sheet sixteen different risk weight categories and comply with the complex rules that apply to each category. Overall, it would make the Standardized Framework a more attractive option for community banks.

ICBA's Specific Comments about the Standardized Approach

Operational Risk

Unlike Basel IA, the proposed Standardized Framework requires a bank to calculate a charge for operational risk and to determine that charge by using the basic indicator approach (BIA). Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, and systems or from external events. This definition also includes legal risk, which is the risk of loss (including litigation costs, settlements, and regulatory fines) resulting from

[4] See FDIC News Release and Chart 3 of the Memorandum from Christopher J. Spoth to the FDIC Board dated October 6, 2005.

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the failure of the bank to comply with laws, regulations, prudent ethical standards, and contractual obligations in any aspect of the bank's business, but excludes strategic and reputational risks.

Under the proposed BIA, a bank would calculate its risk-based capital requirement based on the average of the previous three years' positive gross income multiplied by 15 percent. A bank would exclude any year that gross income was negative or zero. Gross income would equal a bank's total net interest income plus non-interest income minus income from insurance and reinsurance activities. The capital requirement would be set at the beginning of the calendar year for the subsequent calendar year.

ICBA believes that the proposed Standardized Framework over weights operational risk. Although we like the simplicity of the BIA and would not recommend using a different approach, we recommend that operational risk be based on no more than 10 percent of a bank's positive gross income. Otherwise, we believe few community banks will use the Standardized Framework and instead will continue using Basel I because the operational risk charge will negate any benefit of using the more risk-sensitive Standardized Framework. Furthermore, we believe that a lower percentage such as 10 percent would more accurately calculate a community bank's operational risk. We would like to point out also that some credit should be given for how well a bank manages/mitigates its own operational risk.

Residential Mortgage Exposures

Although we agree with most of the proposed risk weights for first-lien residential mortgage exposures listed in Table 7 of the proposal, we recommend a 10 percent risk weight category for those residential mortgage loans with loan to value ratios (LTVs) of less than or equal to 30 percent. We also believe that the risk weight should be capped at 100 percent for all residential mortgage loans with LTVs of 100 percent or less. Residential loans with LTV ratios of between 91-100 percent are often made by community banks in rural areas where property values are low. These residential mortgage loans seldom result in any measurable loss to the bank and therefore should carry no higher than a 100 percent risk weight.

However, we believe that it would be unnecessarily complicated for community banks to have to calculate a separate loan amount and LTV ratio for the unfunded portion of a residential mortgage exposure. Instead, we recommend that the agencies adopt the proposed alternative LTV ratio calculation that would require only the calculation of a single LTV ratio representing a combined funded and unfunded amount when calculating the LTV ratio for a given exposure. Otherwise the complexity and regulatory burden of using LTVs and risk weighting residential mortgage exposures will outweigh the benefit of making the calculation and will discourage community banks from opting into the Standardized Approach.

We agree with the agencies as to how LTVs are to be calculated. The value of the property should be based on the value at origination and banks should have

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the flexibility to update the values for risk-weight purposes when the borrower refinances the mortgage and extends additional funds. For mortgages that are positively amortizing, banks should also have the flexibility to adjust the LTV quarterly to reflect any decrease in the principal balance. For mortgages that negatively amortize, banks should be required to adjust the LTV quarterly to reflect the increase in principal balance and risk weight the loan based on the updated LTV.

As noted in our comment letter on the Basel IA NPR, while using credit scores in conjunction with LTV ratios might further enhance the risk sensitivity of the mortgage loan risk weights, it would substantially complicate the process of computing risk-based capital. Besides the fact that some banking organizations do not rely heavily on credit scoring, those that use credit scores would have to develop operational methods and software for inputting and tracking the scores and categorizing the loans. Credit scores are also much more volatile than LTV ratios and can be inaccurate; therefore, banking organizations would need to periodically update the scores, check their accuracy and possibly change the risk weight category of a loan. For many community banks, the regulatory burden of including credit scores with LTV ratios would outweigh the benefits.

For stand-alone junior mortgages, we also agree with the agencies that a banking organization should use the combined LTV of that loan and all senior loans to determine the appropriate risk weight for the junior lien. However, we disagree with the proposed risk weight designations in proposed Table 8 for these stand-alone junior mortgages**. In our opinion, the proposed risk weights for stand-alone junior mortgages should be significantly reduced to accurately reflect the credit risk of these types of loans. We recommend substituting 50 percent for the 75 percent risk weight category, 75 percent for the 100 percent category, and capping the highest risk weight category for these loans at 100 percent instead of at 150 percent.** As revised, Table 8 would be as follows: [

Table 8.--- Risk Weights for Junior-Lien Residential Mortgage Exposures

Combined loan-to-value ratios (%)	Risk Weight (%)
60 or less………………………………	50
Greater than 60 and less than or equal to 90	75
Greater than 90…………………………………	100

We believe that proposed Table 8 more accurately reflects the credit risks associated with stand-alone junior mortgages. For instance, the proposal to risk weight stand-alone junior mortgages at 150 percent with LTVs higher than 90 percent assumes that the credit risk for these types of loans is significant, when in reality, these loans do not justify capital greater than 100% of the amount of the loan if they are prudently underwritten. Furthermore, if the goal of Standardized Approach is “to minimize differences in capital requirements between the two accords," ICBA believes that the risk weight categories for stand-alone junior mortgages for the non-Core Banks also needs to be adjusted downward from those proposed to compensate for the potential disparity in treatment that would result between Basel II Advanced Approaches and Standardized Approach.

Regulatory Retail Exposures

We agree with the proposed risk weight of 75 percent for regulatory retail exposures that meet certain criteria including that the exposure is part of a well diversified portfolio and is not an acquisition, development and construction loan. However, we recommend that the aggregate amount of the exposure to a single obligor be raised from $1 million to $2 million. This would cover more of the typical lower-risk small business loans that community banks make and would minimize the capital differences between the Standardized Framework and the Basel II Advanced Approach for Credit Risks

Loans 90 Days or More Past Due

ICBA disagrees with the proposal to assign loans that are 90 days or more past due (or that are in non-accrual status) to a higher than 100 percent risk weight category. We believe that the more appropriate way to deal with the risk involved in these kinds of loans is by providing adequate reserve amounts through the bank's loan loss reserve account. As long as they are adequately reserved for, loans that are 90 days or more past due should not be categorized in a risk-weight category higher than 100 percent. If they are not adequately reserved for, than a bank should be increasing its loan loss reserves (or face the penalty of having inadequate loan loss reserves) and not be concerned about changing risk weights for the underlying loan and increasing its minimum risk based capital requirement.

Use of External Credit Ratings

As noted in our comment letter concerning the Basel IA. ICBA generally agrees with the concept of using external credit ratings to enhance the risk-sensitivity of the Basel I risk-based capital rules. Using the external credit ratings that are publicly issued by the Nationally Recognized Statistical Rating Organizations (NRSROs) to assign risk weights for securities held by banks is a reasonable approach to assessing the risk exposure of a bank's securities portfolio. Furthermore, the risk-weight categories in Tables 1-6 of the Standardized Framework are an appropriate way to assess a bank securities portfolio without imposing undue regulatory burden on community banks.

The agencies acknowledge that expanding the use of external ratings will have little effect on the risk-based capital requirements for existing loan portfolios at most banking organizations. For a great majority of community banks that invest most of their securities portfolio in either U.S.government or municipal securities, using external credit ratings to assess the risk exposure of their bank securities portfolio will not have much impact on their overall risk based capital ratios. However, ICBA believes that as long as the approach is not overly complicated, that over time, community banks will find that a more risk sensitive assessment of their securities portfolio to be beneficial. Although ICBA is concerned about the accuracy of credit ratings, we believe that regulatory and legislative steps will be taken to strengthen the accuracy of the ratings.

Core Deposit Intangible Assets

ICBA continues to believe that the agencies should include a revision to the regulatory capital treatment of identifiable, intangible assets. In past comments made during the "Basel 1A" rulemaking period, we requested that the agencies include, subject to limitations, contractually protected core deposit intangible assets ("CDI") in the calculation of core capital. The reasons why we felt such a revision was justified then still apply today.

1. The structure of the contractual protection provided in such arrangements meets the six requirements of a guarantee for credit exposure under the rules.
2. The inclusion of contractually protected CDI would align the allocation of capital with risk exposures within the identifiable intangible asset category.
3. Disparate treatment of CDI versus other identifiable intangible assets such as purchased mortgage servicing rights ("PMSRs") may unfairly disadvantage general banks.

The central role that stable core deposit funding has played in insulating most FDIC-insured institutions from the worst consequences of the current financial crisis presents an entirely new and compelling reason to include contractually protected CDI in core capital. Currently, the complete deduction of CDI from core capital works as a powerful disincentive against core deposit funding dependence. The deduction of CDI, combined with the current inclusion of other identifiable intangible assets related to consumer lending (such as PMSRs), has created a regulatory capital standard that drives financial institutions away from core funding and toward the types of consumer lending that triggered the current crisis in the first place. A realignment of CDI's capital charge will reward institutions that generate and/or acquire core deposit funding, thus minimizing the likelihood of future bank failures triggered by liquidity risk exposures.

Allowing Core Banks to Use the Standardized Approach

As noted above, ICBA continues to have serious concerns about the competitive effects of Basel II even if the Standardized Framework is implemented. To reduce the costs and complexity of Basel II Advanced Approaches, to enhance their flexibility, and mitigate competitive disparities between the Core and non-Core Banks, ICBA supports allowing Core Banks the option of using the Standardized Framework in lieu of the Basel II Advanced Approaches. ICBA believes that the use of the

Standardized Framework by the Core Banks would reduce the impact on risk-based capital by those banks and would mitigate to some extent, the competitive disparity between the two frameworks.

Conclusion

Although ICBA generally supports the Standardized Framework, we still remain very concerned about the implementation of Basel II Advanced Approaches in the United States. ICBA believes that the banking agencies should postpone the Basel II transition period for the Core Banks which is to begin January 1st of next year and immediately begin a reappraisal of the Basel II Advanced Approaches as well as the idea of implementing a bifurcated capital framework in the United States. The largest financial institutions in the United States that are now considered "too big to fail" need to be subject to a rigorous set of risk-based capital requirements that are at least as rigorous as those that would be imposed by Basel I and/or the Standardized Approach. These capital requirements should be set by the banking agencies and not determined by the institutions themselves based on internal risk-based formulas.

ICBA commends the agencies for proposing to allow non-Core Banks the option to opt-in to the Standardized Framework. However, ICBA remains concerned about the complexity of the Standardized Framework and the regulatory burden to comply with the entire framework**.** For this reason, ICBA urges the agencies to allow community banks the flexibility to opt-in to certain sections of the Standardized Framework. This flexibility would substantially reduce the regulatory burden of having to track on a typical community bank's balance sheet sixteen different risk weight categories and comply with the complex rules that apply to each category.

ICBA noted above a number of recommendations for improving the Standardized Framework including: (1) reducing the operational risk charge from 15 percent to 10 percent of a bank's positive gross income, (2) capping risk weights for first-lien residential mortgage exposures at 100 percent, (3) reducing risk weights for junior lien mortgages, (4) increasing the cap for regulatory retail exposures from $1 million to $2 million, and (5) capping the risk weight for loans 90 days or more past due at 100 percent. To reduce the costs and complexity of Basel II Advanced Approaches, to enhance its flexibility, and mitigate the competitive disparities between those banks using the Advanced Approaches and the rest of the industry, ICBA supports allowing the Core Banks the option of using the Standardized Framework in lieu of the Basel II Advanced Approaches.

ICBA appreciates the opportunity to comment on the proposed Standardized Framework. If you have any questions about our letter, please do not hesitate to call me at 202-659-8111 or at Chris.Cole@icba.org.

Sincerely,

Christopher Cole
Vice President and
Senior Regulatory Counsel