

From: Northland Financial, Greg Schwab
Proposal: 1442 (RIN 7100-AD 87) Regs H, Q, & Y Regulatory Capital Rules
Subject: Regs H & Y Regulatory Capital Proposals

Comments:

On behalf of Northland Financial, I am writing to express our very strong concerns and opposition to the pending Basel III bank capital proposals as they would relate to our small community bank.

Many of our concerns relate to the difficulty of monitoring and measuring the various balance sheet components that are proposed to be factored into the risk based capital standards. Implementing a system to monitor loan to value ratios in our residential mortgage lending operations would add a burdensome regulatory element to this function and the proposed risk weighting assignments will almost certainly require us to maintain additional capital against what has long been a very stable source of business for our bank. Further, the assumption that second position residential real estate mortgages are inherently risky (to the point that a related first position mortgage in our bank might also become subject to a higher risk rating) appears to be fundamentally flawed. Coupled with the burdensome consumer protection rules already in place, which make it very difficult for our bank to even offer residential real estate loans to many of our customers, any regulatory effort which would make this process even more difficult in terms of capital requirements will almost certainly result in less consumer credit being made available to our customers and to the customers of banks like ours across the country.

Our bank is also concerned about the proposal to increase the risk weighting for past due loans. Since the accounting rules for delinquent loans and the calculation of the Allowance for Loan Loss have been well established by regulators over the years, the additional burden of allocating capital over and above what is already provided for in the provision and allowance of the bank seems redundant and punitive.

The proposal to include changes in the unrealized gains and losses of our bank's investment portfolio also appears to be ill advised and potentially punitive. Even ignoring the current low level of interest rates (which all but guarantee that banks will lose most of their unrealized portfolio gains as rates rise), the notion that only a slice of a bank balance sheet should be marked to market is flawed. As interest rates change, the values of loans and related funding change too. In theory, a bank with limited interest rate sensitivity should not be subjected to volatile swings in capital just because the market value of the investment portfolio changes.

Finally, we are opposed to any effort to disallow or otherwise force the sun-setting of Trust Preferred funds which have been made a part of our bank capital through the holding company. Whether the very small number of owners of our holding company (which owns 100% of our bank) borrow money to invest in the bank or use their own personal wealth from other sources, the fact is that the bank enjoys the benefit of that equity investment. To preclude Trust Preferred funding while still allowing shareholders to otherwise borrow against the value of holding company stock through traditional stock loans seems arbitrary and ineffective.

Northland Financial is a \$185,000,000 bank headquartered in rural North

Dakota. We have been in business for eighty years and our management team is seasoned and knowledgeable. Applying international and one size fits all accounting rules to our institution will provide little or no benefit to the national banking system, our bank, or to our customers. In the event that the momentum to implement the capital standards proposed by Basel III cannot be stopped, we hope that consideration will at least be given to exempting community banks and small holding companies like ours from the onerous and potentially damaging provisions of the proposal.

Thank you for your consideration of our concerns. Questions regarding this comment letter should be directed to me. I will be very happy to help you in whatever way I can.

Regards,

Greg Schwab
Northland Financial