PACIFIC COAST BANKERS' BANCSHARES

September 28, 2012

Mr. Wayne Byres
Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Mr. David Wright
International Organization of Securities Commissions
C/ Oquendo 12
28006 Madrid
Spain

Mr. John Walsh
Acting Comptroller
Office of the Comptroller of the Currency
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Washington, DC 20219

Mr. Alfred M. Pollard
General Counsel, Attention Comments
Federal Housing Finance Agency, 4th Floor
1700 G Street, NW
Washington, DC 20552

Mr. Robert Freirson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Mr. Gary K. Van Meter
Acting Director
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090

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

Mr. David A.Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, NW
Washington, DC 20581

Via Electronic Submission

RE: Margin requirements for non-centrally-cleared swaps

Pacific Coast Bankers' Bancshares (PCBB) appreciates the opportunity to provide comments on margin requirements for non-centrally-cleared derivatives pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (DFA) and the consultative document by the Basel Committee on Banking Supervision and the Board of the International Organization of Securities Commissions.

Community banks are critical to small businesses and consumers.

PCBB provides correspondent banking services to over 500 community banks and savings associations (together community banks) throughout the United States[1]. We offer a range of services to our community bank clients which help them address their risk management, liquidity and operational needs. In total, our community bank clients lend billions of dollars – largely to small businesses and consumers.

Community banks are also the key provider of financial services to small businesses and thereby serve a critical role in the economy. Indeed, the regulatory burdens that impact community banks directly affect the small businesses that they serve. Our comments are intended to provide a small financial institution's perspective in an effort to support final rules that protect the interests of all market participants.

The two primary goals of margin requirements for non-centrally-cleared derivatives (the promotion of central clearing and the reduction of systemic risk) are not advanced by requiring small financial institutions to post initial margin for swap trades.

In the promotion of central clearing, first small financial institutions are exempt from mandatory clearing under DFA. Second, small financial institutions are engaged in only limited swap activities and, therefore, cannot find cost-effective ways to clear derivatives regardless of any margin incentives. Third, currently, and in the near future, central counterparty clearing houses (CCPs) are not expected to easily accommodate small financial institution's swap trades. In the reduction of systemic risk, small financial institutions did not contribute to systemic risk in the last financial crises and their swap activities are too limited to contribute to systemic risk in the future.

Risk to swap dealers if margin requirement for small financial institutions is similar to nonfinancial end-user.

We believe that a dealer engaging in swap trades with a small financial institution should collect margin as established under that dealer's credit assessment processes and procedures. In the current bilateral trading environment, some dealers collect variation margin from small financial institutions. Dealers also collect initial margin when the risk profile or trading activity of the small financial institution warrant such margin.

Small financial institutions are end-users of swaps and do not pose systemic risk nor credit risk to swap dealers. Small financial institutions pose lower-risk in their swap trades and should be treated by dealers as nonfinancial end users for purposes of the margin requirements.

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[1] All of PCBB's clients would be considered a "small financial institution"; which is to say that these clients have total assets less than $10 billion and are not subject to mandatory clearing of swaps.

Increased systemic risk in the financial system if margin requirement for small financial institutions is not similar to nonfinancial end-user.

Individually, small financial institutions are not systemically-important non-financial entities. Imposing initial margin on these institutions will result in high cost with no discernable benefit to the financial system. Small financial institutions will be particularly disadvantaged against their larger financial institution competitors if initial margin requirements are imposed. Unlike small financial institutions, larger financial institutions, especially dealers, do not need to offset swaps that are used to hedge transactions with nonfinancial end user, because larger financial institutions, especially dealers, have the ability to manage a matched book of offsetting swaps on their own balance sheet without the use of CPPs or futures exchanges. Larger financial institutions and especially dealers will realize a cost advantage because of lower margin costs versus smaller financial institutions. This would most likely result in fewer loans being made to small business and consumer clients by small financial institutions, and/or increase in the concentration of such loans in a small number of larger financial institutions – an outcome that could have the unintended consequence of increasing systemic risk in the financial system.

If small financial institutions are required to post initial margin for uncleared swaps the cost and complexity of doing business for these institutions will increase. This could lead them to take additional risk, remain mis-matched in funding and lending activities, or not offer small business clients loans due to an unbalanced interest rate structure. We believe that this greater cost and complexity will jeopardize small financial institutions' effectiveness in providing banking services and in particular, prudently structure many types of loans to their small business and consumer clients. It will also leave them at a competitive disadvantage relative to larger financial institutions.

Conclusion

We believe that appropriate margining requirements should be in place for all non-centrally-cleared swaps, however, margin requirements should be varied based on the type of swap and the nature of the market participant. Small financial institutions, which are prudentially regulated entities that are subject to minimum regulatory capital requirements, and that enter into interest rate swaps for non-speculative purposes are well equipped to manage risks of non-centrally-cleared derivatives without the imposition of additional margin requirements.

We urge the Basel Committee, the Board of the International Organization of Securities Commissions, CFTC and the Agencies to treat small financial institutions using derivatives to hedge their risks in the same manner as nonfinancial end users for purposes of the margin requirements. If small financial institutions are required to pledge additional initial collateral to support their lending activities (i.e., if initial margin requirements are imposed on swaps entered into by small financial institutions), then small businesses and consumers that rely so heavily on community banks in their own locality will have fewer options for borrowing.

We believe that our recommendations serve to further the intent of DFA, and will help small financial institutions uphold the safety and soundness of the financial system and increase small business job creation and overall economic activity.

We thank the Basel Committee, Board of the International Organization of Securities Commissions, CFTC and the Agencies for their willingness to consider our suggestions and views.

Yours Truly,

Steve Brown
President & Chief Executive Officer
Pacific Coast Bankers' Bancshares