Meeting between Governor Duke and
Representatives of Arvest Bank Group, Inc.
June 27, 2013

Participants: Governor Elizabeth A. Duke, Thomas Boemio, and Mark Buresh (Federal Reserve Board)

Robert Kelly, William G. Roehrenbeck, and R. Scott Grigsby (Arvest Bank Group, Inc.); Edward Yingling (Covington & Burling LLP, counsel for Arvest Bank Group, Inc.)

Summary: Representatives of Arvest Bank Group, Inc. (the "Representatives") met with Governor Duke and Federal Reserve Board staff to discuss the proposed interagency capital rules, particularly the proposed treatment of mortgage servicing assets under the proposed rules and possible alternatives to this treatment. The Representatives focused on topics raised in a letter submitted in advance. A copy of this letter is attached.

Attachment

To: Governor Elizabeth Duke, Board of Governors, Federal Reserve System

From: J. Robert Kelly, Arvest Bank (Fayetteville, Arkansas)

Re: Basel III Proposed Capital Rule – Mortgage Servicing Assets ("MSAs")

Date: June 24, 2013

Thank you for agreeing to meet with us this week on a matter of great importance to Arvest and a number of other mid-size and community banks. In addition to providing you with information that hopefully may be helpful in your deliberations, we are hopeful we might obtain more information about that part of your proposal on bank regulatory capital which would impose new, much higher capital requirements on mortgage servicing assets ("MSAs"). It is our understanding that these proposed requirements were taken directly from the international Basel III agreement with little or no change. While we support strong capital requirements for banks, we note that, as the Federal Reserve Board itself has indicated,[1] these new requirements can affect the cost and availability of mortgages. Unfortunately, the proposal put forth by the regulators contained no analysis or rationale for the dramatic increase in capital requirements for MSAs.

As you know, the proposal on MSAs was part of the extensive international negotiations that led to Basel III. Apparently the MSA provisions of Basel III were a result of the negotiations over capital that should be applied to intangible assets. The proposal on MSAs reportedly was put forth by the European participants and accepted with minor adjustments by the U.S. participants. It is noteworthy that the European housing finance system is very different from that in the U.S., and there is no such thing in Europe as a market for mortgage servicing

[1] January 4, 2012, letter from Chairman Bernanke to Chairman Spencer Bacchus and Ranking Member Barney Frank of the House Financial Services Committee.

rights. It is also noteworthy that Basel III was intended to be applied to large international banks, but our regulators are proposing to apply the new MSA rules, and other capital rules, to all U.S. banks. Thus we have our regulators proposing to apply to all U.S. banks a rule proposed by foreign regulators, which would have no practical impact on foreign banks and which was intended to apply only to large international banks.

A March 25, 2013, letter on Basel III from a broad coalition of business, housing, and community groups stated:

> The new rules on mortgage servicing rights would drive banks to reduce their servicing portfolios or cease servicing mortgage loans. The transition could cause a significant disruption to the financial markets in the U.S. as hundreds of billions of dollars of servicing are moved without any assurance that there is sufficient capacity from non-bank servicers.

Our experience is that non-bank buyers of mortgage servicing rights are already becoming the primary bidders on MSAs when we offer MSAs for sale.

Because the regulators have provided no public analysis of the reasons behind the proposals on MSAs, the following are questions that we ask ourselves and which it would be helpful to discuss:

1. Why is this proposal on MSAs being extended to small and mid-size banks?
2. Given that the mortgage servicing is a scale business, it appears that the proposal, which greatly increases the capital requirements as MSAs grow as a percentage of Tier 1 Capital, could as a practical matter force community and mid-size banks to withdraw entirely from the servicing business, greatly increasing the concentration in the largest servicers. What analysis has been done on the impact of the proposal on the ability of small and mid-size banks to compete in this business?

3. Given the well-known issues the large mortgage servicing companies have faced, what is the impact on consumers if small and mid-size banks exit the business?
4. The argument presented for increased capital requirements relating to intangible assets centers on the concern that such assets may not be liquid in troubled times, and yet MSAs appear to have had an active market for sale during the financial crisis. We will provide you with information about the market for MSAs, in which we are quite active, and we hope you could share with us any analysis the regulators may have undertaken. We believe there may be a misunderstanding about the liquidity of the MSA market.
5. It is notable that the proposed capital requirement for MSAs greatly exceeds that for commercial real estate loans. Yet we are not aware that any bank had serious financial problems during the financial crisis as a result of holding MSAs, while many banks failed due to commercial real estate lending. Is there any analysis of the regulators of the riskiness of MSAs compared to other assets? We have some ideas as to how concerns about MSAs can be ameliorated with proper regulatory safeguards.

We appreciate your willingness to discuss this matter, which is important to a number of midsize and community banks, with us.

June 24, 2013