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October 22, 2012

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W. Washington, D.C.
20551
Delivered via email: regs.comments@federalreserve.gov

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, DC 20219
Delivered via email: regs.comments@occ.treas.gov

Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation,
550 17th Street, N.W.
Washington, D.C. 20429
Delivered via email: comments@FDIC.gov

Re: Basel III Capital Proposals

Ladies and Gentlemen:

Thank you for the opportunity to provide comment on the Basel III proposals[1] that were recently approved by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (collectively the "banking agencies").

We are the President and Chairman of Northwest Financial Corp. ($1.51 billion bank holding company headquartered in Arnolds Park, IA) and its three bank subsidiaries – Northwest Bank ($1.03 billion based in Spencer, IA) First National Bank in Sioux Center ($270 million) and The First National Bank in Creston ($210 million). We are committed to helping our communities prosper and meet the challenges of an increasingly complex world. We are committed to providing our customers with high value community banking services and products and also committed to providing our employees with quality jobs, education and opportunities to prosper.

We understand the goal behind Basel III and strengthening the country's financial system by increasing the level of capital that banks are required to hold. However, those rules are more appropriate for large, complex and internationally focused financial institutions, not for community banks. . As a community bank we remain local and provide service to our customers that we know and can prudently underwrite. We didn't participate in the housing bubble that enveloped the east and west coasts and the sand states – our values remained stable and we practiced safe and sound banking with people and markets that we know best.

[1] The proposals are titled: *Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, and Transition Provisions*; *Regulatory Capital Rules: Standardized Approach for Risk-weighted Assets; Market Discipline and Disclosure Requirements; and Regulatory Capital Rules: Advanced Approaches Risk-based Capital Rules; Market Risk Capital Rule.*

Areas of the Basel III rules that we have the most concern with:

- **Requirement that gains and losses on available for sale (AFS) securities flow through to regulatory capital.** Fair value sensitivity testing encompasses all types of assets and both sides of the balance sheet, not just the AFS security portfolio. Current market rates are near historical lows, and if the AFS security portfolio is included capital ratios will become more volatile. Rate shocks are not being performed at 100 or 200 basis points anymore but 300 or 400 basis points due to the current environment. If rates are shocked +300 basis points, the impact to the AFS portfolio is just over $5 million. Such a move will reduce tier 1 leverage ratio by 36 basis points. But more importantly, the ability to make $48 million of loans within our communities is lost. An alternative to this impact will be to move securities to the held to maturity classification which then reduces the AFS portfolio as a potential source of liquidity.

- **Increased risk weightings for residential first mortgages and home equity loans.** As a community banks we practiced prudent underwriting criteria with the customers we know from our markets. During 2008-2011 we experienced first mortgage losses of 36 bp and home equity losses of 59 bp which are used in the establishment of our allowance for future loan losses and already funded from current capital levels. If current risk weightings are increased from 50% and 100% to a range of 35-100% and 100-200%, we estimate that such a move will reduce the total risk based capital ratio by 43 basis points and impair our ability to make $42 million of loans within our communities. Current mortgages were originated and priced under the prior regulations. Instead of penalizing the bank and raising the cost of capital when the rates can't be adjusted, wouldn't a better practice be to grandfather in existing first and second mortgages? That would also apply to loans that could be 10-20 years old and would avoid the unproductive need to update loan systems for prior loans and determine the LTV at the point the loans were originally underwritten. Banks can adjust their lending practices going forward to avoid the punitive risk weights; they cannot do so with respect to mortgage loans already made. Also for interest rate risk practices many banks might balloon the loan in five or seven years instead of making it a full amortizing loan over 15, 20, or 30 years. As currently written, banks can choose a lower risk weight at the expense of taking on higher interest rate risks in lieu. In addition as current market rates are near historical lows, many first mortgage customers will keep the current first mortgage rates in place for the next 15-30 years and choose to fund any future loans as a home equity as they continue to pay down the first mortgage. The current proposal is harsh as it will then require us to also categorize the first mortgage as a category two loan and increase the risk weighting from the proposed 35-50% to 100-150% further reducing capital ratios and restricting the ability to make loans right at the time when we need the economic growth from the housing industry not further restrictions. In addition, since the ALLL has already been funded, the increase of risk weightings serves as a double negative on capital if the 1.25% limit on ALLL as a tier 2 capital item is not removed.

Current Basel III proposals will continue to add to more complexity for community banks. And at times goes in the opposite direction of good liquidity and interest rate risk planning. If more and more attention continues to be given to compliance activities and burden and Basel III is implemented to align capital requirements with European banks, the community bank sector will consolidate at an accelerating rate. This will have a very negative impact on main street communities throughout the United States.

Please reconsider the final proposed rule. Basel rules were not designed for banks that aren't international in their business approach. Don't implement something that will harm banks in the United States from serving their customers and communities and put additional strain on an economy that is already struggling to recover.

Thank you for your support.

Sincerel ,

Dwight K Conover

Dwight K. Conover
Chairman

Jeff Plagge

Jeff Plagge
President & CEO

c.c. Congressman Steve King
c.c. Senator Tom Harkin
c.c. Senator Charles Grassley