



# FIRST SECURITY BANK



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

September 19, 2012

Subject: Basel III FDIC RIN 3064-AD95, RIN 3064-AD96, and RIN 3064-D97

Thanks for the opportunity to address this issue. Having spent my entire working career of 48 years in the banking industry, I feel compelled to comment on the negative impact Basel III will have on community banks. I am very proud of the role our bank has continuously had in the economic development of our community and surrounding demographic areas. Thanks for your consideration.

There is a Notice of Proposed Rulemaking distributed by the OCC, Fed, and FDIC incorporating the latest Basel III capital framework and to implement the provisions of the Dodd Frank Wall Street Reform and Recovery Act. Here is a short outline explaining the provisions and how it will affect the banking world.

- I. Accumulated Other Comprehensive Income as a component of Tier 1 capital
  - a. This would cause all of our mark to market entries to flow through to common tier one equity. This would cause large swings in our tier one capital that would not be reflective of what actually is happening. Especially in a bank like ours where most of these unrealized losses will never be recognized.
    - i. Would force us to calculate alternative ratios to determine our real capital position.
    - ii. We would hold more securities as HTM, which would greatly reduce our ability to adjust our portfolio for liquidity and funds management. Different institutions could treat identical securities differently, causing different capital treatments for the same risk.
    - iii. We would be more inclined to make shorter term investments as to reduce volatility. While this would increase liquidity, it would greatly impair our ability to produce a profit and generate capital. We would be looking for other ways to generate revenue, which could be higher risk.
    - iv. Not all asset classes would be treated equally. We would only be marking one set of assets to market. First this violates the basic accounting principle of consistency. Secondly it hinders the ALM process as it adds a penalty for using the securities portfolio, which is the most flexible tool in the ALCO toolbox.
- II. Minimum Capital Ratios, Capital Conservation Buffer, and Prompt Corrective Action Requirements
  - a. Introduction of a new common equity Tier 1 capital ratio and a modification of the capital components and ratios for the existing risk-based and leverage capital framework. They are also proposing limits on capital distribution and certain discretionary bonus payments in the bank does not hold a "Capital Conservation



# FIRST SECURITY BANK



Buffer” 2.5% above the minimum threshold for adequately capitalized. In order to be well capitalized, an institution needs to be 2% above the adequately capitalized threshold. Adding another ½% to avoid dividend and bonus restrictions does not make sense.

### III. Residential Mortgage Exposures

- a. This provision would cause us to change the risk weighting on a loan by loan basis based on mortgage type (traditional vs nontraditional) and lien position. Within each of those categories, risk weights would be assigned based on LTV.
  - i. There needs to be a carve out for prudently underwritten loans. Nearly every residential real estate loan we make is prudently underwritten. This simple provision would cut down our work load dramatically.

### IV. Past Due Exposure

- a. This provision says any loan that is 90 days + past due or on nonaccrual that is not guaranteed or not secured, needs to be risk weighted at 150%.
  - i. This doesn't make any sense for us because we deal with loans like this on our ALLL, which is limited to 1.25% of risk weighted assets. In reality, this isn't a big issue for us and we do not have many, if any, unsecured deals this far past due.

### V. Securitization Exposure

- a. No longer would we be able to assign risk weightings based on credit ratings. We would be forced to calculate the risk weighting based on a supervisory formula or a gross-up approach. This initially would cause some labor hours as we would have to complete this calculation for each security we own. Also, these calculations do not give any credit for structural features including purchase price or carrying value of a security. In our case, the discount we own these at is providing us a nice buffer against book losses. It is also interesting when the examiners come in; they nearly all base their classifications on credit ratings.

Regards,

Marlys Boone  
First Security Bank-Sleepy Eye, Benson  
Assistant Cashier / Loan Officer  
PO Box 287  
215 13<sup>th</sup> St S  
Benson, MN 56215  
(320) 843-4411