Mauch Chunk Trust Company

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October 19, 2012

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, DC 20219

Robert E. Feldman
Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation,
550 17th Street, N.W.
Washington, D.C. 20429

Re: Basel III Capital Proposals

Ladies and Gentlemen:

Thank you for the opportunity to provide comment on the Basel III proposals 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").

Mauch Chunk Trust Company is a $310 million independent, locally owned financial provider serving our community since 1902. Our strategic plan has always been servicing customers while assuring the long-term strength of our organization and compliance with all applicable laws and regulations. Currently, our bank has more than 9 percent Tier 1 leverage Capital, more than 16 percent Tier 1 Risk Based Capital, and more than 17 percent Total Risk Based Capital. As a result of the recent financial crisis our risk management focus has been to increase capital well above minimum required ratios while also increasing our loan loss reserves to total loans in excess of 2 percent of total loans.

The first major area of concern in the proposed Basel III pronouncements is the inclusion of accumulated comprehensive income (loss) in common equity Tier 1 Capital computation. Mauch Chunk Trust Company has a $153 million bond portfolio representing 49 percent of assets, currently all held in available for sale with approximately $5 million in unrealized gains. In a "up 300 basis point shock" simulation, assuming discounted cash flows, this would equate to a 12 percent loss or $19 million unrealized loss which translates into an almost a $13 million negative impact on capital. In this scenario, the years where the capital conservation buffer restrictions are enacted, our ability to pay a bank dividend to shareholders could potentially be eliminated. During periods of rising interest rates or deteriorating credit quality market fluctuations will introduce substantial volatility in the management of our bank's capital position. Alternative management measures would have to be taken, such as consideration of shortening the duration of bond portfolios to avoid market changes or be forced to reclassify the portfolio as held to maturity. In either case, this limits the bank's ability to manage overall liquidity, earnings and the interest rate risk position. The new capital proposal ignores current regulatory guidelines established to manage a bank's overall risk position.

Second, an area of concern is the proposed rules that would increased risk weighting for residential mortgages. Our bank follows strict lending underwriting standards of mortgage portfolio loans. This is supported historically by minimal charge-offs in this category. Why should the risk weighting of residential mortgages be higher than other loan types that are considered to be much more risky and with higher historical charge-offs? The risk to a community bank to portfolio a conforming residential mortgage is nominal and was not a factor in the recent financial crisis. Therefore, I question the implementation of the proposal. If these risk weightings are imposed community banks will incur additional administrative burdens to interpret and monitor the new requirements.

Third is the issue relating to the proposed requirement to hold capital for credit enhancing representations and warranties on 1-4 family residential home loans which have been sold into the secondary market not related to the mortgage servicing asset issue. Mauch Chunk Trust Company made the strategic decision to sell mortgages on the secondary market and retain serving rights. By maintaining the service rights we also incur some additional risk in the event of default. This management decision was made to help mitigate our interest rate risk position while continuing to provide local service for our customers. To include these sold loans with treatment similar to on-balance sheet residential mortgage loans in the same way would decrease our capital position. Currently these loans are off-balance sheet with no associated risk weighting. If required to include sold loans with serving rights our capital position could be decreased below the position to be considered "well capitalized". Historical default rates on our mortgage servicing portfolio are minimal. The risk we are taking should be commensurate with the amount of capital we are required to maintain.

Fourth, is the proposal addressing increased risk weights on delinquent loans in which I consider a duplication of capital for it is already included in the reserve for ALLL. Community banks are managing credit risk by completing impairment analyses for all loan classifications. The loan assessment in this process should determine whether or not to increase or decrease the loans risk weighting. This monitoring process along with periodic regulator assessment addresses the issues of credit risk exposure to banks. If included, this could also hinder our ability work with customer repayment options in the future.

The fundamental question remains, do the proposed capital rules decrease the likely hood of future community bank failures or is this an exercise to apply increased complex rules that could put the future of community banking in jeopardy?

The capital requirements as proposed under Basel III will not help prevent another financial crisis but hinders community banks in their ability to manage credit risk, liquidity risk and earnings at risk.

I believe that minimum capital requirements could be adjusted, however, not as proposed by the federal banking regulators as it does not protect community banks. The new capital proposals, if enacted, will be a detriment to small business loans, mortgage lending, and consumer loans. This will affect the communities our bank serves and will affect our local economy.

Respectfully submitted,

Patrick H Reilly

Patrick H. Reilly
President & CEO
Mauch Chunk Trust Company