September 25, 2012

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

Dear Mr. Feldman:

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").

This is sent to you from a thirty five year career, small town banker, in central Nebraska. I have worked for the same commercial bank for the past thirty plus years and was weaned on the Ag crisis of the 1980's. This is a $118 million family-owned bank that has helped this area grow in the consumer, 1-4 family real estate, commercial and agricultural areas for nearly 115 years. I manage a loan department of 6 lenders and 3+ support clerks in a bank that has just less than 30 employees. Our capital is presently at 12.6% Tier1.

I respectfully submit this letter knowing it is the full intent of the regulators to try to bring the U.S. standards more in line with international accounting. Also, having the understanding that, as it states in the register, "Most small state member banks already hold capital in excess of the proposed minimum risk-based regulatory ratios. Therefore, the proposed requirements are not expected to significantly impact the capital structure of most covered small state member banks." In my opinion this is true only on a short term basis.

<u>Issue of Concern:</u> Requiring Unrealized Gains and Losses Flowing Through Capital
The Basel III NPR proposes that the Available –For –Sale (AFS) securities "flow through" to common equity Tier 1(CET1). Presently that is not the case. This change becomes a concern for me for the following reasons.

In looking back at both the 1980's and the housing crisis we now face, it is a historical fact that time heals. Once the poor lending facilities are stopped and the pressure is off, the economy will come back to equilibrium and move forward. In the 1980's regulation and pressure from exams would not allow our judgment or common sense to be considered, but required immediate action

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[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.*

to fix the problem (i.e. Low asset values.). I don't espouse to every calamity getting better without a "fix", but after the source problem is stopped the improvement begins.

Similarly, in the housing collapse, once new loans could no longer be improperly made and sold into the secondary market the situation began to start improving. In both cases the borrowers, who could cash flow their obligations did, and being upside down on the balance sheet for 6 months to 3 years was of little consequence. The problem in both cases was too much debt to value followed by good lenders being restrained.

There is a strange possible similarity to these events if this proposal is pressed on banks during a time when rates could rise rapidly. Today our bank has a good equity position and we have managed our investments in a way that will allow us to meet the lending obligations and not lose money holding excess liquidity. We have a gain in that portfolio today that would, under this proposal, allow for an increase in our lending limit by about $100,000. If rates were to increase by 400 basis points in a short time, with this proposal our lending limit could drop as much as $500,000 during the rise, considering all other things being equal. This move would make the bank's capital look worse when nothing happened but a rate change, and yet it would restrain the bank's options.

Additionally, we are fortunate today to have 12.6% capital. If we were to assume a 10% capital, and this proposal were law, in an upward rate move our (CET1) capital would be lowered by approximately $4 million, due to the disappearance of the AFS premium on investments and loans in the portfolio. The result would then be our capital nearer to 6% and we could have some loans over the legal lending limit. Should the borrowers struggle to make payments due to the increase in rates we could have more risk rated, past due loans that could again add more strain to our capital. All of this while we are trying to fund a reserve, probably being encouraged by examiners that are concerned, due to higher classified assets to total capital.

At that point in time crisis management would be in high gear again! Good lenders and bankers need more flexibility not less in a troubled time. I am against marking to market a securities portfolio that was acquired to hedge against problems, and then becomes the problem because of the hard and fast rules as are being proposed. It is hard to" have your cake and eat it too". Under this scenario we either manage the portfolio for funding needs and risk bad times, or manage the portfolio for capital needs and don't make as many loans. In a small town it is easier to shrink the loan portfolio than to add capital when earnings are gone. It would hurry the closing of lower capitalized banks under these circumstances.

Managing the investment portfolio with the volatility this proposal would inject, would in my opinion, in most cases, shorten the maturities, which adds volatility to the above scenario that is unintended by the regulation. None of the above in my opinion stabilizes the economy by helping banks stay safe and sound. It would force banks into trouble at the same time the general economy is getting in trouble. Additionally, I see nothing positive towards bringing us out of the recession we have recently faced.

I cannot spend the time required to analyze the results of reasonable growth concerning these matters, but it appears to me we could not earn money quick enough to cover an increase in our

totals of say $5 million per year. This growth is possible if not probable without being a high growth organization. This proposal hamstrings the possibilities of natural growth and support for our community. Capital is best acquired through earnings and this proposal would lower small bank earnings in all my possible scenarios.

Issue of Concern: Deduction of Mortgage Servicing Assets that Exceed 10% of an Institution's Common Equity Tier 1

At this time this issue would not affect our institution. However, we have considered keeping the servicing rights on our 1-4 family home loans. This singular item in will prevent small banks from servicing these loans and will move all servicing upstream to either large banks or a provider strongly relying on the secondary market purchasers. This takes away a possible income producer from small organizations. Housing regulations are already causing small town bankers who had no part in the housing crisis to consider not lending for 1-4 family dwellings. Communities do not even maintain, without homes being bought and sold. I feel that this is a second indication of the unintended consequences that will result in this regulation; one more step to shutting down the small bank lending in this country. If this continues commerce will slow and population will continue to drop in the less populated central part of the United States.

I realize there is a phase in period in this regulation. My comments develop around the extreme intent of the regulation. I apologize for my overreaction but I have a job that requires my time daily, and leaves little time to read and digest the complexities of this complicated regulation.

As this letter indicates, I am no politician and less of a letter writer. However, this situation and the regulations that are being issued are having a huge effect on the rural areas. Granted we are less populated and therefore less of a concern for votes and opinions, but we have managed to continue to survive through some tough times. If these rules are not tweaked to allow us to do the job we have done in the past, I have a big concern for rural areas and their survival. 1-4 housing here is not the same as tract housing in any of the big cities. Capital is hard to acquire in Nebraska compared to any coastal state. Earnings grow capital, and earnings come from having opportunities to make things work for our neighbors. Regulations are well intended but there are consequences from those regulations. Please consider some of these consequences.

Respectfully,

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