

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

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 proposals¹ that were recently issued for public comment by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation

Dear Mr. Feldman:

I am writing you to express my concerns relative to the adverse impact that will most certainly result from the Interagency Risk-Based Capital Proposals, more commonly referred to as Basel III. The adverse impact of these proposed changes (which were designed primarily for the largest banks) to capital will be far more punitive for banks less than \$5.0 billion in assets, largely because of their difficulty to access capital markets.

Many of the smaller community banks are the very fiber of rural America's small business and labor force. In fact, according to the acting Chairman for the FDIC, Martin Gruenberg, community banks with less than \$1 billion in assets account for 40% of the small business lending in the US. For many years we have made loans to small businesses secured by personal residences that we hold within our loan portfolios. During the recent economic downturn we did not experience any significant increase in past-dues or foreclosures. Because of the increased capital requirements, and its related costs associated with loans secured by primary residences, we will either lose out to the "too big to fail" banks or, borrowers that traditionally qualified well before the subprime era will be left without reasonable financing options. In addition, marking the investment portfolio to market is counterintuitive to safe and sound banking practices.

The very nature of the investment portfolio is to provide both a source of liquidity as well as a reasonable hedge against a falling rate environment. If we begin marking this portfolio to market, it will cause community banks to substantially shorten the duration of their investment portfolio, giving rise to interest rate risk in a falling-rate environment, which is generally a time

when banks need all the help they can get. (A down-rate environment generally signals a weaker economy.)

Furthermore this will be like another tax upon the already burdened taxpayers. Why? Community banks have traditionally been very active purchasers of locally originated tax exempt bonds. If we substantially reduce our participation in these longer term investments, municipalities will be forced to pay up on the interest rates in order to pull in new investors. This is an unreasonable (and I suspect unintended) consequence that no one wants to have happen to taxpayers.

Lastly, our bank is one of a few holding Trust Preferred Securities (TPS) in support of Tier 1 capital. Most likely you will not receive much in the way of comments related to TPS since few community banks hold TPS. While eliminating this for the "too big to fail" banks was ok, the accelerated elimination of the TPS over 10 years for smaller community banks is far more burdensome. It is easy for the largest banks to replace capital...not so for us. This will only serve to reduce loan growth over the next several years while TPS is eliminated. If it must be eliminated, allow the principal to amortize over the remaining life of the TPS. While this in and of itself will be burdensome, it would be more manageable and, unlike the present proposal, the principal balance would, in fact, be extinguished over time. Even as the proposal is written today, we would be penalized for paying back any TPS principal until 10 years have passed. In other words, if we had \$10 million in TPS, and paid \$1 million toward principal during the first year, the way it is proposed today, we would now have \$8.1 million in tier 1 capital, not \$9 million from allowable TPS. Under this scenario we lose an additional \$900 thousand of tier 1 capital.

I have the highest regard for what is needed to shape and improve the safety and soundness for our industry. As I reflect back upon the reason for most of the recent bank failures, asset concentration dealt by far the greatest death knell for the failed institutions, followed by ineffective boards. Those of us still standing managed our way through this by adhering to sound banking practices, coupled with sound board oversight. The Great Recession did cause many of us to lose some money during this very difficult economic time; however, it is important to remember that many of us also came through it and are once again profitably contributing to the growth of our communities. Please be thoughtful before taking actions that detract from our ability to serve the important needs of our communities.

Sincerely,

Ty Palmer