From: Tammy Robison [mailto:TammyRobison@montgomerybank.com]
Sent: Monday, October 15, 2012 5:51 PM
To: Comments
Cc: 'Troy Wilson'; Max Cook (cmcook@mobankers.com)
Subject: Basel III FDIC RIN 3064-AD95, RIN 3064-AD96, and RIN 3064-AD97

October 15, 2012

FDIC
Via email comments@FDIC.gov

Re: Basel III FDIC RIN 3064-AD95, RIN 3064-AD96, and RIN 3064-AD97

Dear Sir:

This letter is in response to the request for comment on proposed rulemaking relevant to implementation of Basel III requirements.

We believe that small businesses are a key component in job creation and economic recovery in our communities and the country as a whole. We know that community bank loans are the primary source of capital for the small businesses in the communities we serve. The implementation of some of the Basel III requirements will impair capital in community banks and inhibit our ability to fund the capital needs of our consumer and business customers as we struggle to improve the small business economic engines in communities we serve.

Montgomery Bank, N.A. is a community bank with assets of $880 million with ten locations in Eastern Missouri within, what we consider three hub markets: St. Louis, Cape Girardeau, and Sikeston. Our charter is just over one hundred years old. We are a family-owned S-corporation. The Montgomery Family owns 100 percent of the stock of Montgomery Bancorporation, Inc., which is a single-bank holding company owning 100 percent of the stock of Montgomery Bank, N.A.

In light of the financial crisis and tough economic times, we believe it is prudent to strengthen the capital positions of banks. Community banks, including ours, have increased their capital ratios through this economic cycle. Banks in our peer group have increased their tier I capital ratio from 8.76% in 2008 at the height of the real estate meltdown, to 9.53% at the end of the third quarter this year. It does not appear appropriate to begin to restrict or eliminate a portion of capital in community banks or otherwise further restrict banks' capital at a time when lending by community banks is so important to the economic recovery of the country as a whole. My comments focus on three specific areas of the proposed rules, including: (1) elimination of Trust Preferred securities from inclusion of capital; (2) including fluctuations in the market value of investments in income; and (3) changes in the risk weighting of certain assets for capital calculations.

Elimination of Capital Inclusion from Trust Preferred Issues. We do not agree with the view that Trust Preferred issues do not represent a valid capital component of the companies that have them on their books. I am certain that the view of those investors who have lost money on Trust Preferred pools have a clear understanding of where they line-up from a protection of principal invested when it comes to liquidation or forced sale of a bank. Regardless of the validity of the inclusion or not of Trust Preferred debt in capital, in our opinion the near-term elimination of Trust Preferred securities from capital will restrict a significant number of community banks' ability to provide small business and consumer loans in communities they serve. We estimate the elimination of this source of capital will reduce our lending capacity by $20 million per year for every year 10 percent of the current balance is eliminated. If this component is to be eliminated, then a more patient and prudent approach should be considered.

Montgomery Bancorporation's current capital position includes $25 million of a Trust Preferred issue. Of the gross amount of the Trust Preferred issue, only $16 million is includable in tier I capital. We have included in our capital plan a repayment schedule for the retirement of that debt. The repayment of that portion of capital requires the use of capital that would otherwise be available to support growth and other capital needs. If 10 percent of the amount currently includable in tier 1 capital is eliminated in combination with the planned principal reduction of the Trust Preferred debt, then the stress on our capital position would not be tolerable and would require us to forgo our current repayment plan during the regulatory elimination period. It would make more sense to encourage financial institutions to repay the debt than to simply begin to exclude it. Simply eliminating the inclusion of this debt actually restricts financial institutions' ability to repay the debt during the elimination period.

A more appropriate approach would be to delay any changes to the treatment of this class of capital during this important economic recovery period, perhaps for a period of two to three years. Thereafter, begin to exclude a portion of Trust Preferred from capital, but reduce the excluded portion by the amount of actual repayments of the Trust Preferred issue.

Forcing Mark-to-Market Adjustments through the Income Statement. Forcing the mark-to-market adjustments on investments through the income statement also will restrict banks' ability to appropriately manage their balance sheet. This mark-to-market treatment of investment securities violates the fundamental accounting view of a growing concern. It forces the changes in liquidation value of only a segment of the balance sheet through the income statement without regard to the overall financial performance and continuing profitability of the business as a whole.

Like other community banks, Montgomery Bank uses its investment portfolio to manage our liquidity position, but also to appropriately protect our income stream from changes in interest rates. A significant portion of our liabilities are composed of transaction accounts which have limited exposure to changes in cost based on changes in market interest rates. It is prudent for our bank to invest a portion of these funds in relatively longer term loans and investment securities. This helps to stabilize our net interest margin as rates change. It is not appropriate to adjust current period earnings associated with the market volatility of a segment of our balance sheet that is designed to smooth our earnings stream. As interest rates move up, the franchise value of our transaction accounts also increases. We understand that the volatility associated with the value of core deposits is more complex and harder to quantify.

It is easy to quantify the market value of most investment securities, and we believe it is important to disclose those changes in value on financial statements. However, it is not appropriate to run changes in liquidation values of only the segments of our balance sheet related to investment securities through our operating results. Due to the level of transaction accounts on most community banks' books, they are more profitable when rates are relatively high. It appears to be counterintuitive to punish a financial institution's equity strength in an interest rate cycle when they are moving toward increased profitability and rewarding a financial institution's equity position and income when they are moving toward less profitability.

As I have mentioned above, it is very appropriate to disclose in financial statements the changes in market values of investment securities. We do not believe it is appropriate to run any market volatility associated with changes in interest rates on these assets through the income statement. As an alternative, it would be viewed as less onerous if this proposal allowed for the exclusion of market fluctuations in non-credit sensitive investments, including GSAs or Treasuries.

Changes in Risk Weighting of Certain Assets for Capital Calculation Purposes. Aspects of the proposed rules associated with risk weighting of assets appear to be redundant, compound existing capital requirements, and are in conflict with the mission of banks' community support mission, and inhibit our ability to serve the communities where we do business.

We believe that these changes to risk weighting of certain one-to-four family mortgages are the result of the backlash associated with sub-prime lending which was one of the root causes of the economic crisis and economic cycle we find ourselves in. From our bank's perspective and most other community banks, sub-prime lending was not an activity we participated in. More than 20 percent of our loan base is composed of one-to-four family loans within our markets. We have never wavered from our underwriting guidelines. The greatest preponderance of these one-to-four family loans is floating rate, but we do retain some 15-year fixed and even some 30-year fixed as they relate to our CRA commitment in the communities we serve. We closely monitor the levels of fixed rate loans we retain to make certain our balance sheet is in proper balance from an interest rate risk perspective. We also monitor ongoing credit quality issues, including past dues and charge-off levels, as we are required to do and incorporate those into the calculation associated with the adequacy of our allowance for loan loss. As in most community banks, the historical loss ratios on this portion of our loan portfolio could be used to make the case that the existing risk weighting of 50 percent on these loans is too high. It is a little perplexing from our perspective to understand the need to increase it. Capital needs for addressing inherent credit risk in this class of loans and other types of real estate loans are addressed partially in the guidelines associated with the adequacy of our allowance calculation and in the latitude our safety and soundness regulators have in determining the adequacy of our overall capital position.

Increasing the risk weighting for certain components of our one-to-four family loans as well as other real estate loans would restrict our ability to make home mortgages, including seconds and home equity loans in the markets we serve. From a broader perspective, it will cause other community banks to do the same which would further slow the economic recovery in the important housing and real estate sector of the economy.

The bottom line related to this capital restriction is jobs in our communities and our abilities to support the needs of our small business customers in the markets we serve. We strongly urge the implementation of these regulations be reconsidered in light of our current economic cycle.

Yours truly,

MONTGOMERY BANCORPORATION, INC.

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Chairman

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