MidWest*One* Bank™

October 17, 2012

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551
Via email at regs.comments@federalreserve.gov

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, DC 20219
Via email at regs.comments@occ.treas.gov

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation,
550 17th Street, N.W.
Washington, D.C. 20429
Via email at comments@fdic.gov

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.

For the past ten years I have proudly served as the President and CEO of MidWest*One* Bank – a $1.7 billion community bank headquartered in Iowa City, Iowa. Our bankers make business and consumer loans, collect deposits and offer wealth management services to our customers from 22 offices located throughout the eastern portion of the state. Our mission statement is "Take care of our customers and those who should be" and we take those words very seriously.

I understand the Basel III goal of strengthening the financial system by increasing the level and quality of capital that banks are required to hold, however, these rules are more appropriate for large complex financial institutions than for the relatively simple business practices of small banks. Let me take this opportunity to say that it was not the community banks that brought about the financial crisis of 2008. While some large banks and mortgage companies were selling and securitizing loans of questionable value, MidWest*One* was steadily making sound mortgage loans to our local customers. By December of 2009, our bank's mortgage loan servicing portfolio totaled just over $310 million. This amount is comprised of loans held on the bank's books and loans sold to either Fannie Mae or to the Federal Home Loan Bank of Des Moines. During the years of 2008, 2009 and 2010, the worst three years of the crisis, the actual loss experience on these loans was less that 0.15% per year. So, like most community banks throughout the U.S., our institution functioned as a source of stability by originating and delivering high-quality assets to the financial system during a very volatile period.

Further evidence of our role in providing stability has been the bank's increasing capital ratios since the end of 2008. MidWest*One*'s tier 1 risk-based capital ratio has climbed from 9.11% as of December 31, 2008 to 11.27% as of June 30, 2012. This increase in capital came during a period of asset growth, it came without the benefit of a capital raise and it includes the repayment of $16 million of TARP proceeds in the summer of 2011. Please do not interpret any of this as braggadocio; I am simply making the point that this type of performance is typical of most community banks.

As to some of the specific portions of the Basel III rules, I have several areas of concern. The first is the new regulation that would make unrealized gains or losses in a bank's investment portfolio part of its tier 1 capital position. This rule will have the undesirable and unnecessary affect of adding volatility to a bank's capital position. The investment portfolio at MidWest*One* is approximately $530 million representing just over 30% of total assets. We estimate that a 300 basis point rise in interest rates would translate into a decline in the market value of the portfolio of nearly $60 million. Such a move would reduce our tier 1 capital ratio by more than 2 percentage points. This new rule does not take into consideration a bank's overall sensitivity to interest rate movements and therefore cannot provide any insight into a firm's level of interest rate risk. MidWest*One*'s overall interest rate profile is close to neutral, yet a rise in interest rates would result in a significant decline in our capital ratios. As for credit risk taken in the investment portfolio, the existing rules for other-than-temporarily-impaired (OTTI) investments provide a mechanism for potential credit losses to be reflected in capital. Most banks use the investment portfolio as a source of liquidity and to manage interest rate risk. A natural response to the new regulation will be for banks to hold fewer securities or to reclassify existing portfolio assets as held-to-maturity (HTM). How can it be in the best interest of the financial system to ratify a rule which provides no improvement in measuring a bank's ability to sustain losses and at the same time would reduce liquidity system-wide?

My second concern relates to the amount of information and level of detail that we will have to analyze in order to comply with the new risk weights for residential mortgages. MidWest*One* is headquartered in a college town (University of Iowa), which also serves as a regional medical center. University and medical staff move into and out of Iowa City at a rapid pace and many want to purchase a home to live in during the 5 to 7 years they are here. For many of these customers a balloon loan makes good financial sense. Under proposed rules, loans with balloon payments would receive a risk weighting as high as 150% depending on LTV ratio. This does not reconcile with the loan performance we have experienced and may cause us to discontinue a product that has served our customers very well. In addition, the more "granular" approach to risk weighting assets would put enormous pressure on systems and resources. It is not clear that the bank has the data needed to be able to comply with new reporting requirements. We would likely need to hire additional staff to monitor the portfolio – updating collateral values and past due status regularly in order to comply.

Thirdly, the Collins amendment to the Dodd-Frank Act grandfathered the treatment of Trust Preferred Securities (TruPS) for banks between $500 million and $15 billion in assets. This seems reasonable given the limited access to capital that most community banks have. Keep in mind that under the current rules, the treatment of TruPS as tier 1 capital would phase out as these securities approach maturity. Since the mechanism for the elimination of tier 1 capital treatment is already in place, why is there a need to accelerate the process and place undue burden on small institutions? At our institution, TruPS constitute less than 10% of tier 1 capital and yet the rapid elimination of this form of capital will diminish our ability to extend credit in our local market. We believe that the original bargain struck in the Dodd-Frank Act is fair treatment and I would ask that you consider restoring the original rule regarding TruPS.

In this letter, I have touched only on the rules that will have the largest affect on MidWestOne Bank. Other aspects of the Basel III proposal will work to decrease the bank's capital level (exclusion of mortgage servicing assets), increase risk based assets (change in risk weightings for second mortgages, high volatility commercial real estate, and delinquent loans), or substantially increase the administrative burden and cost of compliance. The collective impact of Basel III – reduced capital levels and increased administrative burden – will make it much more difficult for the small, less complex and less risky institutions to survive and to thrive. These new rules will undoubtedly hasten industry consolidation, which reduces consumer choice. I urge you to consider the impact that proposed rules will have on community banks and to consider exempting community banks from the majority of these requirements. In so doing, you will help us to better serve our customers and strengthen our local economy.

Thank you for your attention.

Sincerely,

Charles N. Funk

Charles N. Funk
President and CEO
MidWest*One* Bank