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Gentlemen:

To my understanding, Basel III will establish new capital requirements for banks with the intent reducing systemic risk in the US and internationally. This laudable goal fails to recognize that the US banking system is very different than that of the rest of the world.

Europe, Canada and other countries have very few large banks and many of them are government owned or partially government owned. There are 6,659 banks in the US with only a few truly large banks that pose a systemic risk of any kind. None of them are government owned. They are either privately held or publicly traded on an exchange. Furthermore, the FDIC insurance system, paid for by FDIC Insured banks, guarantees that there will be no risk to the financial system (not to mention the US taxpayers) for the failure of insured banks except for those few banks that are large enough to pose a theoretical systemic risk. Those numbers of banks is surely less than 10 and are probably less than 5. Likewise, the number of nonbank financial institutions that pose a systemic risk are few in number.

We are a $285 million asset banking company with 4 offices located in Rural Minnesota. Minnesota has 386 FDIC insured banks with median assets of $89 Million. Failure of even a group of Minnesota banks would be paid for in full by loss of 100% of shareholder investment and the shortfall, if any, paid by bank funded FDIC Insurance premiums. Such a failure would have no impact whatsoever on the US financial system, much less the international banking system. The success of Community banks, however, has everything to do with the success of small businesses and small communities all over our country. Our system of many banks of all sizes is a huge plus for our economy of many needs both large and small. We are not a one size fits all system and we should not have a one size fits all/ international regulation such as Basel III.

Many community banks invest part of the funds they are unable to lend locally in longer term municipal bonds, as do we. These bonds are an essential support for local units of government and are held in the "Available for Sale" category so that, if interest rates change in any significant way, the bank can sell and reinvest to reduce risk and stabilize future earnings. Under current capital rules, the unrealized gains and losses (fluctuations in value) that occur as a result of ups and downs in the interest rate cycle are excluded when calculating a banks Tier 1 Leverage Ratio. Under the definition of Common Tier 1 Capital in Basel III, these unrealized gains and losses would cause significant fluctuations in capital levels that would virtually force banks with long term municipal bonds, or any long term bonds for that matter (the primary earnings component of bond investments for small banks) to place their long term bonds in the "Held to Maturity" category or reduce the maturity of their bond investments in order to meet common capital requirements. If a bank decides to place long term bonds in the "Held to Maturity" category, these bonds can no longer be sold and reinvested in a rising interest rate environment eliminating an essential risk management tool. If a bank with long maturity bonds chooses to shorten maturities instead, they lose or reduce an essential earnings component of their investment portfolio that makes a significant contribution to their financial health. This is a lose/lose proposition that reduces the franchise value of hundreds of community banks, increases the likelihood that many will merge or sell and small businesses lose an essential source of credit or at least lose access to credit from smaller institutions that tend to be more flexible in meeting their needs further reducing employment and the flow of money that drives local economies and in the aggregate, drives much of the national economy.

The treatment of unrealized gains and losses in the bond portfolio is our most significant concern. We also have concerns about the new risk based capital guidelines being proposed for mortgage loans that would reduce credit availability for consumers and put a damper on home values that already are suffering. We are working to understand these proposed rules better and may have further comment in this regard. There may be other concerns as we begin to understand the proposed rules better.

The characteristics of our bank and hundreds of others like us are that we are relatively small and are engaged in local markets that each have different characteristics to which we apply various strategies to serve the needs of our unique market and customers. If we make a wrong decision or take excessive risk that results in failure, we will have lost our entire investment. We lose our livelihood as well in closely held banks like ours where both the ownership and management are the same.

There are thousands of small closely held community banks that would be less able to serve their local markets under the Basel III rules and would disappear through mergers and sales at a much faster rate than they already are if the new rules are applied to them. These Banks should be exempt from the Base III rules or at least allowed more flexibility than systemically risky banks so that we can continue to serve our markets effectively. The cost of accelerated disappearance of community banks through inability to employ an appropriate balance between risk and investment return or through sale of these banks to larger institutions because of difficulties posed by new capital rules will slow economic growth and interest of economic growth and it makes existing banks larger potentially increasing the number of banks that could become systemically risky. This is counter to the intent of Basel III which is to limit risk in the banking system.

Community banks should not be sacrificed at the altar of a better world order. There are many examples of instances where it has not been in the best interest of the US to agree to an initiative broadly agreed to by other nations. Even if we initiate these rules on the world stage, there should be a community bank exception. Our banking system is very different than that of Europe, Canada and most, if not all, other major powers once you look past the largest 5 or 10 US banks. One of the best components of our financial system is a large number of strong and vital community banks that provide great benefits and pose virtually no financial risk to the US financial system or that of any other country.

Respectfully

P. Stephen Lindholm

Chairman and CEO
Independent Bancshares, Inc.