



# Citizens State Bank of Loyal

"the One Place to go"

*Main Office* • 400 N. Main Street • P.O. Box 218 • Loyal, WI 54446

*Granton Branch* • 110 Maple Street • P.O. Box 129 • Granton, WI 54436 *Neillsville Branch* • 2 Boon Blvd. • P.O. Box 30 • Neillsville, WI 54456

*Spencer Branch* • 302 S. Pacific • P.O. Box 20 • Spencer, WI 54479

October 15, 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 proposals<sup>1</sup> 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. My comments are as follows:

Community banks should be allowed to continue using the current Basel I framework for computing their capital requirements. Basel III was designed to apply to the largest, internationally active, banks and not the much smaller community banks. Community banks did not engage in the highly leveraged activities that severely depleted capital levels of the largest banks and created panic in the financial markets.

Community banks operate on a relationship-based business model that is specifically designed to serve customers in their respective communities on a long-term basis. This model contributes to the success of community banks all over the United States through practical, common sense approaches to managing risk.

The proposed risk weight framework under Basel III is way too complicated and will be an onerous regulatory burden that will penalize community banks and jeopardize the housing recovery. Increasing the risk weights for residential balloon loans, interest-only loans, and second liens will penalize community banks who offer these loan products to their customers and deprive customers of many financing options for residential property. Additionally, higher risk weights for balloon loans will further

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<sup>1</sup> 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.*

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Loyal: Phone (715) 255-8526 • Fax (715) 255-9315 • Toll Free (800) 599-8399

Granton: Phone (715) 238-7169  
Fax (715) 238-8412

Neillsville: Phone (715) 743-7494  
Fax (715) 743-7495

Spencer: Phone (715) 659-5159  
Fax (715) 659-5370

Website: [www.csbloval.com](http://www.csbloval.com) • Email: [csb@csbloval.com](mailto:csb@csbloval.com)

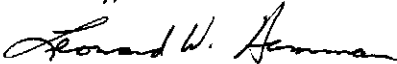
penalize community banks for mitigating interest rate risk in their asset-liability management. Community banks will be forced to originate only 15 or 30 year mortgages with durations that will make their balance sheets more sensitive to changes in long-term interest rates. Many community banks will either exit the residential loan market entirely or only originate those loans that can be sold to a GSE. Second liens will either become more expensive for borrowers or disappear altogether as banks will choose not to allocate additional capital to these balance sheet exposures. Community banks should be allowed to stay with the current Basel I risk weight framework for residential loans. Furthermore, community banks will be forced to make significant software upgrades and incur additional operational time and costs to track mortgage loan-to-value ratios in order to determine the proper risk weight categories for mortgages.

Access to capital for community banks is limited, with capital increased from earnings which is not easily generated. Basel III could hamper a bank's ability to meet and maintain minimum capital requirements.

In summary, the Basel III Capital Proposals will negatively affect customers of community banks as certain mortgage products may be eliminated and the overall operational costs of complying with the Basel III requirements may lead to increased costs to customers. The Basel III calculations are complicated and will require substantial additional costs for community banks, diverting resources away from assisting our communities in obtaining the needed loans to enhance the local economy.

Thank you for your attention to my comments.

Sincerely,

A handwritten signature in black ink, appearing to read "Leonard W. Hamman". The signature is fluid and cursive, with the first name being the most prominent.

Leonard W. Hamman  
EVP-CCO