FIRST FEDERAL

October 22, 2012

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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.

First Federal Savings Bank of Twin Falls, chartered in 1916, is a $482 million mutual community bank with eleven offices in southern Idaho. We employ 205 employees. We take our role as a community bank seriously as we provide excellent service and opportunities to the citizens of the Magic Valley. We have transformed over the years from a traditional thrift to a full-service community bank making mortgage, consumer, and commercial loans. We consider ourselves the premier home-mortgage lender in southern Idaho and are very careful in our loan underwriting. We offer free checking, online and mobile banking, and many services for small businesses such as cash management, funds transfers, and remote deposit. We work with many small businesses from independent restaurants and trucking companies to a local oil company. We enjoy serving the communities and people of southern Idaho and look forward to many more years of service.

We understand the need for capital regulations which protect the banking industry and we are not opposed to regulations which are necessary to insure the safety and soundness of community banks across the nation. We have been very aware of our capital numbers over the years and have enjoyed a well-capitalized status. We were careful in past years to avoid subprime lending as well as exotic mortgage loan structures and have seen the benefits of avoiding the pitfalls that have plagued the industry. First Federal is a very conservative lender, underwriting loans prudently and offering the communities we service loan products to help and enhance their lives and the vitality of our communities. We began commercial lending in 1992 and have carried our strong housing underwriting history into the commercial loan venue and have not been seriously negatively affected by the economic downturns of the last four or five years.

Although our capital levels are estimated to meet all proposed capital rules according to the Regulatory Capital Estimation Tool, there are a number of issues in the new Basel III and Standardized NPR proposals that concern us.

First of all, we were pleased to hear Comptroller of the Currency Thomas J. Curry make the following comment in his speech in San Diego:

> We recognize that the extra volatility that such an AOCI pass through would cause would be expensive and difficult to manage—a source of significant regulatory burden—especially to banking institutions, including mutual thrifts, that do not regularly access the short term capital markets. We have already received enough substantive comments on AOCI that I can promise you that we will be taking a very serious look at what our options are to address this conundrum once the comment period ends.

AOCI is a concern we have relative to the new proposals. Our balance sheet is not heavily invested in assets which will be significantly impacted by AOCI at this time, but could be in the future. Even with our limited exposure to the capital volatilities associated with proposals in this area, our net income would fluctuate and provide for information relative to the safety and soundness of the bank, which would be out of context. Our president just returned from a meeting with the OCC in Montana. One of the topics of discussion was the loans-to-deposits ratio. We currently have a loans-to-deposits ratio of about 89%, and the perception of our president was that the OCC was quite concerned about higher ratios. We recognize the risks associated with an elevated loans-to-deposits ratio, but if we were required to keep our ratio lower, that would require more investments on the balance sheet, thus increasing the volatility of our capital as a result of AOCI. As the proposal only deals with investment securities and does not take into account other aspects of the balance sheet, it seems to be a one-sided proposition.

Secondly, the rules already impacting residential mortgages and the proposed rules make mortgage lending more difficult and more costly. We have heard of institutions which have provided home loans for years deciding to exit or contemplating exit from the market. Our determination is to not exit the market. As mentioned earlier, we view ourselves as the premier mortgage lender in southern Idaho, but find ourselves constantly devoting more and more resources to compliance and regulatory burdens with respect to mortgage lending. We have been very successful in home lending in the valley and find the proposed rules creating even more difficulty and anxiety as we go forward with our main line of business. We service over $500 million of mortgages and look forward to providing these services to our market. Considering certain one-to-four-family residential loans as Category II loans makes the assumption that our underwriting practices for second-liens, for example, are not appropriate. We do consider home equity loans and lines of credit as an asset class in which we have a great amount of experience. In fact, we are typically more concerned over second liens we have with borrowers who have their first mortgage with another lender than those who have their first and second liens with First Federal. Knowing our customers, underwriting appropriately and watching LTVs is important, which I believe we do to a high standard. I do not disagree with the enhanced capital requirements based on different LTV levels. I believe the different risk weights based on LTVs could be the focus with avoidance of the complexity and debatable advantage of different treatment of so-called Category II loans. The complexity of the Standardized Approach NPR is evident.

The Mortgage Servicing Asset (MSA) proposed requirement will not currently impact First Federal as our MSA is currently about four percent. However, I do believe that proper market valuation instead of a ten-percent-of-capital limitation would appropriately cover the issues at hand. If the asset is at market value, why limit its contribution to capital. If the concept is that we are not valuing it correctly, let's fix that. We are currently valuing our MSA at 63 basis points and have been disgusted with the income statement volatility associated with the valuation of the MSA. I think proper valuation is the answer, not choosing a level at which it is ultimately removed from capital.

Generally, relative to the different risk ratings associated with the proposed rules associated with high volatility commercial real estate lending and delinquent loans is a matter we spend hours on each quarter evaluating ALLL and setting appropriate levels for the allowance for losses. We view ALLL as a buffer to our capital and feel that setting higher risk weights on these particular assets would be a duplication of effort and potential penalty. Our losses have historically been much below our peers and often we find it hard to justify raising our ALLL levels based on history, but do so based on our peer groups and the need to protect our capital against potential loses.

We feel the proposed requirements would be overly punitive to the community banking system and would create difficulties in administration because of the complexity of the calculations. We feel as we come out of one of the more difficult economic periods in our 96-year history that we are well positioned for the future. We feel that the capital levels we adhere to and the time and effort put into ALLL analysis continue to serve us well, and that there is a simpler approach that could be followed by community banks to see to the safety and soundness and continued viability of this part of the banking system. Our compensation costs continue to rise as we hire additional personnel to implement all of the regulatory changes and proposed changes coming through the system, and find this to be a potentially greater negative impact to the bank and our capital than the risks supposedly circumvented by the new proposed capital regulations. As a mutual we depend on increasing capital through earnings. As compensation costs increase and opportunities for fee income decrease, our ability to add to capital is diminished.

We appreciate the opportunity to make comment to the proposed capital regulations and understand the need for prudent capital requirements on the banking system. We will do our part in providing for the safety and soundness of First Federal Savings Bank of Twin Falls, but feel we can do this through capital requirements already in place, or through enhanced capital requirements in a more simplified approach. Ultimately, we feel that 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 community banks. We operate on a relationship-based business model that is specifically designed to serve customers in our 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.

We believe we can reach the required goals through simpler methods, which will protect our community banks in the United States and provide for the continued success of our communities, our customers and our banking system.

Sincerely,

Jay P. Dodds
EVP/CFO
First Federal Savings Bank of Twin Falls