From: Roy W. Terwilliger
To: regs.comments@federalreserve.gov; Regs.Comments; comments@fdic.gov
Cc: Joe Witt
Subject: Commenbts on proposed rulemaking as proposed by BaselIII
Date: Tuesday, October 23, 2012 5:56:50 PM

Sent via OCC Secure Mail
Jenifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW

Office of the Comptroller of the Currency
250 E Street, S>W> Mail Stop 2-3
Washington, D.C. 20219

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 2f0429

RE: My Comments on the proposed Basel III

To Whom It May Concern:

Flagship Financial Group In. is a two-bank holding company with Banks located in two Minnesota Communities. The Banks are Flagship Bank Minnesota , Wayzata, MN and Flagship Bank Winsted, Winsted, MN. Our Directors and Officers are opposed to the standards set forth in Basel III. We believe the change will have a negative impact on our community banks and the local residential lending market, which will impact all banks and the recovery of the local housing market.

Let me be a little more specific as it relates to our larger bank, Flagship Bank Minnesota which is approximately a $100 million asset community bank with two offices located in Eden Prairie and Wayzata. We believe there will be five primary areas where Basel III will have a direct impact:

- First, about 22% of our current loan portfolio is made up of consumer junior real estate loans. The deterioration of the real estate market has resulted in most of these loans having current loan to values greater than 80% many over 90%. These loans will all move from the current 100% risk weight bucket to the 150 % or 200% bucket. This will have an immediate impact on our risk based capital of about $11,000,000 in increased risk. While we understand that the increase is the intention of Basel III, we also believe that the real estate loans that have survived the downturn in the economy are good loans to good borrowers. Basel III does not recognize the strength of the borrower, only the loan to value of the collateral which is a poor method of determining credit risk.

- The second impact is directly related to the results of the increase in risk weighting on consumer real estate loans. With the added pressure on our capital, Flagship will need to make loan decisions based on impact to capital, instead of the quality of loan and the community needs for consumer real estate loans. Home equity lines of credit, one of the life lines to consumer spending will become very difficult to offer. There are also some very good reasons to provide quality balloon lending, purchase money second mortgages, and high loan to value first mortgages which benefit the consumer and the real estate market. These types of loans will also be very hard to justify due to the impact on capital. The end result from our Bank, and we believe from our peers, is a tightening of the real estate market at a time when the real estate market still needs stimulus from banks.

- The third impact is due to the increase in risk weighting of unused commercial loan commitments. Many of our commercial customers rely on the cash flow needed by lines of credit. The Bank has structured loans so that they are under one year in duration to the 0% risk weighting applicable to Basel II. The increase in risk weighting on these loans to 20% will make the Bank reconsider having lines of credit outstanding. This will have a definite impact on our commercial borrowers and their ability to adjust to fluctuations in their business cycles. Many of these are very strong credits with cash flow and abundant collateral, but neither financial strength or collateral, as emphasized in the rest of Basel III, have an impact here. All unused commitments will have a negative impact on collateral.

- The fourth impact is the requirement to track loan to value, balloon payments and other criteria from our lending portfolio will result in significant personnel costs and most of our real estate loans will need to be recoded so they can be tracked.

- Finally, we believe that the advanced approach available to the larger banks will a have a negative impact on all smaller community banks. The large banks will be able to offer niche products which community banks will not be able to offer due to capital impacts.

Flagship Banks believe that capital is very important and reforms are probably necessary. We believe that collateral based lending is a poor lending practice and therefore believe that basing capital requirement on collateral is also a poor practice. Basel III should be eliminated or reworked so that the quality of the borrower is the driving force behind the required capital reserves. It makes no sense that a five year balloon mortgage at 30% loan to value to a borrower with an 800 credit score counts more against capital than a 90% loan to value 30 year loan to a borrower with a 550 credit score.

Thank you for your consideration.

Roy Terwilliger

Roy Terwilliger
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