Fishback Financial Corporation

October 15, 2012

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 NW
Washington, DC 20429

Submitted via www.regulations.gov.

**Re: Regulatory Capital Rules – Docket Nos. OCC-2012-0008 and OCC-2012-0009
FDIC RIN 3064-AD95 and RIN 3064-AD96**

To whom it may concern:

This comment letter was written on behalf of Fishback Financial Corporation (FFC), a privately-held financial holding company headquartered in Brookings, SD. We began as a check-cashing station in 1880 and have grown to include four (4) First Bank & Trust charters in 16 locations along the Interstate 29 corridor in Eastern South Dakota and Southwestern Minnesota. Our assets total nearly $1.7 billion.

We submit the following in response to the Joint Notice of Proposed Rulemaking and Request for Comments regarding Regulatory Capital Rules related to:

- Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition provisions, and Prompt Corrective Action; and
- Standardized Approach for Risk-Weighted Assets and Market Discipline and Disclosure Requirements.

We appreciate the opportunity to comment on the notices of proposed rulemaking. We are in favor of many aspects of the proposed rules and support the efforts to improve the methodology to calculate appropriate capital levels. We do not oppose the proposed increases to required minimum capital levels. However there are certain aspects of the proposed rules which we believe will harm our ability to serve the financial needs of our communities, and others for which clarification is needed.

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Accumulated Other Comprehensive Income (AOCI)

Under the proposed rule, unrealized gains and losses on available for sale (AFS) securities must flow through to common equity tier 1 (CET1). The inclusion of unrealized gains and losses on AFS securities is an area of great concern as it will have a significant impact on our capital accounts, capital account management, and overall balance sheet management.

Changes in the market value of investments over varying rate cycles create volatility in FFC's capital levels. For example, the change from our current unrealized gain on the investment portfolio to the projected net unrealized loss after a 200 basis point increase in interest rates equates to approximately $17 million or 1.30% of total risk based capital.

The proposal will also alter our asset-liability management activities and force us to maintain a much shorter duration on investments that are marked to market when it is not optimal for FFC's overall interest rate risk management.

Based on the above, we would request that the agencies eliminate this new requirement. In the alternative, we would request that the agencies exempt unrealized gains and losses that predominantly result from changes in interest rate risk.

Mortgage Servicing Assets

The proposed rule requires financial institutions to deduct all mortgage servicing assets that exceed 10% of its CETI. The amount below 10% will have a 100% risk weight (250% in 2018).

Many community banks like ours provide mortgage servicing and the related asset often exceeds 10%. We pride ourselves in providing quality, customer-focused mortgage servicing. Our customers know where and how to reach us, and they have grown accustomed to personal contact with our mortgage servicing staff. Additional capital restrictions on mortgage servicing assets will increase community bank costs and may ultimately encourage exit from this business. The consolidation of mortgage servicing away from community banks and towards large nationwide companies cannot be in the best interests of consumers.

Based on the above, we would request that the agencies exempt existing mortgage servicing assets from the 10% CETI cap.

Trust Preferred Securities (TruPS)

The proposed rule phases out TruPS in annual increments until they are eliminated entirely in January 2022. The proposal is inconsistent with the Collins Amendment of the Dodd-Frank Act and will eliminate an essential, and difficult to replace, source of low cost capital for community banks. FFC in particular will suffer a loss of $30 million of capital.

We would request that the final rule be consistent with related provisions of the Dodd-Frank Act, which grandfather TruPS for banks between $500 million and $15 billion in assets.

Residential Mortgages

The agencies propose to impose new methods for risk weighting mortgages that may result in increased risk weights up to 200%. The proposal includes murky definitions and retroactive restrictions and requirements that will be difficult to implement.

We would request that the agencies clarify the definition of balloon payment and include only payment-option or negative amortizing loans. FFC will be less inclined to offer amortizing adjustable rate mortgages, an effective credit tool for borrowers, if the risk exposure remains as proposed. We would also request that the definition for category 1 loans be modified to align with existing underwriting guidelines. Finally, we would request that the final rule grandfather all existing mortgage exposures. Most community banks do not have the system functionality or access to data necessary to assign the proposed mortgage categories. Nor do they have the resources needed to examine old mortgage records in order to calculate the proposed risk weights and loan-to-value ratios on each.

Credit Enhancing Representations

Under the proposal, banks must treat credit enhancing representations or warranties on assets sold or transferred to third parties as off-balance sheet guarantees and apply a 100% credit conversion factor (CCF). It is unclear if the CCF expires with the representation or warranty.

This proposal will cause substantial capital changes for a significant volume of sold mortgages. If FFC is no longer able to sell mortgages on the secondary market due to increased capital requirements, our customers will face restricted access to credit. Therefore, we would request that the agencies ensure risk-based capital charges do not apply to mortgages once they are sold to third parties, even when the seller agrees to take back mortgages with very early payment defaults. In the alternative, we would request language clarifying that the CCF expires with the representation and warranty period.

High Volatility Commercial Real Estate (HVCRE)

The proposed rule defines high volatility commercial real estate (HVCRE) as acquisition, development, and construction (ADC) commercial real estate loans except 1-4 family residential ADC loans and commercial real estate ADC loans that meet certain requirements. Each HVCRE loan will be assigned a 150% risk weight, a 50% increase over current risk weights.

We estimate HVCRE accounts for 20% of our commercial real estate portfolio. The proposed rule will result in significant cost and regulatory burden as FFC and similarly situated banks attempt to establish new systems to capture and track the data needed to risk weight these properties. The proposal will also limit our ability to offer terms suitable to the impacted customers' needs.

We would, therefore, request that the agencies simplify the risk weighting criteria.

Delinquent Loans

The agencies propose to assign 150% risk weight to nonresidential loans over 90 days past due. FFC accounts for the potential loss exposure of delinquent and any problem loan through provisions to the allowance for loan and lease losses (ALLL).

The adequacy of the ALLL is subject to significant review and oversight by Senior Management, the Board of Directors, and our regulators. If the ALLL is adequate relative to FFC's loan portfolios, any additional capital requirements are duplicative and retroactive. Further, the introduction of a capital penalty for past due loans will discourage banks from working with their borrowers through difficult times as removing these loans from the balance sheet will become a priority. To alleviate this result, we would request that the provisions be eliminated from the final rule.

Conclusion

Thank you for the opportunity to comment on the Basel III Regulatory Capital Proposals. If you have any questions or would like more information regarding the above, please feel free to contact me by email at dave.waligoske@bankeasy.com or by telephone at 605/696-2200.

Sincerely,

Dave Waligoske
President and CEO of Fishback Financial Corp.

CC South Dakota Division of Banking
South Dakota Bankers Association