From: First Community Bank, Sam Waters

Proposal: 1442 (RIN 7100-AD 87) Regs H, Q, & Y Regulatory Capital Rules

Subject: Regs H & Y Regulatory Capital Proposals

Comments:

Federal Reserve Board:

I writing to express my concern over the proposed rules and passage of Basel III. I am the President and Chairman of First Community Bank of Glasgow Montana. We serve primarily small rural communities in Eastern Montana in addition to a small segment of business in Western Montana. We feel we operate under a fairly conservative operating plan that not only serves our customers but provides for a fair return to our stockholders. We maintain a conservative loan to deposit ratio in the 70 to 75% range. With the economic down turn and the lack of loan demand however this ratio has now dropped to 65 to 70%. As a result we do carry a fairly significant investment portfolio on a regular basis. As with all investors, we regularly see the market value of those investments change with the ever changing interest rate markets. We have recorded those adjustments in value on our balance sheet as required by regulation without any impact on our regulatory capital.

The passage of Basel III would in fact change all of that and now require all banks to record such value adjustment to the bank's regulatory capital. This has the potential of adding a huge amount of volatility to our banks capital. Interest rates are at all time lows and have been held at those lows for several years. Most banks including First Community Bank have been forced to reinvest its portfolio at these rates. When rates do begin to increase and that increase promises to be significant, First Community Bank will be forced to write down a significant amount of its capital because of the decreased value of its investments. This scenario will be replayed continually in the future making long term capital planning extremely difficult to impossible.

The other concern I have with Basel III is with the risk rating of our loan portfolio, primarily with real estate loans. Home equity, home improvement and 2nd mortgage loans have been used extensively by our customers. In the small communities we serve, we see very little change in home ownership in those communities. People generally buy a home for life and then use built up equity to improvement their home or use equity in their home to help make other investments such as college expenses for their children or to start a business. The same can be said for farm and ranch owners and the equity in their farm or ranch. Basel III has the potential of eliminating these products and services to our customers by increasing the risk rating on these types of loans to as high as 200%. This will require banks to increase capital to cover this sweeping risk rating change. Many banks including First Community Bank will have to seriously consider eliminating these types of products as they will simply not be able to generate enough capital to cover the costs of the risk rating change along with the overall requirement for more bank capital.

Small banks such as First Community Bank have very little access to the capital markets. Capital in small banks is primarily raised from earnings or additional investment from our stockholders. Basel III promises to reduce earnings by forcing banks to change their investment strategies and reducing loan volume. Reduced earnings will make for a smaller return on equity and slower capital growth. Stockholders will be less favorable to investing money into the bank as earnings and return on equity decrease.

One of the primary reasons for the writing and adoption of Basel III has been for the leveling of capital markets world wide. This leveling of world wide capital requirements was to make sure that banks operating world wide or in multiple counties are all operating on a level playing field. I applaud that, however I wonder why this has to be forced upon a little bank in Northeast Montana which serves primarily small communities in Montana. This is simply another attempt to write a one size fits all regulation that will ulimately cripple community banks in rural America and the economies of the communities and areas we serve.

I strongly urge you to exempt small community banks such as First Community Bank from Basel III and write capital requirements that reflect our business culture and that of the communities we serve.

Sincerely

Samuel D. Waters
First Community Bank