FIRST STATE Bank
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September 14, 2012

Jennifer J. Johnson, Secretary
Board of Governors, Federal Reserve System
20th St. & Constitution Ave. N.W.
Washington, D.C. 20551

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

Robert E. Feldman
Executive Secretary
Attn: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th St. N.W.
Washington, D.C. 20429

Ladies and Gentlemen,

I am writing to provide comment on the Basel III proposals which 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.

I am the Chief Financial Officer of First State Bank of Middlebury, Indiana, a independent community bank of approximately $380 million in assets. I am hopeful that you will allow community banks such as ours to continue to use the Basel I capital standards.

It seems to us that the new proposed standards were designed to assess risk on an international level, and therefore apply much greater risk weighting than would be appropriate for the type of business being done by community banks. The higher capital requirements that would result from the application of the proposed rules would be a significant hindrance to growth and business development for many banks. We think that this would create more obstacles to the economic recovery of the nation.

The concept of mark to market accounting is also detrimental to economic recovery. Including Other Comprehensive Income or Loss in the equity component of capital calculations would be just that. Mark to market accounting can create losses to balance sheets that are unrealistic, and in fact, contributed greatly to the economic disaster from which we are still trying to recover. Unrealized losses may in fact never become realized losses, and the inclusion of those as an equity component will unnecessarily tie the hands of many banks in their ability to develop new business. With interest rates at historically low levels, rates will inevitably be rising in the not too distant future. This will increase the unrealized losses in all banks' portfolios, and will lead to a capital crisis under the proposed rules.

The newly proposed risk weighting standards in Basel III would also be a very complicated requirement for community banks, and would greatly hinder residential mortgage lending and the housing recovery. Many community banks offer variable-rate or balloon mortgages as a way of managing interest rate risk. We would now be penalized for these types of lending and the result would be fewer options for the mortgage customers. Second liens are also likely to become much more expensive, or unavailable, to consumers. We believe the current risk weighting standards of Basel I are much more appropriate for community bank loan portfolios.

In conclusion, it seems that the proposed Basel III capital rules would unjustly penalize smaller banks for problems caused by the business practices of the very large banks. Community banks do not engage in the same types of high-risk transactions as banks that operate on an international level. We feel very strongly that the proposed rules could have dire consequences for community banks across the country, and would be detrimental to the economic recovery of our nation.

Sincerely,

FIRST STATE BANK OF MIDDLEBURY

Greg R. Krider
Sr. VP/CFO