Union State Bank

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October 22, 2012

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

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, N.W.
Washington, D.C. 20429

Re: Basel III Capital Proposals

Ladies and Gentlemen:

Thank you for the opportunity to provide comment on the Basel III proposals[1] that 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. In my comments I want to;

1.) Introduce who we are for better reader clarity
2.) Provide a 25 historical prospective from main street Everest, KS (population 300)
3.) Prescriptive address what needs to change in this proposed set of regulation
4.) Issue a warning if this regulation is enacted as proposed

[1] The proposals are titled: *Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, and Transition Provisions*; *Regulatory Capital Rules: Standardized Approach for Risk-weighted Assets; Market Discipline and Disclosure Requirements; and Regulatory Capital Rules: Advanced Approaches Risk-based Capital Rules; Market Risk Capital Rule.*

Who We Are:

Union State Bank of Everest (USB) is headquartered in Northeast Kansas in the same small town it first chartered to serve in 1901. Over our bank's 111 years of operations, USB has been lead by four Presidents. The longest tenured President, H.M. Means, lead the company from 1919 through 1944. He successfully guided our organization through the post WWI years, the roaring 1920's, the dirty 30's, up through the beginning of WWII. By anyone's measure he was an amazing community banker.

I have had the honor of leading USB since 1989 from main street Everest, Ks, population 300. In 1989 the bank was operating from one building with $12MM of assets under management in a Kansas banking market where 80% of the banks were larger. By the beginning of the bank crisis of 2007, USB had grown to $100MM in assets and serving three rural communities. Because of the lessons learned in the 1980's, USB was well position at the beginning of this banking crisis. Over the last 5 years of the crisis, USB has been in the top 15% of all banks nationally in earning performance. USB's strong asset and earning profile has allowed it to leap forward by acquiring and merging three local community banks. Currently, USB operates in five, and soon to be six, rural communities in northeast Kansas and northwest Missouri with $260MM in assets under management. USB is now in the top 20% of Kansas bank in assets, still operates it main office from main street Everest, and still minute on a national stage.

25 Year Historical Perspective from Main Street Kansas:

In 1989 the organization was just emerging from 2nd great agriculture depression and lucky to survive. As we looked for ways to grow and diversify our geography and agricultural loan concentrations, we saw new opportunities with the collapse of the S&L industry and failure of the Farm Credit System to make home loans and ag real estate loans. At the time these were new frontiers of lending for Kansas Community banks. After all, we learned through the 1980's that Agriculture had too much debt and that we needed to diversify our portfolios if we were to survive. Banks all over Kansas did the same thing and began to grow their residential lending portfolios, all with balloon loan products. In the community banking arena these balloon loans products serve the customers and bankers well as we use the balloon maturity as an opportunity to review with the borrow there financials and balanced their ability to make new payment amounts with the bank's need to control interest rate risk. Community bank's had just came through an interest rate market that broke the S&L industry, but understood that bankers can only charge what a customer was able to pay.

In the 1990, computing advances lead to the development of securitization of mortgage products with the creation and buildup of Fannie and Freddie. Soon Wall Street learned the same skill sets and by the turn of the century local banks were facing stiff completion by nation mortgage AGGREGATORS. We all know the rest of the story, as corruption grew unchecked until the collapse in 2007. I might add that in the midst of this buildup from 2000-2005 regulators and the public saw a residential mortgage with the same credit quality as a US Treasury.

Prescriptive address what needs to change in this proposed set of regulation:

1.) One Size Does Not Fit All.

How can it even be conceived that a capital standard designed internationally for the most complex institutions in the world to bring international capital standards consistent, has anything to do with the capital needs of a bank on main street Everest that has been operating safely for 111 years? For every bank in Kansas (approximately 300) a regulatory capital framework using the simplest of capital ratios - dividing Tier I capital by total assets is perfectly adequate. It was that way in our state prior to the last change in the capital framework and it worked! Bankers to this day in Kansas don't take the time calculate risk based capital components in our day to day or month to month capital management. We use this basic calculation as described above and we generally only look at the risk based numbers we have to complete all the calculation for Call Reports. Moving to a vastly more complex of asset buckets and capital calculations makes no sense for our bank.

This simplicity is in stark contrast to the largest banks in the country who have complex assets and capital components with enough Wall Street engineering to confuse everyone from stock holders to regulators. The firms certainly have earned the complexity of capital proposal, but not main street banks.

2.) Unrealized Gains should not be posted to earnings:

USB is fortunate to have a small bond portfolio because we are active lenders and operate at loan to asset levels of 75-80% with very short loan durations. As a result, it makes sense for as a sub-S bank to invest most of our small bond portfolio in long term muni bonds. We are also fortunate at this time to have a gain of $2MM - $2.5MM, which is relatively large to our Tier 1 Capital of $18MM. It would be nice to move this gain at the moment to capital. However, we hold all of our bond in Available for Sale (as most small banks do) and we all know some day rates will go up and we may run as large of an unrealized loss. Why would regulator's for a non-complex bank want to design a certain capital call event? This just makes no sense for small banks that do not have a trading book of business. Does it make sense for Goldman to mark to market at the end of each day… absolutely. Does it make sense to mark to market the bonds assets of USB at the end of each month… absolutely not.

3.) Highly capitalized and numerous buckets for residential real estate loans:

USB helped to fill the residential credit need in our rural communities with the failure of the S&L industry of the 90's. We have competed and survived the assault of Wall Street empower mortgage brokers in the last 10 years. Wall Streets ability to aggregate loans across this nations and then exploit such products as balloon real estate loans under the watchful eyes of your regulators should earn the burden of this complexity of regulation. That has nothing to do with Kansas banks meeting the needs of Kansas consumers with well delivered balloon products. One-third of our bank's loan portfolio is in home loans, with most being balloon loans. Regulator's have already crammed down our pricing to the point that we go the government's website for each loan to see what we can charge. Now don't even take into consideration that the websites index is based on flawed pricing structure set in motion by a flawed capital standard that allowed Fannie and Freddie to grow and fail. But despite that point, each day we set our loan rates not on the market in rural areas, but from a regulator's website because of fear of high price mortgage regulations directed at subprime lenders. Now over lay that with this new capital standard the may cause us to increase our capital footing under our residential loan portfolio by 8X all the time being limited by our pricing. We may either be forced to re-engineer our mortgage products or get out of the home loan business. Our rural communities need our direct mortgage lending as it is nearly impossible to meeting the new stricter appraisal and underwriting standards of the Fannie and Freddie products. This proposal will kill rural home lending.

5.) Issue a warning if this regulation is enacted as proposed:

Warnings can only be issued from positions of strength. The community bankers hold the high ground on Capitol Hill in the banking crisis as compared to Wall Street Banks and even regulatory agencies for that matter.

We fought hard to prevail in many Dodd – Frank battles. These victories will not be overturned by a proposed joint regulatory rule. The imposing of this standard to small banks was a misstep by regulator's that surprise the whole industry. As a small bank, the implementation of this reg as proposed has backed us into a corner for our very survival.

In closing, I hope the regulators give careful consideration in moving forward with imposing this on small banks. HM Means fought for organization to survive from 1919 to 1945. I believe this reg as proposed has the potential to put our organization out of business. We will not go down with out a major political fight.

Sincerely yours,

Steven J. Handke

Steven J. Handke
President, CEO