WELCH STATE BANK

Member F D I C

September 28, 2012

To: Federal Reserve Board

From: Jay Victor, Sr. Vice-President, Welch State Bank, Welch OK

Reference: Basel III Docket No. 1442

To whom it may concern:

I'm a community banker in a rural Northeast Oklahoma. Our bank has approximately $200 million in assets with three locations. Our market niche has been financing rural dwellings and properties that do not qualify under FNMA or GNMA guidelines. Most of these properties are purchased by low to moderate income families. The average size of our 1-4 family residential loans is approximately $47,000. These are not customers that are actively marketed to by larger institutions and the properties do not qualify for secondary market financing due to acreage, age of the structure, or type of construction. The historical performance of our "in-house" residential loans has been much better than statistical equivalents for secondary market loans.

We analyzed both our loan and bond portfolios under the new criteria of Basel III and Standardized Approach. Our Total Risk-Based ratio plunged from 21.1% to 14.3%. Tier 1 Risk-Based capital dropped from 19.9% to 13%. Common Equity Tier 1 Risk-Based capital fell from 21.2% to 10.5%. Shocking would be a proper adjective to describe results of the latter. The drastic change of the various capital adequacy measurements is due to the combination of revised mark-to-market devaluation in our bond portfolio and the dramatic changes in risk weighting for residential loan assets. Basel III leaves few options for risk management and gives no consideration for our banks historical loss profile. The bank will have few options other than to restrict lending until the revised capital risk measurements can be improved. The new bond risk calculations will limit community bank participation in the municipal bond market. The cost of funding local schools and similar projects will increase as a result of the new rules. Our entire community will be negatively impacted.

Additionally, we reviewed our loan portfolio and found that less than 10% of our existing 1-4 Family residential loans meet the new Standardized Approach NPR Category 1 criteria. This is due primarily because of balloon features or interest rate caps that were usual and customary for direct bank lending when they were originated. The existing 1-4 family loans will continue to pressure capital measurements until they pay down, refinance or pay off. The balloon or rate cap features were used to manage interest rate risk exposure, a key component in CAMELS ratings. If we originate new in-house 1-4 family loans to meet Category 1 criteria, our ability to manage IRR will be abated precisely at the time our risk is greatest.

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The collateral and loan tracking requirements will be all but impossible for our institution to perform. Our computer systems do not have the ability to link first and second mortgages to the same collateral. I have had conversations with our core provider and they question if they will be able to track the loans to the extent you have required in your guidance. At a minimum, we will have to review all loan codes by hand and establish additional identification of loans that qualify or do not qualify for Category 1 risk weighting. Most likely we will have to maintain separate logs by hand, of loans where we hold both the first and second mortgages. The guidance mentioned that regulators believe it wouldn't be a burden for banks. You are near-sighted on that assumption.

We must be able to manage the bank in a way that insures long term profitability and stability so we can continue to serve our community. The very people you are trying to protect and so adamantly encourage us to serve, are going to be the ones that are negatively impacted most.

Thank you for your consideration.

Jay Victor

Jay Victor
Sr. Vice-President