Lonoke
101 S. Center
P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
Fax 501/676-5046

Carlisle
213 N. Court
P.O. Box 752
Carlisle, AR 72024-0752
870/552-7500
Fax 870/552-7714

Gurdon
100 E. Main
P.O. Box 446
Gurdon, AR 71743-0446
870/353-2521
Fax 870/353-2314

Fayetteville
2125 E. Joyce Blvd.
P.O. Box 8670
Fayetteville, AR 72703-0011
479/251-8900
Fax 479/251-7092

Heber Springs
1450 Southridge Road
P.O. Box 660
Heber Springs, AR 72543-0660
501/250-8400
Fax 501/362-8106

Springdale
1022 Jones Road
P.O. Box 8550
Springdale, AR 72766-8500
479/361-4400
Fax 479/361-5008

FSB Online Banking
www.firststatebk.com

"FDIC" and "RIN 3064-AD95"

October 5, 2012

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

Re: Basel III Capital Proposals

Dear Mr. Feldman:

Thank you for the opportunity to provide comment on the Basel III proposals [1] that were recently approved by the Federal Deposit Insurance Corporation, the Federal Reserve Board, and the Office of the Comptroller of the Currency. These proposals offer significant changes to the banking industry's capital structure, and they will impact all of us and the manner in which we'll conduct future business. Therefore it is vitally important that all aspects of these proposals are thoroughly reviewed, and their impact on the industry completely evaluated. Given the economic distress that this country has encountered over the past several years and the need to address its cause(s), the basis for the proposed capital changes have merit. Furthermore, many of the suggestions seem well-founded. However, when the proposals are enacted they will have some unintended consequences that will negatively impact a small bank like ours. This is the reason that we're calling your attention to such matters, and to respectfully request that you and the other bank regulatory authorities revisit certain aspects of the proposals and amend them to address the banking community and our concerns.

First State Bank is a state chartered, non-member financial institution that was established in 1935 and is headquartered in Lonoke, Arkansas. It is truly a community bank with total assets of about $265 million and branch locations in six Arkansas communities, four of which are rural areas. First State Bank helps support each of these communities via the banking services offered and the financial assistance it provides the local schools, churches, and civic and charitable organizations. Unfortunately, our early estimates suggest that for the bank to remain

[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.*

The proposed rules revising certain methodologies for calculating risk-weighted assets will also have an undesirable impact on our bank. If these changes were implemented at June 30, 2012, our bank's risk-weighted assets would increase by 10 percent ($17.5 million) from that which was reported in the June Call Report.

The risk weighting changes suggested for one-to-four family mortgage loans is of significant concern to us. Unlike the mortgage companies and the large financial institutions, which had sizable home mortgage lending operations, our bank did not exploit the mortgage business with complete disregard of common sense, practical lending, and obvious greed. First State Bank, like most all other community banks, maintained prudent loan underwriting in providing home financing for local residents. Furthermore, the home loans that this bank has originated are not packaged and sold on the secondary market, as many would not qualify because the property is located in rural communities. Instead these home loans have been kept "in-house" and are being serviced by our employees. To do this, we use loan products that have payment schedules (i.e., monthly principal and interest) that equate up to 30-year terms, but have maturities that range from two (2) to seven (7) years. The basis for this structure is to lessen the institution's interest rate risk. Neither we nor our regulators want the bank to be holding fixed rate, 30-year loans in a rising interest rate environment. This practice and deregulation are what destroyed the savings and loan industry. Now variable rate loans might mitigate interest rate risk; however, this type financing is unpopular when fixed rates for home loans are currently so low, and will likely stay that way until the housing industry and overall economy improve. If this proposal is left unchanged, our bank will need to revisit its home lending programs, because the proposed risk weighting for part of our one-to-four family home loan portfolio doubles and the other part triples.

We also believe that this proposed change could damage small communities as less credit will be available for home purchases, down payment requirements and lending costs will increase, and customers will find it harder to obtain mortgages meeting their needs and situations. The end result is further declines in home ownership, especially in smaller communities.

Although we take some exception to the risk weightings based on the loan-to-value percentage for the Category 1 residential mortgage loans, should you still find it necessary to implement the "Standardized Approach," we would strongly suggest that you include in Category 1, those one-to-four family home mortgage loans, which are structured on traditional repayment terms (i.e., up to 30 years), but have balloon features (i.e., a maturity date of 2 to 7 years). In our opinion, this amendment would greatly lessen the negative impact the current proposal would have on our bank and the communities it serves.

The proposed increased risk weightings for delinquent loans and obligations that finance acquisition development and construction (ADC) activities will also cause our bank's total risk weighted assets to rise and its capital ratios to fall. Credit risk in delinquent

loans and ADC advances have historically been addressed in loan loss reserves, and it seems reasonable that this should be continued.

Under the capital proposal, the risk weightings for delinquent loans will be at least 50 percent more than repossessed assets and other real estate owned. If implemented, this proposal will cause our bank to revisit the design and execution of work-out plans. It will also influence the longevity of such strategies, if they are put into action. Therefore, we foresee this proposal limiting opportunities for troubled borrowers to remedy their situations, thus resulting in more foreclosures. Such occurrences would be detrimental to our bank and the communities that it serves.

If the bank cannot produce sufficient earnings to increase or maintain enough capital to comply with the proposed changes, additional funding will need to be obtained from external sources. Attracting such resources is challenging enough in this environment; however, the capital proposals will make this even more difficult as the requirements will result in decreased investment returns, which will cause investors to seek more lucrative financial opportunities outside the banking industry. We don't believe that the Basel III proposals were intended to place our institution and many other community banks at a competitive disadvantage when raising equity, but they very well could.

We again want to thank you for the opportunity to comment on the Basel III proposals, as these changes will significantly impact the banking industry. As such, we would respectfully ask that you closely review our comments and those received from others, thoroughly weigh the consequences that the Basel III and Standardized Approach NPRs will have on the industry and our communities, and strongly reconsider foregoing some of these capital related modifications or at least amending them so that they are less intrusive.

As Chairman of a small community bank and a farmer in the Lonoke community, my responsibilities are three-fold: 1) ensuring that 59 employees have good stable employment; 2) providing small communities such as Lonoke, Heber Springs and Gurdon, Arkansas with banking services beneficial to the success of the economy; and 3) providing agricultural commodities necessary for economic growth. Throughout the latest recession, many of our customers have struggled financially which is relative to our bank and its current condition. I think that the proposed ruling departs from regulations favorable not just to our bank but to all small community banks. It is evident through field examiners that new regulations are implemented with a one-size-fits-all concept; therefore, small community banks should not be subject to the same complex standards required of the large banks on Wall Street.

With First State Bank being far removed from the subprime transactions that shook the foundation of the financial industry, Basel III and all it is implications are going to certainly impact our capital planning and ratios in addition to our current business model. Additionally, the consequences of Basel III with regards to interest charges, capital restrictions and the need to increase capital to cover variances in the bond portfolio will force us to alter the way we not only lend to our customers, but also invest in deposit

customers' money. Over the years, First State Bank has tailored is services to the customers in each community, but now the bank will have to show that it can withstand stress against a more complex and stringent capital mandate. The new provisions will only add another layer of complexity to an already challenging requirement. I truly hope that you take the time to listen to community bankers across America and adjust the implementation of these laws to help restore communities.

Sincerely,

Neil Bennett, Jr.

Lonoke
101 S. Center
P.O. Box 320
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which correlates into less funds being available to support community needs, to repay debt, and to compensate shareholders.

The proposal to apply unrealized gains and losses on "available for sale" (AFS) securities to Common Equity Tier 1 Capital is one of the proposed changes that would require greater earnings retention. These additional funds would be needed to bolster bank equity to compensate for the changes that regularly occur in the market value of AFS securities. Currently, the bank's entire investment portfolio is designated AFS and these assets' values readily fluctuate with the financial markets. For example, between year-end 2011 and March 30, 2012, the bank experienced a 337 percent change in the dollar volume of unrealized gain/loss on AFS securities; and between the first and second quarters of 2012 this change was 243 percent. These fluctuations moved the bank's Tier 1 Capital ratio by as much as 22 basis points. Mind you this has occurred in an ultra low and stable interest rate environment. Our analysis shows that market value changes will be much more pronounced and detrimental to the bank's capital position when the economy begins to improve and interest rates start to rise. The situation will be compounded by the additional government guaranteed mortgage backed securities that the bank has purchased during this period of very weak loan demand and at a time where we've experienced historic low yields for investments, including Treasury securities.

This situation could obviously be mitigated by reclassifying some of the bank's holdings to "held-to-maturity" (HTM). However, such action would reduce available liquidity since HTM securities cannot be sold prior to maturity, and it would require the bank to amend its contingency funding plans and seek alternative sources. The bank could also purchase securities that had a shorter maturity, but this would limit current and future profitability. Furthermore, if the entire banking industry employed a strategy of buying shorter term investments it would result in less funding for housing, government agencies, local municipalities, and school districts.

We heard in one of the early regulatory presentations about these proposals that the basis for recognizing, for capital purposes, unrealized gains/losses on AFS securities was based on the Financial Accounting Standards Board's (FASB) plan to change fair-value accounting. However, after much comment from the banking community and consideration of the potential impact such would have on financial institutions, the FASB has voted to relax its position on this matter. Furthermore, the International Accounting Standards Board's ruling eliminates the AFS category in 2015, which will result in securities being measured at amortized cost, just like loans.

Based on this information and the potential consequences of this proposal, we would respectfully ask that the regulatory agencies follow the FASB's lead and forego the requirement that unrealized gains and losses on AFS securities flow through the bank's equity. Should you still find it necessary to implement this proposal, we would strongly suggest that you exclude, from accumulated other comprehensive income, price fluctuations that occur in securities that have little or no credit risk (e.g., debt obligations of the U.S. government, government agencies, and government sponsored enterprises).

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With thirty years in banking and as a stockholder, I have seen many changes in how banks operate. The proposed changes have me extremely concerned about the impact they would bring to our communities and our industry. It is not just the jeopardy of the small community bank, but the ripple effect that needs to be considered. These changes could cause

banks to experience considerable hardship to the point they could not continue to operate which in turn would cause consumers' faith in the banking industry to fail.

We again want to thank you for the opportunity to comment on the Basel III proposals, as these changes will significantly impact the banking industry. As such, we would respectfully ask that you closely review our comments and those received from others, thoroughly weigh the consequences that the Basel III and Standardized Approach NPRs will have on the industry and our communities, and strongly reconsider foregoing some of these capital related modifications or at least amending them so that they are less intrusive.

Your consideration of these requests will be greatly appreciated.

Sincerely,

Julie Turney
Vice President – Loan Officer & Deposit Administration
First State Bank

FIRST STATE BANK

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P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
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In my fifteen year banking career I have experienced many regulatory changes, but this proposal, if implemented may have far reaching consequences for small banks as we may no longer be able to compete. Small banks are still favored in most communities but we need to be able to meet their lending needs and this proposal would greatly impact our ability to do so. Our local economies can not stand the possible loss of community banks and the jobs they provide.

We again want to thank you for the opportunity to comment on the Basel III proposals, as these changes will significantly impact the banking industry. As such, we would respectfully ask that you closely review our comments and those received from others, thoroughly weigh the consequences that the Basel III and Standardized Approach NPRs will have on the industry and our communities, and strongly reconsider foregoing some of these capital related modifications or at least amending them so that they are less intrusive.

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Brenda Carr

Brenda Carr
AVP Loan Administration

Financial Center

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This situation could obviously be mitigated by reclassifying some of the bank's holdings to "held-to-maturity" (HTM). However, such action would reduce available liquidity since HTM securities cannot be sold prior to maturity, and it would require the bank to amend its contingency funding plans and seek alternative sources. The bank could also purchase securities that had a shorter maturity, but this would limit current and future profitability. Furthermore, if the entire banking industry employed a strategy of buying shorter term investments it would result in less funding for housing, government agencies, local municipalities, and school districts.

We heard in one of the early regulatory presentations about these proposals that the basis for recognizing, for capital purposes, unrealized gains/losses on AFS securities was based on the Financial Accounting Standards Board's (FASB) plan to change fair-value accounting. However, after much comment from the banking community and consideration of the potential impact such would have on financial institutions, the FASB has voted to relax its position on this matter. Furthermore, the International Accounting Standards Board's ruling eliminates the AFS category in 2015, which will result in securities being measured at amortized cost, just like loans.

Based on this information and the potential consequences of this proposal, we would respectfully ask that the regulatory agencies follow the FASB's lead and forego the requirement that unrealized gains and losses on AFS securities flow through the bank's equity. Should you still find it necessary to implement this proposal, we would strongly suggest that you exclude, from accumulated other comprehensive income, price

fluctuations that occur in securities that have little or no credit risk (e.g., debt obligations of the U.S. government, government agencies, and government sponsored enterprises).

The proposed rules revising certain methodologies for calculating risk-weighted assets will also have an undesirable impact on our bank. If these changes were implemented at June 30, 2012, our bank's risk-weighted assets would increase by 10 percent ($17.5 million) from that which was reported in the June Call Report.

The risk weighting changes suggested for one-to-four family mortgage loans is of significant concern to us. Unlike the mortgage companies and the large financial institutions, which had sizable home mortgage lending operations, our bank did not exploit the mortgage business with complete disregard of common sense, practical lending, and obvious greed. First State Bank, like most all other community banks, maintained prudent loan underwriting in providing home financing for local residents. Furthermore, the home loans that this bank has originated are not packaged and sold on the secondary market, as many would not qualify because the property is located in rural communities. Instead these home loans have been kept "in-house" and are being serviced by our employees. To do this, we use loan products that have payment schedules (i.e., monthly principal and interest) that equate up to 30-year terms, but have maturities that range from two (2) to seven (7) years. The basis for this structure is to lessen the institution's interest rate risk. Neither we nor our regulators want the bank to be holding fixed rate, 30-year loans in a rising interest rate environment. This practice and deregulation are what destroyed the savings and loan industry. Now variable rate loans might mitigate interest rate risk; however, this type financing is unpopular when fixed rates for home loans are currently so low, and will likely stay that way until the housing industry and overall economy improve. If this proposal is left unchanged, our bank will need to revisit its home lending programs, because the proposed risk weighting for part of our one-to-four family home loan portfolio doubles and the other part triples.

We also believe that this proposed change could damage small communities as less credit will be available for home purchases, down payment requirements and lending costs will increase, and customers will find it harder to obtain mortgages meeting their needs and situations. The end result is further declines in home ownership, especially in smaller communities.

Although we take some exception to the risk weightings based on the loan-to-value percentage for the Category 1 residential mortgage loans, should you still find it necessary to implement the "Standardized Approach," we would strongly suggest that you include in Category 1, those one-to-four family home mortgage loans, which are structured on traditional repayment terms (i.e., up to 30 years), but have balloon features (i.e., a maturity date of 2 to 7 years). In our opinion, this amendment would greatly lessen the negative impact the current proposal would have on our bank and the communities it serves.

The proposed increased risk weightings for delinquent loans and obligations that finance acquisition development and construction (ADC) activities will also cause our bank's total risk weighted assets to rise and its capital ratios to fall. Credit risk in delinquent loans and ADC advances have historically been addressed in loan loss reserves, and it seems reasonable that this should be continued.

Under the capital proposal, the risk weightings for delinquent loans will be at least 50 percent more than repossessed assets and other real estate owned. If implemented, this proposal will cause our bank to revisit the design and execution of work-out plans. It will also influence the longevity of such strategies, if they are put into action. Therefore, we foresee this proposal limiting opportunities for troubled borrowers to remedy their situations, thus resulting in more foreclosures. Such occurrences would be detrimental to our bank and the communities that it serves.

If the bank cannot produce sufficient earnings to increase or maintain enough capital to comply with the proposed changes, additional funding will need to be obtained from external sources. Attracting such resources is challenging enough in this environment; however, the capital proposals will make this even more difficult as the requirements will result in decreased investment returns, which will cause investors to seek more lucrative financial opportunities outside the banking industry. We don't believe that the Basel III proposals were intended to place our institution and many other community banks at a competitive disadvantage when raising equity, but they very well could.

We again want to thank you for the opportunity to comment on the Basel III proposals, as these changes will significantly impact the banking industry. As such, we would respectfully ask that you closely review our comments and those received from others, thoroughly weigh the consequences that the Basel III and Standardized Approach NPRs will have on the industry and our communities, and strongly reconsider foregoing some of these capital related modifications or at least amending them so that they are less intrusive.

As an Executive Vice President, investor and shareholder of a small community Bank; I think that the proposed ruling will move away from banking standards beneficial not just to our bank but to all small community banks. First State Bank is a practical bank with six locations and operates primarily in small business lending. The rules of Basel III are complex and will have a widespread negative effect on community banks. Our bank should not be subject to the same complex standards required of larger and riskier banks such as those on Wall Street. I have discovered that when new regulations are implemented, the regulators' interpretations mean one-size-fits-all. However, small community banks and big Wall Street banks are drastically different. Laws that are designed which have a global affect on all banks make it difficult for smaller banks to have any type of success. Basel III is going to certainly impact our capital, current business model, and the communities we serve.

"FDIC" and "RIN 3064-AD95"

Your consideration of these requests will be greatly appreciated.

Sincerely,

John H. Duke III
Executive Vice President

Lonoke
101 S. Center
P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
Fax 501/676-5046

Carlisle
213 N. Court
P.O. Box 752
Carlisle, AR 72024-0752
870/552-7500
Fax 870/552-7714

Gurdon
100 E. Main
P.O. Box 446
Gurdon, AR 71743-0446
870/353-2521
Fax 870/353-2314

Fayetteville
2125 E. Joyce Blvd.
P.O. Box 8670
Fayetteville, AR 72703-0011
479/251-8900
Fax 479/251-7092

Heber Springs
1450 Southridge Road
P.O. Box 660
Heber Springs, AR 72543-0660
501/250-8400
Fax 501/362-8106

Springdale
1022 Jones Road
P.O. Box 8550
Springdale, AR 72766-8500
479/361-4400
Fax 479/361-5008

FSB Online Banking
www.firststatebk.com

September 4, 2012

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

Re: Basel III Capital Proposals

Dear Mr. Feldman:

Thank you for the opportunity to provide comment on the Basel III proposals[1] that were recently approved by the Federal Deposit Insurance Corporation, the Federal Reserve Board, and the Office of the Comptroller of the Currency. These proposals offer significant changes to the banking industry's capital structure, and they will impact all of us and the manner in which we'll conduct future business. Therefore it is vitally important that all aspects of these proposals are thoroughly reviewed, and their impact on the industry completely evaluated. Given the economic distress that this country has encountered over the past several years and the need to address its cause(s), the basis for the proposed capital changes have merit. Furthermore, many of the suggestions seem well-founded. However, when the proposals are enacted they will have some unintended consequences that will negatively impact a small bank like ours. This is the reason that we're calling your attention to such matters, and to respectfully request that you and the other bank regulatory authorities revisit certain aspects of the proposals and amend them to address the banking community and our concerns.

First State Bank is a state chartered, non-member financial institution that was established in 1935 and is headquartered in Lonoke, Arkansas. It is truly a community bank with total assets of about $265 million and branch locations in six Arkansas communities, four of which are rural areas. First State Bank helps support each of these communities via the banking services offered and the financial assistance it provides the local schools, churches, and civic and charitable organizations. Unfortunately, our early estimates suggest that for the bank to remain in compliance with all the proposed capital requirements, it will need to retain more of its earnings, which correlates into less funds being available to support community needs, to repay debt, and to compensate shareholders.

The proposal to apply unrealized gains and losses on "available for sale" (AFS) securities to Common Equity Tier 1 Capital is one of the proposed changes that

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Lonoke
101 S. Center
P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
Fax 501/676-5046

Carlisle
213 N. Court
P.O. Box 752
Carlisle, AR 72024-0752
870/552-7500
Fax 870/552-7714

Gurdon
100 E. Main
P.O. Box 446
Gurdon, AR 71743-0446
870/353-2521
Fax 870/353-2314

Fayetteville
2125 E. Joyce Blvd.
P.O. Box 8670
Fayetteville, AR 72703-0011
479/251-8900
Fax 479/251-7092

Heber Springs
1450 Southridge Road
P.O. Box 660
Heber Springs, AR 72543-0660
501/250-8400
Fax 501/362-8106

Springdale
1022 Jones Road
P.O. Box 8550
Springdale, AR 72766-8500
479/361-4400
Fax 479/361-5008

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We heard in one of the early regulatory presentations about these proposals that the basis for recognizing, for capital purposes, unrealized gains/losses on AFS securities was based on the Financial Accounting Standards Board's (FASB) plan to change fair-value accounting. However, after much comment from the banking community and consideration of the potential impact such would have on financial institutions, the FASB has voted to relax its position on this matter. Furthermore, the International Accounting Standards Board's ruling eliminates the AFS category in 2015, which will result in securities being measured at amortized cost, just like loans.

Based on this information and the potential consequences of this proposal, we would respectfully ask that the regulatory agencies follow the FASB's lead and forego the requirement that unrealized gains and losses on AFS securities flow through the bank's equity. Should you still find it necessary to implement this proposal, we would strongly suggest that you exclude, from accumulated other comprehensive income, price fluctuations that occur in securities that have little or no credit risk (e.g., debt obligations of the U.S. government, government agencies, and government sponsored enterprises).

The proposed rules revising certain methodologies for calculating risk-weighted assets will also have an undesirable impact on our bank. If these changes were implemented at June 30, 2012, our bank's risk-weighted assets would increase

Lonoke
101 S. Center
P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
Fax 501/676-5046

Carlisle
213 N. Court
P.O. Box 752
Carlisle, AR 72024-0752
870/552-7500
Fax 870/552-7714

Gurdon
100 E. Main
P.O. Box 446
Gurdon, AR 71743-0446
870/353-2521
Fax 870/353-2314

Fayetteville
2125 E. Joyce Blvd.
P.O. Box 8670
Fayetteville, AR 72703-0011
479/251-8900
Fax 479/251-7092

Heber Springs
1450 Southridge Road
P.O. Box 660
Heber Springs, AR 72543-0660
501/250-8400
Fax 501/362-8106

Springdale
1022 Jones Road
P.O. Box 8550
Springdale, AR 72766-8500
479/361-4400
Fax 479/361-5008

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We also believe that this proposed change could damage small communities as less credit will be available for home purchases, down payment requirements and lending costs will increase, and customers will find it harder to obtain mortgages meeting their needs and situations. The end result is further declines in home ownership, especially in smaller communities.

Although we take some exception to the risk weightings based on the loan-to-value percentage for the Category 1 residential mortgage loans, should you still find it necessary to implement the "Standardized Approach," we would strongly suggest that you include in Category 1, those one-to-four family home mortgage loans, which are structured on traditional repayment terms (i.e., up to 30 years), but have balloon features (i.e., a maturity date of 2 to 7 years). In our opinion, this amendment would greatly lessen the negative impact the current proposal would have on our bank and the communities it serves.

The proposed increased risk weightings for delinquent loans and obligations that finance acquisition development and construction (ADC) activities will also cause our bank's total risk weighted assets to rise and its capital ratios to fall. Credit risk in delinquent loans and ADC advances have historically been addressed in loan loss reserves, and it seems reasonable that this should be continued.

Lonoke
101 S. Center
P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
Fax 501/676-5046

Carlisle
213 N. Court
P.O. Box 752
Carlisle, AR 72024-0752
870/552-7500
Fax 870/552-7714

Gurdon
100 E. Main
P.O. Box 446
Gurdon, AR 71743-0446
870/353-2521
Fax 870/353-2314

Fayetteville
2125 E. Joyce Blvd.
P.O. Box 8670
Fayetteville, AR 72703-0011
479/251-8900
Fax 479/251-7092

Heber Springs
1450 Southridge Road
P.O. Box 660
Heber Springs, AR 72543-0660
501/250-8400
Fax 501/362-8106

Springdale
1022 Jones Road
P.O. Box 8550
Springdale, AR 72766-8500
479/361-4400
Fax 479/361-5008

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Under the capital proposal, the risk weightings for delinquent loans will be at least 50 percent more than repossessed assets and other real estate owned. If implemented, this proposal will cause our bank to revisit the design and execution of work-out plans. It will also influence the longevity of such strategies, if they are put into action. Therefore, we foresee this proposal limiting opportunities for troubled borrowers to remedy their situations, thus resulting in more foreclosures. Such occurrences would be detrimental to our bank and the communities that it serves.

If the bank cannot produce sufficient earnings to increase or maintain enough capital to comply with the proposed changes, additional funding will need to be obtained from external sources. Attracting such resources is challenging enough in this environment; however, the capital proposals will make this even more difficult as the requirements will result in decreased investment returns, which will cause investors to seek more lucrative financial opportunities outside the banking industry. We don't believe that the Basel III proposals were intended to place our institution and many other community banks at a competitive disadvantage when raising equity, but they very well could.

Many employees as myself of First State Bank own stock in Lonoke Bancshares, Inc. which is the holding company of First State Bank. Some employees own no more than one or two shares which are significant to them. They invested in a community bank because they feel strong about the bank giving back to the community in support of local public, civic and charitable organizations. Community banks help the area grow and prosper. As the bank grows then the employee investment grows. With the above mentioned Basel III proposals, the banks capital could be adversely affected and could seriously jeopardize their investment in the bank and community.

We again want to thank you for the opportunity to comment on the Basel III proposals, as these changes will significantly impact the banking industry. As such, we would respectfully ask that you closely review our comments and those received from others, thoroughly weigh the consequences that the Basel III and Standardized Approach NPRs will have on the industry and our communities, and strongly reconsider foregoing some of these capital related modifications or at least amending them so that they are less intrusive.

Your consideration of these requests will be greatly appreciated.

Sincerely,

Keith McHan

Keith McHan
SR. Vice President
First State Bank

Lonoke
101 S. Center
P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
Fax 501/676-5046

Carlisle
213 N. Court
P.O. Box 752
Carlisle, AR 72024-0752
870/552-7500
Fax 870/552-7714

Gurdon
100 E. Main
P.O. Box 446
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P.O. Box 8670
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Springdale, AR 72766-8500
479/361-4400
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September 4, 2012

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

Re: Basel III Capital Proposals

Dear Mr. Feldman:

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We again want to thank you for the opportunity to comment on the Basel III proposals, as these changes will significantly impact the banking industry. As such, we would respectfully ask that you closely review our comments and those received from others, thoroughly weigh the consequences that the Basel III and Standardized Approach NPRs will have on the industry and our communities, and strongly reconsider foregoing some of these capital related modifications or at least amending them so that they are less intrusive.

As a Director of First State Bank and a retired Insurance Agent, I know First State Bank to be a common-sense bank with total assets of $256 million, six locations and operating primarily in small business lending. Our bank should not be subject to the same multifaceted criteria required of larger and riskier banks. Basel III is going to certainly impact and present more volatility in regulatory capital. I think that this proposed rule will also place additional burden on our ability to raise capital when needed especially in the small communities that our bank serves such as Lonoke, Gurdon and Heber Springs, Arkansas.

Your consideration of these requests will be greatly appreciated.

Sincerely,

Robert Bailey

FIRST STATE BANK

Lonoke
101 S. Center
P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
Fax 501/676-5046

Carlisle
213 N. Court
P.O. Box 752
Carlisle, AR 72024-0752
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Fax 870/552-7714

Gurdon
100 E. Main
P.O. Box 446
Gurdon, AR 71743-0446
870/353-2521
Fax 870/353-2314

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P.O. Box 8670
Fayetteville, AR 72703-0011
479/251-8900
Fax 479/251-7092

Heber Springs
1450 Southridge Road
P.O. Box 660
Heber Springs, AR 72543-0660
501/250-8400
Fax 501/362-8106

Springdale
1022 Jones Road
P.O. Box 8550
Springdale, AR 72766-8500
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"FDIC" and "RIN 3064-AD95"

September 4, 2012

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

Re: Basel III Capital Proposals

Dear Mr. Feldman:

Thank you for the opportunity to provide comment on the Basel III proposals [1] that were recently approved by the Federal Deposit Insurance Corporation, the Federal Reserve Board, and the Office of the Comptroller of the Currency. These proposals offer significant changes to the banking industry's capital structure, and they will impact all of us and the manner in which we'll conduct future business. Therefore it is vitally important that all aspects of these proposals are thoroughly reviewed, and their impact on the industry completely evaluated. Given the economic distress that this country has encountered over the past several years and the need to address its cause(s), the basis for the proposed capital changes have merit. Furthermore, many of the suggestions seem well-founded. However, when the proposals are enacted they will have some unintended consequences that will negatively impact a small bank like ours. This is the reason that we're calling your attention to such matters, and to respectfully request that you and the other bank regulatory authorities revisit certain aspects of the proposals and amend them to address the banking community and our concerns.

First State Bank is a state chartered, non-member financial institution that was established in 1935 and is headquartered in Lonoke, Arkansas. It is truly a community bank with total assets of about $265 million and branch locations in six Arkansas communities, four of which are rural areas. First State Bank helps support each of these communities via the banking services offered and the financial assistance it provides the local schools, churches,

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.*

FIRST STATE BANK

Lonoke
101 S. Center
P.O. Box 320
Lonoke, AR 72086-0320
501/676-3106
Fax 501/676-5046

Carlisle
213 N. Court
P.O. Box 752
Carlisle, AR 72024-0752
870/552-7500
Fax 870/552-7714

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and civic and charitable organizations. Unfortunately, our early estimates suggest that for the bank to remain in compliance with all the proposed capital requirements, it will need to retain more of its earnings, which correlates into less funds being available to support community needs, to repay debt, and to compensate shareholders.

The proposal to apply unrealized gains and losses on "available for sale" (AFS) securities to Common Equity Tier 1 Capital is one of the proposed changes that would require greater earnings retention. These additional funds would be needed to bolster bank equity to compensate for the changes that regularly occur in the market value of AFS securities. Currently, the bank's entire investment portfolio is designated AFS and these assets' values readily fluctuate with the financial markets. For example, between year-end 2011 and March 30, 2012, the bank experienced a 337 percent change in the dollar volume of unrealized gain/loss on AFS securities; and between the first and second quarters of 2012 this change was 243 percent. These fluctuations moved the bank's Tier 1 Capital ratio by as much as 22 basis points. Mind you this has occurred in an ultra low and stable interest rate environment. Our analysis shows that market value changes will be much more pronounced and detrimental to the bank's capital position when the economy begins to improve and interest rates start to rise. The situation will be compounded by the additional government guaranteed mortgage backed securities that the bank has purchased during this period of very weak loan demand and at a time where we've experienced historic low yields for investments, including Treasury securities.

This situation could obviously be mitigated by reclassifying some of the bank's holdings to "held-to-maturity" (HTM). However, such action would reduce available liquidity since HTM securities cannot be sold prior to maturity, and it would require the bank to amend its contingency funding plans and seek alternative sources. The bank could also purchase securities that had a shorter maturity, but this would limit current and future profitability. Furthermore, if the entire banking industry employed a strategy of buying shorter term investments it would result in less funding for housing, government agencies, local municipalities, and school districts.

We heard in one of the early regulatory presentations about these proposals that the basis for recognizing, for capital purposes, unrealized gains/losses on AFS securities was based on the Financial Accounting Standards Board's (FASB) plan to change fair-value accounting. However, after much comment from the

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banking community and consideration of the potential impact such would have on financial institutions, the FASB has voted to relax its position on this matter. Furthermore, the International Accounting Standards Board's ruling eliminates the AFS category in 2015, which will result in securities being measured at amortized cost, just like loans.

Based on this information and the potential consequences of this proposal, we would respectfully ask that the regulatory agencies follow the FASB's lead and forego the requirement that unrealized gains and losses on AFS securities flow through the bank's equity. Should you still find it necessary to implement this proposal, we would strongly suggest that you exclude, from accumulated other comprehensive income, price fluctuations that occur in securities that have little or no credit risk (e.g., debt obligations of the U.S. government, government agencies, and government sponsored enterprises).

The proposed rules revising certain methodologies for calculating risk-weighted assets will also have an undesirable impact on our bank. If these changes were implemented at June 30, 2012, our bank's risk-weighted assets would increase by 10 percent ($17.5 million) from that which was reported in the June Call Report.

The risk weighting changes suggested for one-to-four family mortgage loans is of significant concern to us. Unlike the mortgage companies and the large financial institutions, which had sizable home mortgage lending operations, our bank did not exploit the mortgage business with complete disregard of common sense, practical lending, and obvious greed. First State Bank, like most all other community banks, maintained prudent loan underwriting in providing home financing for local residents. Furthermore, the home loans that this bank has originated are not packaged and sold on the secondary market, as many would not qualify because the property is located in rural communities. Instead these home loans have been kept "in-house" and are being serviced by our employees. To do this, we use loan products that have payment schedules (i.e., monthly principal and interest) that equate up to 30-year terms, but have maturities that range from two (2) to seven (7) years. The basis for this structure is to lessen the institution's interest rate risk. Neither we nor our regulators want the bank to be holding fixed rate, 30-year loans in a rising interest rate environment. This practice and deregulation are what destroyed the savings and loan industry. Now variable rate loans might mitigate interest rate risk; however, this type financing is unpopular when fixed rates for home loans are currently so low,

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and will likely stay that way until the housing industry and overall economy improve. If this proposal is left unchanged, our bank will need to revisit its home lending programs, because the proposed risk weighting for part of our one-to-four family home loan portfolio doubles and the other part triples.

We also believe that this proposed change could damage small communities as less credit will be available for home purchases, down payment requirements and lending costs will increase, and customers will find it harder to obtain mortgages meeting their needs and situations. The end result is further declines in home ownership, especially in smaller communities.

Although we take some exception to the risk weightings based on the loan-to-value percentage for the Category 1 residential mortgage loans, should you still find it necessary to implement the "Standardized Approach," we would strongly suggest that you include in Category 1, those one-to-four family home mortgage loans, which are structured on traditional repayment terms (i.e., up to 30 years), but have balloon features (i.e., a maturity date of 2 to 7 years). In our opinion, this amendment would greatly lessen the negative impact the current proposal would have on our bank and the communities it serves.

The proposed increased risk weightings for delinquent loans and obligations that finance acquisition development and construction (ADC) activities will also cause our bank's total risk weighted assets to rise and its capital ratios to fall. Credit risk in delinquent loans and ADC advances have historically been addressed in loan loss reserves, and it seems reasonable that this should be continued.

Under the capital proposal, the risk weightings for delinquent loans will be at least 50 percent more than repossessed assets and other real estate owned. If implemented, this proposal will cause our bank to revisit the design and execution of work-out plans. It will also influence the longevity of such strategies, if they are put into action. Therefore, we foresee this proposal limiting opportunities for troubled borrowers to remedy their situations, thus resulting in more foreclosures. Such occurrences would be detrimental to our bank and the communities that it serves.

If the bank cannot produce sufficient earnings to increase or maintain enough capital to comply with the proposed changes, additional funding will need to be obtained from external sources. Attracting such resources is challenging enough in this environment; however, the capital proposals will make this even

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more difficult as the requirements will result in decreased investment returns, which will cause investors to seek more lucrative financial opportunities outside the banking industry. We don't believe that the Basel III proposals were intended to place our institution and many other community banks at a competitive disadvantage when raising equity, but they very well could.

We again want to thank you for the opportunity to comment on the Basel III proposals, as these changes will significantly impact the banking industry. As such, we would respectfully ask that you closely review our comments and those received from others, thoroughly weigh the consequences that the Basel III and Standardized Approach NPRs will have on the industry and our communities, and strongly reconsider foregoing some of these capital related modifications or at least amending them so that they are less intrusive.

As an employee of First State Bank, my job is very important to me. The bank is also very important to my community. Please consider all the people of the communities that community banks serve.

Your consideration of these requests will be greatly appreciated.

Sincerely,

Steven Orsburn