HomeTown Bank

October 18, 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 approved by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (collectively the "banking agencies").

HomeTown Bank is headquartered in Roanoke, VA and was formed in November 2005. We have grown to $375 million in assets during the past seven years. We are publicly traded and a registrant of the U.S. Securities and Exchange Commission (SEC). With five branches located in Roanoke, Smith Mountain Lake and the New River Valley, our local bankers, managers, and staff help people and businesses prosper with a full range of products and services delivered with unsurpassed customer service. HomeTown Bank is part of the fabric of our community. We work here, we invest here, and we volunteer here. As a community bank, we consider it our responsibility to make the community a better place for everyone. That's the vision our founders had in mind in 2005 when they said: "We are a locally owned and managed bank committed to providing quality financial services to local consumers, professionals and small and medium-size businesses. We are motivated by our community's needs and our desire to provide a reasonable return to our stockholders."

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[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.*

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Discussed below are four major areas of concern with the Basel III Capital Proposals that will negatively impact HomeTown Bank and the communities in which we operate. These are not the only areas of concern, but in the interest of time, are considered the most significant:

I. First is the overall impracticality of requiring community banks to comply with the proposals. While the proposals may be appropriate for very large domestic banks and foreign banks that have historically been allowed to operate with less capital than community banks, they are not appropriate to implement in a community bank structure that we have in place in the United States. Community banks did not engage in the highly leveraged activities that severely depleted capital levels of the largest banks and created panic in the financial markets. Basel III is an international accord designed to improve capital levels in all banks across the world. It should be noted that other countries do not have a community banking industry like the one that exists, currently, in the United States. That difference makes it highly undesirable, unworkable, and untenable to adopt a one-size-fits-all capital strategy and compel implementation in this country.

II. Second is the inclusion of unrealized gains and losses on available-for-sale securities in the common equity Tier 1 computation. HomeTown Bank has a very conservative investment philosophy. Our bond portfolio totals approximately $65 million as of September 2012. The portfolio is all Available for Sale (AFS) and primarily made up of Agency, Mortgage Back, and Municipal bonds. These bonds are thoroughly researched prior to purchase and have little, if any, risk of loss, but are subject to interest rate risk, which we monitor and manage very closely.

    Our country is in an unprecedented period of low interest rates. Banks currently have significant unrealized gains in their investment portfolios. The proposals would serve to increase regulatory capital in the short term; however, as interest rates will unequivocally rise in the future, this inflated capital would quickly be depleted and dramatically move in the opposite direction. Our bond portfolio was in an unrealized gain position of approximately $1.5 million net of income tax in September 2012. An increase in interest rates of 100, 200, and 300 basis points would have a negative after-tax impact of approximately $0.13, $1.87, and $3.73 million, respectively, to the proposed capital computations. Our most recent publically available total bank equity capital was approximately $34.1 million as of June 30, 2012. Our Tier 1 leverage, Tier 1 risk-based capital, and Total risk-based capital ratios as of the same date were 8.72%, 11.84%, and 13.09%, respectively. Negative impacts to regulatory capital ratios will occur as a result of recognizing these unrealized losses while there are no changes to the Bank's actual equity and risk profile. This proposal will introduce a significant amount of cyclicality and volatility into the banking system which should not be the goal of the banking agencies.

III. Third is the increased risk weighting on delinquent loans. We are already required to analyze delinquent loans and trends in delinquent loans through our Allowance for Loan Loss analysis. This is a highly scrutinized area reviewed during every examination and by our independent external CPA firm annually. Requiring additional risk weighting on delinquent loans will result in a doubling effect of decreasing capital ratios while also decreasing capital by building reserves for estimates of future losses. Another unintended consequence of this proposal is that we would increase our aggressiveness in moving these delinquent loans off the balance sheet as opposed to working with borrowers to restructure loans or resolve issues.

IV. Fourth is the overall complexity and requirements to interpret and implement the proposals. The scope and granularity of the proposed rules will require the collection and reporting of new information in order to calculate the risk weights of assets for our institution. For example, the requirements for risk weighting real estate loans into category one and two and by loan-to-value percentage are going to necessitate massive, labor intensive and expensive work in our management information systems. We will at a minimum need to acquire new software and install new systems in order to comply with the complex calculations. Additionally, we will likely need to outsource all or part of the implementation to a third party. It will cause HomeTown Bank to incur new costs and regulatory burden in an already over-regulated environment with no benefit to our customers or community.

Numerous laws and regulations passed by congress and required by banking agencies have reduced income opportunities for community banks. The inability to generate appropriate returns on capital is making raising capital at most community banks nearly impossible. To impose additional regulatory burden and demand increased capital requirements on community banks during this tumultuous banking environment is fiendish as we strive to improve and grow the United States economy. Community banks should be allowed to continue using the current Basel II framework for computing their capital requirements. This model contributes to the success of community banks all over the United States through practical, common sense approaches to managing risk. Thank you for your time and consideration.

Respectfully submitted,

Michele A. Vanover

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AVP, Loan Review Officer