From: Fayette County National Bank, Domigene Yellets

Proposal: 1442 (RIN 7100-AD 87) Regs H, Q, & Y Regulatory Capital Rules

Subject: Regs H & Y Regulatory Capital Proposals

Comments:

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

Oct 22, 2012

Re: Basel III Capital Proposals

Thank you for the opportunity to comment on the Basel III proposals 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.

Fayette County National Bank is a $90 million bank with 4 locations in Fayette County West Virginia, and has been in existence since 1900. We have always had capital levels greatly in excess minimum requirements. But this could change under Basel III,

We fully support appropriate and strong capitalization of the nation's banks as well as all financial institutions. This can be accomplished by simply raising minimum capital requirements. However, to require community banks to comply with capital requirements that were clearly meant for large global banks is an unjustified burden on us due to the complexity of the rules. Managing the risk of community banks is best served by adequate regulatory oversight. Requiring additional and adequate capital for higher-risk international and too-big-to-fail banks is appropriate, and these are the banks to which Basel III is intended.

It appears to us that community banks in general are seeing an increase in regulatory oversight which is not a result of any specific issues or mismanagement, but rather a "one size fits all" regulatory response to the financial crisis caused by the mistakes of the too-big-to-fail banks and non-bank financial institutions plus inadequate regulatory oversight on these entities. Community banks did not engage in the risky activities that caused systemic problems in financial markets. Community banks operate in a conservative manner designed to serve our customers in our respective communities on a long-term basis. We do this by successfully managing our risk in compliance with existing regulatory expectations, such as maintaining an adequate ALLR, adequately managing our IRR, and striving to achieve adequate CAMELS ratings. Examiners currently conduct quarterly oversight of community banks, and have the ability to require adjustment to bank capital levels. Our regulator is familiar
with our bank and the risk we have, and should know how much capital we need - not some complex, time-consuming formula designed for large global banks

We would like to comment specifically on the following:

Available-for-Sale gains/losses inclusion in Tier I capital

In our situation, we currently have a $1.7MM gain in our AFS securities portfolio. With interest rates so low, an eventual increase in market rates is unavoidable. This gain will, of course, shift to a multi-million dollar loss and our capital will be negatively affected.

If this rule is adopted, a large portion of banks will probably switch from AFS to HTM securities. As with most community banks, we use our AFS investments to manage IRR sensitivity by increasing or decreasing cash flows when necessary due to market changes. This will also limit our ability to have liquid assets and will decrease our liquidity position. This provision will certainly change our investing behavior as well as those of other banks, and country-wide could have a negative impact on the investment market.

Temporary valuations change due to market interest rate changes, not credit risk.

Increased risk-weighting for residential mortgages

Our residential mortgages make up over 70% of our loan portfolio. In our area we have not had a major downturn in home prices and only a slight increase in foreclosures. Our ALLR is more than adequate to absorb any unusual losses in this area due to the constant monitoring of our past dues and any possible losses. The Basel III risk weighting of residential mortgages unfairly increases the current risk weighting. It will require a large amount of time to review our residential mortgages to assign an initial risk weight and continually re-evaluate the risk weights based on changing collateral values and other required risk factors. Hiring of additional staff plus increased costs to change coding in our processing systems will of course increase the cost of booking these loans which will be passed on to the customer. When you multiply this effect across the country, this can have an unintended consequence of slowing the housing market. Plus penalizing high LTV loans with higher risk weights will only curb future lending.

Increasing the risk weights for residential balloon loans will unfairly penalize community banks like us who offer these loan products to customers, and will only decrease the availability of loan products to customers who demand these products as well as decrease financing options for many. We will either be forced to offer these loans at a higher cost or be forced to only offer longer term, fixed rate loans - which will only increase our long-term interest rate risk. So, to us, this appears to be a catch-22 type of situation.

Increase risk weights on delinquent loans

Banks already have a classification system for risk of loss in their loan portfolios, and set aside reserves for loans that could be a loss to the bank. By increase the amount of capital we hold based on past due status of loans, we are being required to impact capital twice. The risk related to problem loans are already being managed through the ALLR in compliance with required guidance in this area plus regular regulatory review - not by adding these to a capital requirement.

In conclusion, Basel III requirements as applied to community banks do more harm than good when it comes to managing risk, and can have far reaching, long term unintended consequences. None of the requirements of Basel III will do anything to help community banks serve our customers by making loans and investing in our community. And again, community banks are not the ones who caused any of the financial problems over the last few years and should not be made to comply with requirements that were meant for systemically significant banks. Community banks are not the same as too-big-to-fail banks and should not be regulated as such. Simply raising minimum capital levels is the solution for community banks - not adding more complex compliance & regulatory requirements that will be costly and extremely time consuming plus have a negative impact on our customers and the economy.

Thanks for taking the time to read my comments, and hopefully you will listen to community banks on this issue.

Mrs. Domigene Yellets
Fayette County National Bank