October 11, 2012 **Cabarrus Bank & Trust**

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W
Washington, DC 20219.

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, NW
Washington, DC 20219

Re: Basel III Proposals

Ladies and Gentlemen:

Cabarrus Bank & Trust appreciates the opportunity to submit comments in regards to Basel III's proposed rulemaking (NPRs) [1] that were recently approved and released on June 12, 2012 by the joint agencies ("the agencies") including: the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation.

Cabarrus Bank & Trust is a community-owned and operated full service bank that is part of the Uwharrie Capital Corp family of financial services. Our four major business groups are Corporate Banking, Personal Banking, Convenience Banking and Wealth Management. Cabarrus Bank & Trust has a developed and successful core strategy of building deep, long-term customer relationships in which we are a trusted advisor and primary banking partner. Our company is community focused with an emphasis on local decision-making and strong community support. We focus on the well being of our community, delivering products and services with the best interest of our customers in mind.

We recognize the massive challenges that the agencies face developing a system that accurately reflects risks across the universe of financial institutions from small community banks to Bank of America, all which are part of the same system. Cabarrus Bank & Trust supports the agencies' desire to address the apparent capital shortage in the industry. As we have considered the proposals and

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[1]NPRs are: 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 and Disclosure Requirements; and Regulatory Capital Rules: Advanced Approaches Risk-based Capital Rules; Market Risk Capital Rule.

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their implications within the industry, we believe several of these changes, in practice, will counteract the intentions of the agencies.

The areas that we feel will have the highest negative impact to Cabarrus Bank & Trust, as well as all other community banks, are:

- Accumulated Other Comprehensive Income (AOCI) as a component of Tier 1 Capital
- Minimum Capital Ratios, Capital Conservation Buffer, and Prompt Corrective Action requirements
- Standardized Approach for Risk-weighted Assets
    - Residential Mortgage Exposure

Accumulated Other Comprehensive Income (AOCI) as a component of Tier 1 Capital

The proposal recommends that AOCI, including unrealized gains and losses on securities, be included as part of Tier 1 capital. Our primary concern with this proposal is this could create substantial volatility in the banks' capital ratios, which may also produce inconsistent reporting. This is a concern because the volatility in the AOCI for Available-for-Sale (AFS) investment securities is a result of changes in the market interest rates and no reflection of the credit quality or other risk associated with the investment. GAAP allows banks to choose between Held to Maturity (HTM), Available for Sale, and Trading methods. If a bank has the intention and the ability to hold a security to maturity, they can choose HTM or AFS methods; otherwise, the security must be considered trading in which the market risk is captured and reflected in their capital. We believe this change would force banks to place all securities in HTM, essentially ignoring the market risk and misrepresenting the value of the portfolio to shareholders. In addition, these changes would alter the strategies of community banks' portfolio managers by enticing them to have an increased concentration of investments in short-term treasuries which would result in a decrease of interest income. Decreased income flows directly through to produce lower retained earnings and capital, counter to the agencies goals.

Minimum Capital Ratios, Capital Conservation Buffer, and Prompt Corrective Action requirements

The agencies have introduced several changes regarding capital ratios, minimums, and buffers. The proposed recommendations create a new Tier 1 common capital ratio, adjust the current prompt corrective action (PCA) minimums and introduce a new 2.5% buffer above and beyond the current PCA "well-capitalized" ratios, which are 2% above "adequately capitalized". We understand the importance of common equity and the recommended adjustments to the minimums and are not opposed to these modifications; however, we believe the new buffers create confusion and inconsistently restrict management actions. We recommend the agencies consider continuing the use of current monitoring procedures and apply the buffers and restrictions associated, as needed, through formal enforcement actions; similar to the current practices. We believe the agency will create confusion with the addition of new ratios, a change in the minimums, and the creation of buffers. Various restrictions will be enforced based on varying calculations putting additional capital pressure on community banks.

Standardized Approach for Risk-weighted Assets (Including Residential Mortgage Exposure)

In the current PCA risk-weighting of residential mortgage loans, there are two risk premiums (percentages) applied to these loan types based on their lien position. The Basel III proposal establishes a matrix for these loans ranging from 35% to 200% risk-weighting driven by lien position and loan to value (LTV) ratios. A large portion of community banks' mortgage loans in their portfolio (not securitized and sold in the secondary market) are junior liens. With the recent decline in property values, these loans carry a higher LTV and therefore would bear a higher risk-weighting with the proposal. Again, the consequence of these recommendations will result in lower capital ratios and will in no way be a reflection of a change in the credit quality. The calculation based on 200% will generate increased unnecessary write-down and provision to preserve capital. If a loan fails to pay and there is no remaining collateral, the maximum a bank can loose is 100%; therefore, this 200% requirement unfairly burdens banks' capital, and results in negative consequences to the investors and customers. In addition to our concerns with the impact to community banking, our concern is also with the entire local economic system. The financial services industry, especially local community banks, are a reflection of their economies. These changes in risk premiums for residential mortgage loans are going to incent banks to reduce mortgage loans in order to comply with the aforementioned additional capital requirements. This will put undue pressure on the housing market from the lack of available financing and continue our anemic recovery.

In conclusion, Cabarrus Bank & Trust is grateful for the opportunity to comment on the proposal. We support the intentions of the agencies to improve the capital framework in the financial services industry and appreciate the concern and focus to build the banks' capacity to absorb losses during rough economic times, similar to the recent recession, but believe the current proposal needs revision to be palatable to all interested parties. Increased volatility in Tier 1 capital, higher capital requirements, and a higher risk-weighting of assets will result in a reduced ability to leverage capital for growth. This reduced growth will require banks to pay a dividend to support their stagnant stock price. The proposed changes will impede this by lowering the rate of return, all ending in a lower trading value. Furthermore, all of these increased regulations require more manpower, which increases overhead, lowering earnings and decreases capital, again counterproductive to the intention of the agencies.

Thank you for taking the time to listen to our concerns and if you have any questions or would like any additional information please feel free to contact us.

Sincerely,

Patricia K. Horton

Patricia K. Horton

President & CEO

Cabarrus Bank & Trust