Maryland Bankers Association

October 22, 2012

The Honorable Ben S. Bernanke, Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551
regs.comments@federalreserve.gov

Docket R-1430 and R-1442
RIN No. 7100-AD 87

The Honorable Thomas J. Curry, Comptroller
Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, DC 20219
regs.comments@occ.treas.gov

Docket ID OCC-2012-0008 and OCC-2012-0009
RIN 1557-AD46

The Honorable Martin J. Gruenberg, Acting Chairman
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation,
550 17th Street, N.W.
Washington, D.C. 20429
comments@fdic.gov

RIN 3064-AD95 and RIN 3064-AD96

Re: *Regulatory Capital Rules: Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action and Regulatory Capital Rules: Standardized Approach for Risk-weighted Assets; Market Discipline and Disclosure Requirements (the "Proposals")*

Heads of the Agencies:

On behalf of our members, the Maryland Bankers Association (MBA) respectfully submits the following comments in response to the Basel III and Standardized Approach proposals that were approved on June 7, 2012 by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (collectively the "banking agencies").

Founded in 1896, MBA is the only Maryland-based trade group representing banks in the state. The 131 banks operating in Maryland hold in excess of $116 billion in FDIC-insured deposits in about 1,800 branches across the state. The Maryland banking industry employs more than 45,000 banking professionals in Maryland. MBA's members include banks of all sizes and charter types including: state-chartered banks, national banks and federal thrifts, and state banks chartered outside of Maryland.

MBA appreciates the opportunity to comment on the proposals. Some of MBA's members have already submitted their comment letters. However, we are hearing concerns from a number of community bank members about submitting comment letters for fear of spotlighting the specific impact of the proposals on their ability to raise capital to meet the new standards and to continue to meet the credit needs of their communities. We are pleased to submit this comment letter on behalf of our members. To give you a better sense of the institutions MBA represents, a membership list, along with bank size and charter is included as attachment D.

A primary focus of MBA's comment is the practical impact of the Basel III and Standardized Approach proposals on Maryland's banks, their loan products and ability to lend, and the resulting effect on businesses, customers, and the economy. To help MBA assess the potential impact of the proposals rules in these areas, we:

1. Requested an analysis from the Federal Home Loan Bank of Atlanta (FHLBank Atlanta) on the impact to community banks,
2. Requested an analysis from one of our member banks with a regional presence on the impact to their loan products, and
3. Conducted a membership survey on the impact of the proposals on member institutions and their ability to serve customers and community.

The resulting information is included in MBA's comment letter. It is our hope that this information illustrates the very real concerns raised by our members about the impact of the proposed Basel III and Standardized Approach capital rules on banks' ability to effectively serve their communities and customers.

MBA's comment letter is divided into the following sections.

I. General Perspectives
II. Specific Issues of Concern and MBA's Recommendations
III. Hypothetical Community Bank Profiles and Impact of Proposals – as analyzed by the FHLBank Atlanta
IV. Analysis of Products Impacted by the Proposals – A Maryland Bank's Perspectives
V. Impact of Proposals on Community Banks, Lending, and Ability to Serve Customers – MBA Membership Survey Results
VI. Conclusion

We sincerely hope you find this information useful as you consider the various rule changes included in the Basel III and Standardized Approach proposals.

I. General Perspectives

The Maryland banking industry supports strong capital standards. Since the financial crisis, banks across Maryland have increased the amount of capital that they hold and are working diligently to comply with new reforms resulting from the Dodd-Frank Act. The Proposals could fundamentally change how banks calculate their regulatory capital requirements. If adopted as proposed, the Proposals would increase the minimum levels of required capital, narrow the definition of capital, and increase the risk weighted assets for various asset classes. The proposed Basel III and Standard Approach standards would require banks of all sizes to increase their capital and liquidity holdings dramatically, would diminish lending and stifle economic growth across the State.

According to MBA's recent survey of our members, 65% of survey respondents reported they would face a reduction in capital levels under the Proposals. The Proposals will force banks to seek capital at a time when capital is scarce and complicate the capital raising process by forcing many banks to seek capital simultaneously. In addition to a capital scare environment, a financial institution's ability to raise capital is greatly influenced by their specific business model and their communities. For example, non-public banks face specific, serious limitations. "We are a non-public company, our stock does not trade. Going to the capital markets will be difficult as we will be competing with public companies that report in the press and are followed by institutional investors. Our shareholders have been paid dividends since 1899 and it will be difficult to project a continuation of dividend payment due to the buffer on top of capital standards. We would only need a couple million in capital and cost to raise small amounts of capital is large on a relative basis." According to one of our mutual members, "Ours is a simple process – we are a true mutual – we have no holding company – thus our capital increase via our net income."

Emphasizing the impact of the local economy, one member commented "…it is virtually impossible for a bank on the Delmarva Peninsula to raise additional capital for the sale of stock given the cloud that looms over the head of every community bank. We do not operate under any regulatory order but Stock prices for Community Banks in our area have plummeted. The only meaningful way to increase our capital is a no growth slow growth or even shrinkage strategy. Growing the bank only decreases your capital further. These rules are designed to shrink or eliminate the community banks operating in my market area." If unable to raise the necessary capital, banks will need to pursue alternatives – such as decreasing their asset base, restricting loan growth and the overall balance sheet, and reducing deposits.

Additionally, the Proposals are so complex that smaller banks simply don't have the capability to go through the analysis required on loans and investments. One MBA member reported, "Because the size and complexity of our bank does not justify the resources to be put into Software and labor to do the new basil three calculations, it will result in a dead cost to us and additional labor to calculate capital based upon the new standards." This in turn has implications for lending and customer service. "…Credit administration will be strained. Credit availability will be lessened." According to MBA's survey, 100% of responding banks indicated they would face reporting challenges and costs due to the Proposals.

MBA's survey of our members also indicates a very real concern among some of MBA's community bank members about their ability to survive given the difficulty in accessing new sources of capital and the higher proposed capital requirements on their "bread and butter" lending – mortgage loans and loans to small businesses. In fact, 83% of survey respondents reported that their lending would be severely impacted and that their product offers would change if the Proposals were adopted as proposed. One institution reported that, "Due to affect on interest rate risk and capital our growth would be severely limited. We will evaluate marginally profitable branches and consider closing them. We many of our historic borrowers would have to go to credit unions, finance companies and other nonblank institutions for their loans." Echoing similar concerns, another bank added, "A likely solution to the increased capital burden will be to reduce the size of our asset base. Not only will this reduce our ability to do new lending, it will reduce our need for customer deposits. Having a significantly smaller asset base will also likely change the size and composition of our workforce."

An additional point of concern is credit unions, by their very nature, are not covered by the proposals. The credit union industry offers many of the same products that banks do and have similar structures of smaller, community banks. Many have aggressively pursued more bank activities, including greater commercial lending authority. Further, the credit union industry holds more than $1 trillion in assets and represents a significant portion of the financial services industry. To put that number into perspective, in the banking industry it would take 6,000 banks (starting with the smallest and working upward) to account for $1 trillion in assets.

The credit union industry has a large presence and, due to their tax exempt status, is growing. In Maryland credit unions have double their market share from 10% to 20% in the last ten years. If the proposals are applied to banks and not credit unions, it will further exacerbate to an extremely unlevel playing field and effectively drive business from banks to credit unions – which is not always in the best interest of the customer or the State.

Maryland bankers want to be sure that they are able to continue to serve their communities and businesses. A strong economy is dependent on job growth and job growth is dependent on the availability of capital. We want to be sure that the new rules do not reduce the ability of Maryland's banks to generate this capital and make loans and investments.

II. Specific Issues of Concern and MBA's Recommendations

While we support requiring appropriate levels of capital to ensure that financial institutions are well positioned to weather future storms, we have strong concerns about the Proposals which are summarized below along with recommendations for changes:

1. **The Proposals apply to all banks regardless of their complexity. This one-size fits all approach will have disparate impact on traditional banks**. These institutions generally do not invest in securitizations, use complex derivatives or engage in substantial off-balance sheet transactions. Most community banks lack the operational capacities to manage the

volatility of bank balance sheets that will be introduced if the Proposals are adopted without substantial change. Further, if the capital rules are adopted as proposed, and applied retroactively, our members will be required to reassess every aspect of their portfolio loans. This will impose substantial hardship.

Our members will need to review the underwriting that was done for each loan and determine whether such underwriting, which was done in accordance with acceptable regulatory guidance and industry practice, complies with the new requirements of the capital proposal. Institutions will need to verify, for example, that the underwriting for each loan properly assessed the borrower's repayment ability based on the factors set forth in the proposal. They will also be required to ensure that loans were properly documented in accordance with new and somewhat subjective criteria.

- ***MBA recommendation:*** *The proposals should be modified to take into account the large diversity of bank balance sheet compositions, risk profiles and business models. A tailored regulatory approach will enable banks of all sizes to operate under varied economic conditions in a safe and sound manner while continuing to meet their community and customers' needs.*

2. **Requirement of recognizing unrealized gains and losses on available for sale (AFS) securities, reported through OCI, will have a substantial impact on an institution's capital accounts**. This requirement includes unrealized gains and losses from debt securities whose valuations primarily change as a result of fluctuations in interest rates, as opposed to changes in credit risk. Our current environment of historically low interest rates will result in unusually high unrealized gains. These same unrealized gains will become unrealized losses during a period of interest rate increases. Sixty-five percent of responding banks indicated they would be negatively impacted by this change in MBA's recent survey. While the level of impact ranged from institution to institution, the effects were significant – some banks predict that this will move them from well capitalized to adequately capitalized.

   For example, one bank reported that "in general our capital ratios are stable or slightly improve with Basel III. But when we apply a 3.00% rate shock to our AFS securities, our capital ratios fall dramatically by over 2.00% to adequately capitalized. We feel this will cause us to dramatically adjust our investment strategy where we will substantially shorten our duration of our portfolio and most likely we will shift a significant portion to held to maturity. These actions will reduce our earnings and place unneeded pressure on our liquidity. This will both slow the growth rate of the bank and impair loan growth."

   According to another MBA member bank, "Our most recent analysis projects a decrease in market value of investments of 12.8% given a 300 bp increase in rates. Carried through to equity, this has a negative impact on our unrealized loss on securities AFS of $4.75 million. Tier 1 capital would decrease by 20.71% and total capital would decrease by 19.28%. According to the capital calculator distributed on 9/24/12, our bank would be reclassified from well capitalized to adequately capitalized."

- ***MBA recommendation:*** *We believe that the inclusion of the AFS adjustment within capital is unnecessary.*

3. **<u>Increased risk weighting for residential mortgage loans will make mortgage loans more difficult to obtain in many markets, including those in areas typically served by community banks (ex. rural communities)</u>**. MBA has had extensive conversations with our members about the proposals. We also issued a membership survey to better assess the impact of the proposals on a variety of areas including residential mortgage lending. The feedback on the changes to risk-weighting of residential mortgage exposures has been consistent and extremely concerning. There is a very real concern that the proposals, if adopted without significant modification, will drive many community banks out of the residential mortgage lending business – or restrict their ability to provide mortgage products their customers have used safely for decades (ex. products for first time homebuyers, who have less than 20% down).

   Below are some examples from our bank members on the anticipated impact to lending:

   - If 1-4 family residential loans are risk weighted at 100% it will definitely change our strategy in going after those loans. In our market area that is a significant loss to the public.

   - Lending will have to be curtailed in the 1-4 family, HELOC's and small business. All of this is the backbone of the community lending arena. The economy will suffer even greater if this happens.

   - As we will not be able to write balloon mortgages, we will be forced to write 10- and 15-year fixed term mortgages. This will result in low production and potential increase in interest rate risk. A&D loans to small real estate developers will not be affordable.

   - Risk based capital restrictions that punish banks for extending higher loan to value residential mortgages will have the unwelcome side effect of eliminating programs for first time homebuyers, who rarely have a down payment equal to 20% of the appraised value. This aspect will interfere directly with CRA initiatives.

- ***MBA recommendation:*** *We believe the implementation of changes to the risk-weight of residential mortgage exposure should be eliminated. Issues with residential mortgage lending should be addressed at the risk management level and through the supervisory process.*

4. **<u>The punitive risk weights of up to 200 percent for home equity and second lien loans will both increase the cost of credit to the consumer and restrict the availability of consumer credit</u>**. A first lien HELOC may qualify for Category 1 treatment only if the institution underwrote the loan based on the maximum contractual exposure under the terms of the HELOC. Further, junior lien transactions are Category 2 transactions unless they are held by the same financial institution with no intervening lienholder and otherwise contain the characteristics of a Category 1 loan. Whether a residential loan is given a Category 1 or a Category 2 designation can have a profound influence on an institution's overall capital profile. This is particularly the case for smaller community banks.

   We are very concerned that the risk weight will push banks to greatly restrict or discontinue these product lines. HELOCs and second lien loans are an important source of credit for consumers and small business. While we appreciate the concerns with the current environment, many banks have conducted these loans safely and soundly and enabled small business and customers' access to critical credit. The arbitrary risk-weighting will have a significant impact on lending in this area.

   In fact, according to MBA's survey, 67% of responding banks indicated that HELOCs lending would be severely impacted if the Proposals are adopted without significant change. "HELOC's will be more limited and we will not extend them to good customers if it took us over the appropriate LTV thresholds. We will focus our secondary market mortgages to investors with the shortest reps and warranty periods." Reduced ability to generate HELOC and second line lending has implications for borrowers and the overall economy. "If we are unable to continue to lend to the small business customer, the 1-4 family (that doesn't qualify on the secondary market) and HELOCs, then they will start leaving the community banks. The economy cannot recover if this happens."

   - ***MBA recommendation:*** *The arbitrary risk-weighting in this area should be eliminated. Issues with home equity and second lien loans should be addressed at the risk management level and through the supervisory process.*

5. **<u>Increasing risk weights on "High Volume Commercial Real Estate" loans is a redundant means of raising capital requirements for banks</u>**. Further, the punitive risk weight does not account for the institution's experience and expertise in this type of lending, the adequacy of its policies and procedures and the level of concentration. These loans are basically defined as all non 1-4 family acquisitions, construction, and development loans. The economic importance of these types of loans is underscored by one of MBA's member banker's comments, "The only area of economic growth has been in high volatility commercial real estate loans. All non-1-4 family acquisition and construction loans for rental homes it the only area of economic growth in our market area that is of any significance."

   MBA asked our members to assess the effect that the proposal to bump the risk weights on all "High Volume Commercial Real Estate Loans" up from 100% to 150%. Fifty-eight percent of respondents indicted their risk-weighted assets would be impacted. A troubling 33% reported they would discontinue lending in this area if the Proposals were adopted as introduced. Of the thirty-three percent that reported there would be little to no impact – this was since they either 1) did not currently generate these types of loans or (2) had so few loans on their portfolio that they were not impacted.

- ***MBA recommendation:*** *Issues with "High Volume Commercial Real Estate" lending should be addressed at the risk management level and through the supervisory process.*

6. **Increasing risk weights on delinquent loans is also a redundant means of raising capital requirements**. Banks are already highly regulated in this regard and criticized severely if not adequately recognizing the need for capital to mitigate the risks of delinquencies. Under the current accounting system, when a loan is on nonaccrual status or 90 days or more past due it is tested for impairment. The same is true for a security. If an asset is determined to be impaired, the bank assesses what amount of the asset is collectable. If the full carrying amount of the asset is not expected to be collected, based on the value of the collateral or expected cash flows, an increase in loan loss reserves is required.

   Considering the current process, our members tell us that the added risk-weighting included in the proposals will result in unnecessary double-counting of risk. Maryland banks work extensively with their customers to try to mitigate financial difficulties and avoid foreclosure. We are very concerned that the proposed rules will discourage banks from working with their customers since the risk weight for Other Real Estate Owned (OREO) is less than a delinquent loan.

   MBA survey respondents raised concerns about this proposal. Thirty-three percent of survey respondents reported a negative impact to over all capital; 17% indicated that they would have to reduce lending as balance sheets would need to shrink to fit under the new rules. In addition, important affects to how troubled loans and assets are handled were raised. "Due to the affect on capital ratios from this change, we will no longer be able to work with customers for extended periods of time or be willing into enter into forbearance agreements." "We would be forced to dump troubled assets at lower prices, adversely affect profitability and flood the market with more negative comps."

   - ***MBA recommendation:*** *This provision should be eliminated. Existing accounting rules address this issue of risk sufficiently.*

7. **Elimination of Trust Preferred Securities (TruPS), which were grandfathered by the Collins amendment to the Dodd-Frank Act, will significantly diminish available capital for community banks**. TruPS have served as an important source of capital for a variety of small-cap institutions. These same institutions have found it very difficult to raise capital in our current environment. Further, small, privately-held banks have extremely limited access to capital. An arbitrary phase-out of TruPS in an environment where capital is scarce will result in the need for affected banks to shrink their balance sheet and therefore reduce lending.

The arbitrary phase-out of TruPS is not consistent with the intent of Congress that debated this issue during the development of the Dodd-Frank Act. Congress recognized the value and importance of TruPS to community banks and decided (through the Collins Amendment) to grandfather TruPS as tier 1 capital for institutions under $15 billion.

Without a method to replace the TruPS with equity capital, the loss of this capital would greatly reduce the ability of banks to lend to small businesses and customers and could have a serious impact on the safety and soundness of holding companies. The result will be that banks will need to decrease loans - which is the last thing we need in our current economic environment. During the Dodd-Frank Act debate on this issue, it was estimated that removing trust preferred securities as tier one capital will pull more than $100 billion in capital from community banks nationwide. This capital supports over $1 trillion in assets in the banking system. Many banks in Maryland use this as a capital source. One member bank indicated that if this regulation goes into effect, they "will likely consider shrinking its asset base by…29% in order to account for this new treatment for TruPS."

- ***MBA recommendation:*** *Remain consistent with the intent of the Collins amendment and allow for the grandfathering of existing trust preferred instruments for institutions under $15 billion in total assets.*

8. **As currently drafted, the ambiguous requirement to hold capital for credit enhancing representations and warranties on 1-4 family residential home loans which have been sold into the secondary market threatens to drive community banks out of the mortgage lending business**. The proposal requires a 100% risk weight to assets subject to a "credit-enhancing representation or warranty" which includes provisions to protect the purchaser from losses resulting the default or nonperformance of the counterparties. Many community banks originate residential mortgages and sell them into the secondary market in order to manage interest rate risk.

   This is critical since smaller banks do not have the interest rate risk capacity to hold 30-year mortgage loans in their portfolios. These loans frequently include agreements that the originating bank repurchase the loan if it defaults with in a specified period of time, etc. If the 100% risk weight is applied to these loans, many community banks will not be able to continue the practice of originating and selling into the secondary market. Without this ability, their capacity to make residential mortgage loans will be dramatically reduced and customers will face a greatly diminished mortgage market.

   - ***MBA recommendation:*** *Risk weighting in this area needs to be carefully constructed so that it does not stifle mortgage lending by traditional depository institutions that are highly regulated with strict underwriting standards.*

9. **The limitation of inclusion of the value of mortgage servicing assets will further limit the involvement of traditional banks in mortgage loan servicing**. We are very

concerned about this change. These traditional, community focused banks are some of the best and most prudent loan servicers. Their involvement in mortgage servicing is good for the customer and good for the industry. For example, some customers want to deal with banks that they know will keep the servicing rights to their loans. Some institutions have already sold their mortgage servicing assets to a non-depository, non-bank servicer. Limiting the inclusion of the value of mortgage servicing assets in a bank's capital will encourage banks to get out of the mortgage servicing business. Furthermore, one of MBA's members has significant mortgage servicing rights associated with HUD-related loans, a niche that this bank has served.

- ***MBA recommendation**: This provision should be eliminated.*

10. **The added risk weighting for residential mortgage loans (from a 50% risk rating to a minimum of a 100% risk weighting) will discourage the use of and/or significantly increase the pricing of balloon mortgages and/or other adjustable rate mortgages.** Another consequence of the retroactive treatment required by the Proposals, and the automatic categorization that it requires, is the treatment of balloon and demand (or "call") loans and the effect that such treatment will have on the availability of credit to rural and/or low- to-moderate income communities. Under the proposal, the presence of a balloon feature in a residential mortgage loan will require an institution to automatically categorize that loan as Category 2. We assume that demand loans, which allow an institution to demand repayment of a loan after an agreed upon period, would also require this treatment. Many of our members use loans with balloon and demand features, to manage interest rate risk and as a means to allow customers to renew their loans without going through the expensive and time-consuming refinance process. This is particularly the case with our members that serve rural and low- to moderate-income communities. The impacts to balloon loans and demand / call loans follow.

    - Balloon Loans: Many of MBA's community bank members originate residential mortgage loans with balloon features. According to MBA's recent survey, 33% of responding banks use a balloon payment structure on 1-4 residential mortgage first liens. The extent of institutions using a balloon payment varied considerably. Some of our members – with an outstanding record for operating on a safe and sound basis – have loan portfolios with a heavy concentration of balloon loans. These loans are typically underwritten with standard loan terms, but include a balloon payment portion. These loans differ from the Option ARM loans that typically have had a much higher default rate. The residential balloon loans used by Maryland's traditional banks are generated for customers that want to work with a bank they know will maintain the servicing rights to the mortgage and/or customers that are not able to qualify for a conventional mortgage product that would be sold into the secondary market. The added risk weighting for balloon residential loans will lead to a higher interest rate risk for banks. This in turn will discourage banks from providing these loans or push banks to significantly increase the pricing for balloon loans in order to offset the increased interest rate risk costs.

- Other Adjustable Rate Mortgages -- Call / Demand Loans – Primarily located on the Eastern Shore, some of Maryland's smaller community banks offer residential mortgage loans with "call" or "demand" provisions. Banks use this loan feature as a way of offering a more competitive rate and repayment option to borrowers and as a means for managing interest rate risk. According to MBA member feedback, this provision allows them to keep the loans in portfolio rather than sell them into the secondary market. Consumers benefit by more competitive interest rates, repayment options, and the ability to work with a bank that services its own mortgages. If there is a "call" or "demand" feature in the loan, it will be a part of the written agreement (and found in the promissory note). The federal Truth-in-Lending Act requires a specific disclosure if the loan has a "demand" or "call" feature.

  Call or demand features on residential mortgage loans give community banks the ability to offer residential mortgage loans without the complexity and cost of becoming a seller/servicer for Fannie Mae or Freddie Mac and enable them to offer an affordable mortgage loan option for low and moderate income borrowers and first time home buyers. For interest rate sensitivity measure purposes, residential mortgage loans with call/demand features are reported as immediately repriceable; however, in practice, banks do not arbitrarily increase loan rates and rarely exercise this option for residential mortgage loans with call provisions. The following survey responses illustrate this point:

    1. Over the bank's 118 year history, the bank has only implemented an across-the-board rate increase twice. The first was during the Great Depression era, and the second was during the high inflation and interest rate environment that prevailed in the late 70's early 80's.
    2. Our residential mortgage loans are made with a 3 year demand feature in order for us to manage interest rate risk. We have only put the demand feature in effect one time on one mortgage. It was an employee who was given a 1% discount on their mortgage and then left our employment. After the 3 years, we increased that mortgage by 1%.

During periods of declining rates, banks frequently adjust mortgage interest rates downward at the time it may call a loan in order to retain customers and relationships. This can be done at no cost to the borrower and saves the borrower thousands of dollars associated with a total loan refinance. In addition, the rate and term flexibility provided by demand lending is a tool that can be used to preserve homeownership. For example, when a borrower encounters a financial hardship, and conditions warrant payment relief, banks have the flexibility to re-amortize a residential mortgage loan with a demand feature to produce a lower and more affordable payment for the borrower. This again, is accomplished without the cost associated with a complete refinance.

MBA believes that balloon and demand loans are consumer and business friendly loan arrangements that provide a number of flexible repayment, rate, and term options. The automatic categorization of balloon and demand loans as Category 2 loans would decrease the repayment options available to an institution and its customers. As mentioned, these loans are primarily made by our members that service rural and low- to moderate-income communities. Borrowers in those communities would be adversely affected by a drying up of this type of credit. Moreover, the community banks in those communities would take an immediate hit to capital if required to recategorize these loans. Often those institutions are in the most difficult position of raising new capital.

- ***MBA Recommendation:*** *We urge you to reconsider including balloon residential mortgage and certain adjustable interest rate loans in Category 1 loans, rather than classify them as Category 2 loans. This is consistent with current rules. If the agencies' conclusion is to leave this portion of the proposal unchanged, we strongly encourage you to grandfather balloon or demand residential mortgage loans settled before January 1, 2015.*

III. Hypothetical Community Bank Profiles and Impact of Proposals – as analyzed by the FHLBank Atlanta

To help assess the potential impact of the Proposals on Maryland's community banks, MBA requested an analysis from the FHLBank Atlanta. Below are the summaries of three hypothetical community bank profiles with varying asset mixes and the potential impact of the Proposals. Attachment A provides a detailed and modeled explanation of the impact on the various components of each of the hypothetical banks.

- **Model Bank #1 (Assets: $470 million)**

The community bank in this example opened in the summer of 2008 and has maintained high credit standards and, as a result, did not have a high level of classified assets or write-offs. From 2008 until 2012, the bank increased its Available For Sale ("AFS") securities portfolio to offset a decline in loan demand, as was not uncommon for financial institutions, in order to redeploy cash flows from shrinking loan portfolios. During this time period, rates dropped to historic lows and their Other Comprehensive Income increased due to unrealized gains in the AFS portfolio.

This bank currently has Tier 1 Leverage capital of 9.14%, and if the NPR provision is implemented and rates rise 300 bps starting in 2015, their Tier 1 Leverage capital would drop to 7.58%. Additionally while the interest rate risk in the AFS portfolio is more than hedged, the Accumulated Other Comprehensive Income (AOCI) treatment in the proposed regulations causes capital to significantly move in the opposite direction of that predicted by the institution's asset-liability analysis. Further, this bank has a portfolio of five-year jumbo balloon mortgages. The AOCI treatment in the proposed regulations and the change in risk weights on balloon mortgages potentially will cause excessive impacts to capital ratios (see attachment A).

- **Model Bank #2 (Assets: $375 million)**

The community bank in this example is located in a growing city with a robust economy due to the fact that three large corporations are headquartered there. The bank's performance from 2008 to 2012 has been steadily improving and is considered healthy in comparison to its peers. In 2009, as with most other banks at the time, the bank had an increase in problem loans followed by subsequent charge-offs in 2010. By mid-2012, asset quality had improved and Allowance for Loan and Lease Losses to Non-Performing Loans has returned to historical levels.

While this bank can continue to portfolio loans as part of the agreement to attain Small Business Lending Fund (SBLF) debt at 1%, the impact is seen in their risk based capital ratios declining due to the volume and increased risk weighting these assets will have under the Proposals. In this scenario, the bank will also need to address the phase-out of (Trust Preferred Securities (TruPS) required when the institution's assets are greater than $500 million. This could occur as early as mid-2015. When layering in the repayment of TruPS over a 10-year period, the bank's risk based capital ratios decline below well capitalized from 2017 to 2019. While the Proposals require the bank to increase the risk weightings on residential mortgages with LTV greater than 80%, this discourages refinancing, as well as, lending to first time homebuyers. Housing is simply an inventory of potential loans. If bankers are required to hold additional capital against the higher LTV loans, then many borrowers will not qualify for mortgages originated and portfolioed at a bank. It seems conflicting to have SBLF that encourages banks to make more loans to small business while the Proposals raise the risk weightings on these assets, as well as, mortgage related loans.

- **Model Bank #3 (Assets: $130 million)**

The community bank in this example offers a diversified selection of loan products. The bank weathered the recent economic recession and ensuing recovery and has continued to experience moderate loan growth and strong credit quality over the past four years. During this time period, they continued to make construction loans for 1-4 residential mortgages and commercial real estate construction loans in their community. Deposit growth was also robust during this time period, while net income was near breakeven from 2008 to 2012.

In addition this bank took down $4.7 million in Troubled Asset Relief Program (TARP) funds and, given their marginal growth in net income, will be challenged to build up retained earnings to pay off this debt while dealing with the forecasted impact of the higher capital ratios phased-in in 2014 and 2015. The bank has three options to pay off the TARP funds: 1) grow earning assets and net income to build up retained earnings; 2) raise capital; or 3) shrink the assets.

In the case of this bank, regardless of their approach, the components of the Proposals will make it extremely difficult to pay off TARP funds. Instead, the bank will need to deal with a significant increase in the cost of these funds. This creates a problem in 2014 and especially 2015, when risk-based requirements for Common Equity Tier One Risk Based Capital (RBC) and Tier One RBC are being phased in. In addition, the change in risk weights take effect in 2015, causing risk weighted assets (denominator of the three risk based capital calculations) to increase by an amount across the industry of 20% (as estimated in the Standardized Approach NPR).

IV. Analysis of Products Impacted by the Proposals – A Maryland Bank's Perspectives

To help assess the potential impact of the Basel III and Standardized Approach proposed rules on lending and loan products, MBA requested one of our bank members with a regional presence to conduct an analysis of their current portfolio, the impact of the proposals, and the effect on product lines. Below is that bank's summary of the impact to their home equity lines, mortgage construction, and 5/1 ARMS.

- **Home Equity Lines**

This regional bank's home equity line portfolio is $303,033,556, which represents 32% of all residential mortgages. Under current capital requirements, 14% of this portfolio would be classified in the 50% risk weight category, with the remainder falling in the 100% risk weight bucket. The Proposals will move every single loan to at least a 100% risk weight. In fact, 8% of the home equity line portfolio would be given a 200% risk weight. The net effect of all risk weight changes to home equity lines is a $48MM increase to net risk weighted assets.

An overlooked piece of the Proposals is the requirement that in order to be classified as Category 1, the interest rate cannot increase by more than 2% in a 12-month period, or 6% over the life of the loan. This bank currently prices all home equity lines with a 24% interest rate ceiling. Although most home equities are eliminated from Category 1 due to being a second position lien, the bank's current pricing strategy will always eliminate first position liens, since it is possible for the rate to increase by more than 6%. In addition, home equity lines are typically given a 480-month term, which violates another characteristic of a Category 1 loan (30 year term max). Therefore, the bank will have to change its home equity line structure to avoid having the entire portfolio classified as Category 2.

- **Mortgage Construction**

This Maryland regional bank's mortgage construction portfolio is $130,556,938, which represents 14% of all residential mortgages. This portfolio is an area of strength for the bank, as it has grown over 20% since the beginning of the year (the rest of the loan portfolio has grown just 2%). Under current capital requirements, 97% of this portfolio would be classified in the 50% risk weight category, with the small remainder in the 100% risk weight category. The Proposals will move 87% of this portfolio to a 100% risk weight, 8% to a 150% risk weight, and 4% to a 200% risk weight. The net effect of all risk weight changes to mortgage construction loans is a $73MM increase to net risk weighted assets. This represents a 108% increase to risk weighted mortgage construction loans.

Loan pricing is again the reason most construction loans move to Category 2. The bank caps the 12-month rate increase at 5%, instead of the 2% required as part of Category 1 characteristics.

- **5/1 ARMS**

The bank's 5/1 ARM portfolio is $247,513,060, which represents 26% of all residential mortgages. Under current capital requirements, 99% of this portfolio would be classified in the 50% risk weight category. The Proposals will move 62% of the portfolio to a 100% risk weight, 5% to a 150% risk weight, and 4% to a 200% risk weight. The net effect of all risk weight changes to 5/1 ARMS is a $101MM increase to net risk weight assets. This represents a 82% increase to risk weighted 5/1 ARM loans.

Loan pricing and term are again the primary reason for the large shift to Category 2 for 5/1 ARMs; 36% of the portfolio has a term over 30 years (typically 31 years), and 48% is priced with a 12-month rate increase of 5%.

- **Summary**

After examining all residential mortgage portfolios, the net impact of the Proposals is an increase of $240.6MM (35.4%) to total risk weighted assets. As a result, the bank would need to raise this amount in additional capital. This could severely reduce the bank's ability to lend, particularly in the segments detailed above. While the bank may be able to change loan pricing and terms going forward (hopefully still driving the same level of business), there is still an existing $935MM portfolio that will be held to the same new standards. Most concerning are the Category 1 characteristics regarding 12-month and lifetime rate increases, which appear rather arbitrary. This single characteristic is responsible for pushing 74% of the bank's residential mortgage portfolio into Category 2.

V. Impact of Proposals on Community Banks, Lending, and Ability to Serve Customers – MBA Membership Survey Results

MBA has been in very close contact with our members on the Basel III and Standardized Approach proposals. To further assess the potential impact of the Proposals on Maryland banks and their ability to meet the needs of their communities and customers, MBA conducted a membership survey of both chief financial officers (CFO's) and chief executive officers (CEO's). The results are very informative and we have included them as attachments B and C for your consideration.

MBA believes this type of feedback on the impact of the proposals is very valuable in determining the real world effect of the proposed changes. In particular, the survey respondent's commentary helps illustrate how banks are struggling with the proposed changes and highlight specific concerns about credit availability and economic impact. We encourage you to review the survey results included in attachments B and C so that you can get a sense of our members' concerns.

VI. Conclusion

In conclusion, for the reasons described above, MBA is extremely concerned about the potential effect of certain aspects of the Proposals on financial institutions that serve our State, particularly regional and community banks. We respectfully urge the Agencies to tailor the standards in a more narrow and less complex way so that our financial institutions can continue to serve communities across Maryland.

Please contact me if you have questions or would like to discuss MBA's concerns in greater detail. Thank you for your consideration of MBA's position and for the opportunity to comment on these significant proposals.

Sincerely,

Kathleen Murphy
President & CEO
Maryland Bankers Association

cc: Member Institutions of the Maryland Bankers Associations
Maryland Congressional Delegation
Mark Kaufman, Maryland Commissioner of Financial Regulation

Attachments: A – Hypothetical Community Bank Profiles and Impact of the Proposals – as provided by the FHLBank Atlanta
B - CEO Survey Results - MBA Basel II and Standardized Approach Proposals Impact Survey
C – CFO Survey Results - MBA Basel II and Standardized Approach Proposals Impact Survey
D- List of MBA Member Institutions, Asset Size and Chartering Agency

Attachment A

Hypothetical Community Bank Profiles and Impact of the Proposals – as Analyzed by the Federal Home Loan Bank Atlanta

Overview

In evaluating the impact of the Basel III Capital Regulation and Standardized Approach Notice of Proposed Rulemaking (NPR), we assessed the effect on 3 different representative community bank profiles.[1]

Summary of Issues

- Model Bank #1 (Assets: $470 million) – Issues with losses on available for sale (AFS) securities when rates rise (40% of portfolio in securities) and maturing jumbo balloon mortgage loans because of the effect of the new risk ratings (100%, 150% and 200%) under the Basel III proposal.

- Model Bank #2 (Assets: $375 million) – Trust Preferred Securities (TruPS--needs to go away when assets reach $500 million) and SBLF get phased out. Portfolio of mortgage loans will also reduce in size, having an adverse affect on homeownership and community development.

- Model Bank #3 (Assets: $130 million) – TARP that can never go away because of common equity limitations.

Model Bank #1

In this example, the hypothetical community bank opened in the summer of 2008 and has maintained high credit standards and thus did not have a high level of classified assets or write-offs. From 2008 until 2012, the bank increased its Available For Sale ("AFS") securities portfolio to offset loan demand declines, as was not uncommon for financial institutions to do in order to redeploy cash flows coming off shrinking loan portfolios. During this time period, rates dropped to historical lows and their Other Comprehensive Income increased due to unrealized gains in the AFS portfolio.

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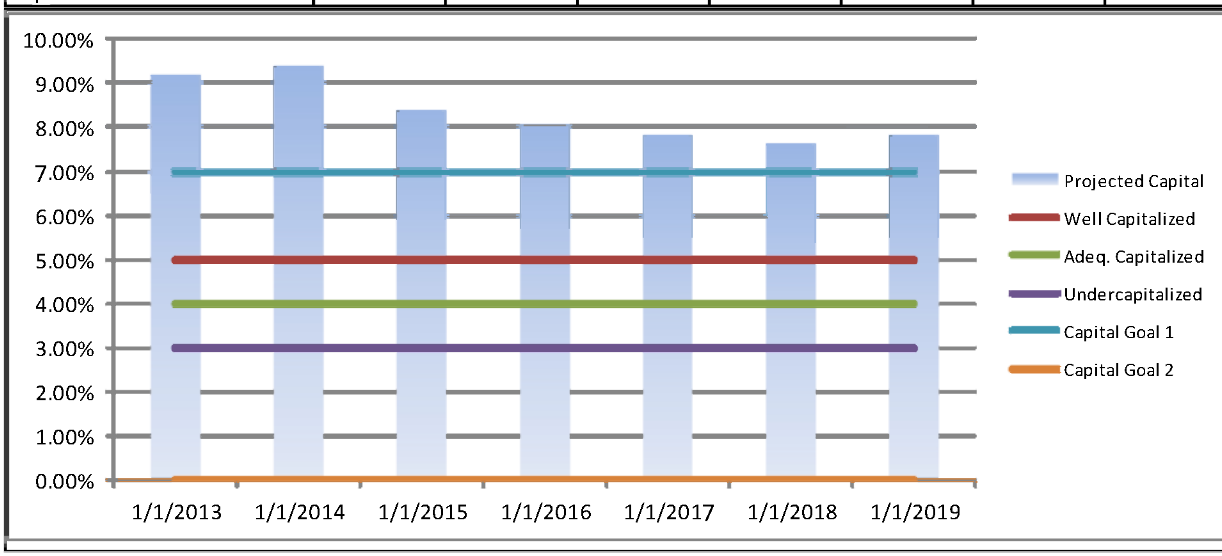
[1] The assessment was performed using Farin & Associate's Capital Speedboat Model, an Excel model that evaluates the effect of phase-in of the proposed capital regulations.

In modeling this institution, the balance sheet mix was held constant and assumed ROAs of .75%, annual growth of 7%, and a dividend payout of 0% of net income. We established capital goals of 2% over regulatory minimum capital requirements. The binding capital constraint for this institution was the Tier One Leverage ratio.

The BASEL III NPR has a provision to recognize unrealized gains and losses on all AFS securities in common equity tier 1 capital. In this bank's case, they currently have an unrealized gain of $1.7 million on its AFS portfolio which totals around $180 million (or roughly 40% of assets). Assuming a portfolio duration of 2.9 years and a market rate rise of 300 basis points, the market value is estimated to drop 8.7%, at which time the unrealized gain of $1.7 million becomes an unrealized loss $13.9 million. Currently, the bank has Tier 1 Leverage capital of 9.14% and if the NPR provision is implemented and rates rise 300 bps starting in 2015, **their Tier 1 Leverage capital would drop to 7.58%**.

Tier 1 Leverage	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018	01/01/2019
Projected Capital	9.14%	9.34%	8.35%	8.05%	7.79%	7.58%	7.81%
Well Capitalized	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
Adeq. Capitalized	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
Undercapitalized	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%	3.00%
Capital Goal 1	7.00%	7.00%	7.00%	7.00%	7.00%	7.00%	7.00%
Capital Goal 2	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%



Ironically, the institution's interest rate risk reports show it as being asset sensitive with EVE increasing in a rising rate environment. In other words, the interest rate risk in the AFS portfolio is more than hedged, yet the AOCI treatment in the proposed regulations causes capital to make a significant move in the opposite direction of that predicted by the institution's asset-liability analysis.

Another challenge is that when the bank in this hypothetical example opened, they started to portfolio 5 year jumbo balloon mortgages. At the time, these loans offered attractive yields and borrowers were very creditworthy. These loans are now maturing and many of them will be renewed. The new BASEL III NPR rules would require that balloon mortgages fall into category 2, which requires them to be risk weighted 100% if LTV <=80, 150% if LTV is between 80 to 90 and up to 200% if LTV is >90. Depending upon the current market values of the underlying properties at the time of renewal into a new 5 year balloon and the original amortization schedules, many of these refinanced loans may require higher risk weightings, leading to a decline in all capital ratios as a result of risk weighted assets increasing in the denominator.

We conclude from this test that both the AOCI treatment in the proposed regulations and the change in risk weights on balloon mortgages potentially will cause excessive impacts to capital ratios that are inconsistent with financial institutions' actions to hedge interest rate risk and undeserved based on the actual underwriting of balloon mortgages.

Model Bank #2

The hypothetical community bank in this example is located in a growing city with a robust economy due to the fact that it is the headquarters for three large corporations. **The bank's performance from 2008 to 2012 has been steadily improving and is considered healthy in comparison to its peers**. In 2009, as with most other banks at the time, the bank had an increase in problem loans followed by subsequent charge-offs in 2010. By mid-2012, asset quality had improved and Allowance for Loan and Lease Losses to Non-Performing Loans has returned to historical levels.

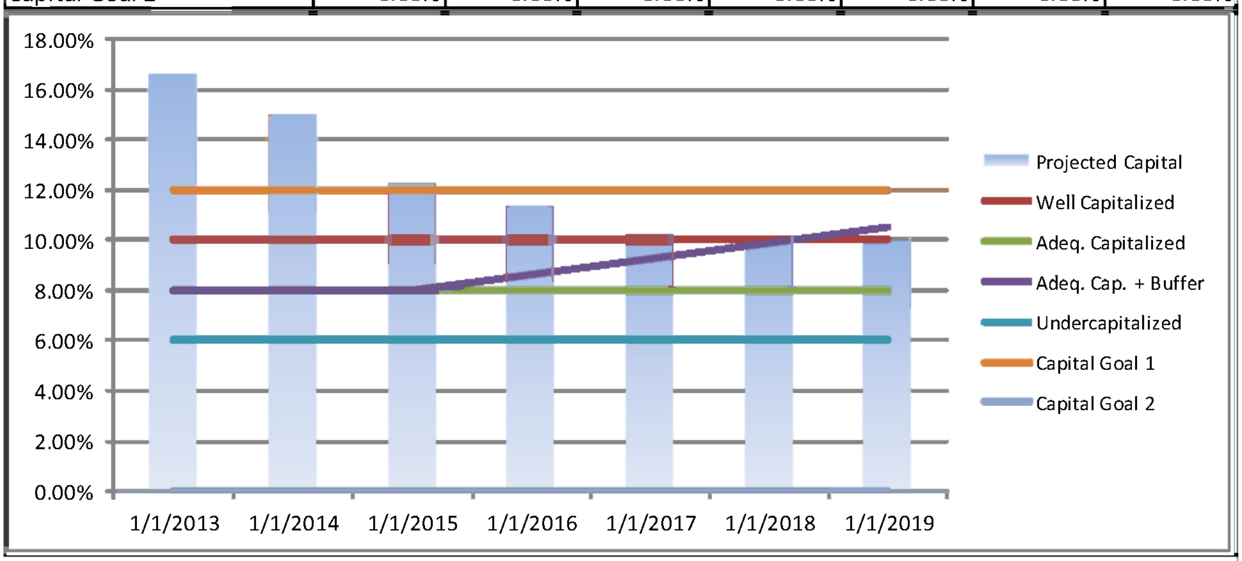
The challenge this bank faces with the new Basel III Capital Regulations relates to the phase-out of trust preferred securities (TruPS) from tier 1 capital over a 10-year period. As of June 2012, the bank has $8 million in TruPS outstanding. The bank currently has total assets of $375 million and the phase-out period to remove TruPS from tier 1 capital is accelerated when total assets are over $500 million.

The bank also has Small Business Lending Fund (SBLF) debt in the amount of $15.5 million and this currently counts as tier 1 capital. The SBLF was created as an incentive for banks with total assets less than $10 billion to make loans to businesses with less than $50 million in annual sales. The bank took down the SBLF debt 12 months ago at a rate of 1%. SBLF debt must be paid back in 10 years and has a variable rate of 1 to 9% depending upon the banks' increase in originations of qualifying small business loans. If lending does not increase in the first 2 years, the rate on the SBLF increases to 7%. The rate on the SBLF debt will automatically increase after 4.5 years to 9%.

In modeling this institution, we held the balance sheet mix constant and assumed ROAs of .80%, annual growth of 10%, and a dividend payout of 20% of net income. We established capital goals of 2% over regulatory minimum capital requirements. The bank's total assets reach $500 million by mid-2015 and they still have $8 million in TruPS outstanding. The SBLF debt pays down from $15.5 million to $3.25 million by mid-2015 and is completely paid off by 1/1/2017. The binding capital constraint during the forecast period for this institution was their Tier One Risk Based and Total Risk Based Capital Ratios. The following graph shows an example of capital growth relative to minimum requirements and the capital goals established for the institution.

Total Risk Based Capital drops below their Well Capitalized and Adequately Capitalized plus buffer in 2019.

Total Risk Based	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018	01/01/2019
Projected Capital	16.58%	15.01%	12.21%	11.31%	10.21%	10.09%	9.94%
Well Capitalized	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%
Adeq. Capitalized	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Adeq. Cap. + Buffer	8.00%	8.00%	8.00%	8.63%	9.25%	9.88%	10.50%
Undercapitalized	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Capital Goal 1	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%
Capital Goal 2	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

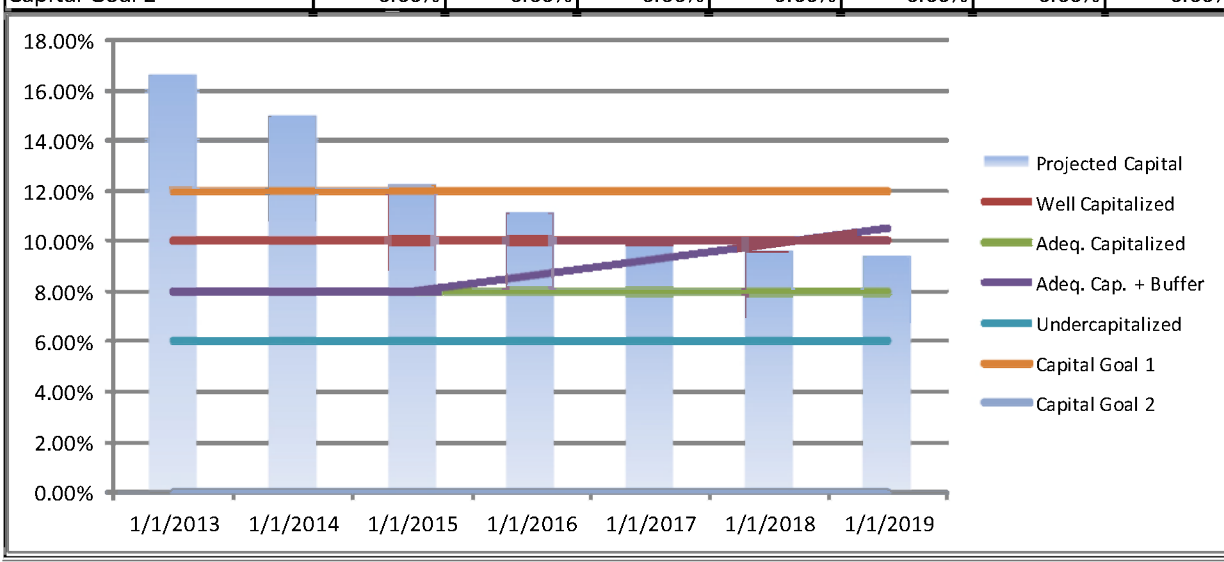


In summary, this forecast does allow the bank to continue portfolioing loans as part of the agreement to attain the SBLF debt at 1%, however the impact can be seen in **risk based capital ratios declining due to the volume and increased risk weighting these assets will have under Basel III**. In this scenario, the bank will also need to address the phase-out of TruPS required when the institution's assets are greater than $500 million.

We'll address paying off the TruPS in the following example by modeling the assumption that the bank begins to pay off the TruPS when they reach $500 million in total assets. All other assumptions used were the same as described earlier. The bank's total assets reach $500 million by mid-2015 and, at that time, the bank pays off $800,000 in TruPS per year for 10 years. TruPs is completely paid off by 6/30/2025.

The binding capital constraint during the forecast period for this institution was their Tier One Risk Based and Total Risk Based Capital Ratios. As shown below, the Total Risk Based Capital falls below their Capital Goal in 2016 and then below Well Capitalized in 2017 through 2019.

Total Risk Based	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018	01/01/2019
Projected Capital	16.58%	15.01%	12.21%	11.12%	9.86%	9.61%	9.36%
Well Capitalized	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%
Adeq. Capitalized	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Adeq. Cap. + Buffer	8.00%	8.00%	8.00%	8.63%	9.25%	9.88%	10.50%
Undercapitalized	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Capital Goal 1	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%
Capital Goal 2	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%



In summary, when layering in the repayment of the TruPS over a 10-year period, the bank's risk based capital ratios decline below well capitalized from 2017 to 2019.

While the proposed Basel III capital regulations require the bank to increase the risk weightings on residential mortgages with LTV greater than 80%, this discourages refinancing, as well as, lending to first time homebuyers. Housing is simply an inventory of potential loans. If bankers are required to hold additional capital against the higher LTV loans, then many borrowers will not qualify for mortgages originated and portfolioed at a bank. It seems conflicting to have SBLF that wants and encourages banks to make more loans to small business while Basel III raises the risk weightings on these assets, as well as, mortgage related loans.

This bank has a portfolio of 1-4 residential mortgages that represents 22% of total assets. The impact of the increased risk weighting of category 1 residential mortgages with LTV > 80% or greater has material impact on their capital ratios. That impact can be seen in the above Total Risk Based Capital chart as a significant reduction in the ratio from 15.01% in 2014 to 12.21% in 2015 when the changes in the risk weights become effective. Growing communities need to have healthy banks, able and willing to make these loans available to qualified borrowers.

Model Bank #3

The hypothetical community bank in this example offers a diversified selection of loan products. The bank weathered the recent economic recession and ensuing recovery and has continued to experience moderate loan growth and strong credit quality over the past four years. During this time period, they continued to make construction loans for 1-4 residential mortgages and CRE construction loans in their community. Deposit growth was also robust during this time period. Net income was near breakeven from 2008 to 2012.

In 2009, they took down $4.7 million in TARP and, given their marginal growth in net income, they will be challenged to build up retained earnings to pay off this debt while dealing with the forecasted impact of the higher capital ratios phased-in in 2014 and 2015. The bank has three options to pay off the TARP: 1) grow earning assets and net income to build up retained earnings; 2) raise capital; or 3) shrink the assets. These three options are evaluated below.

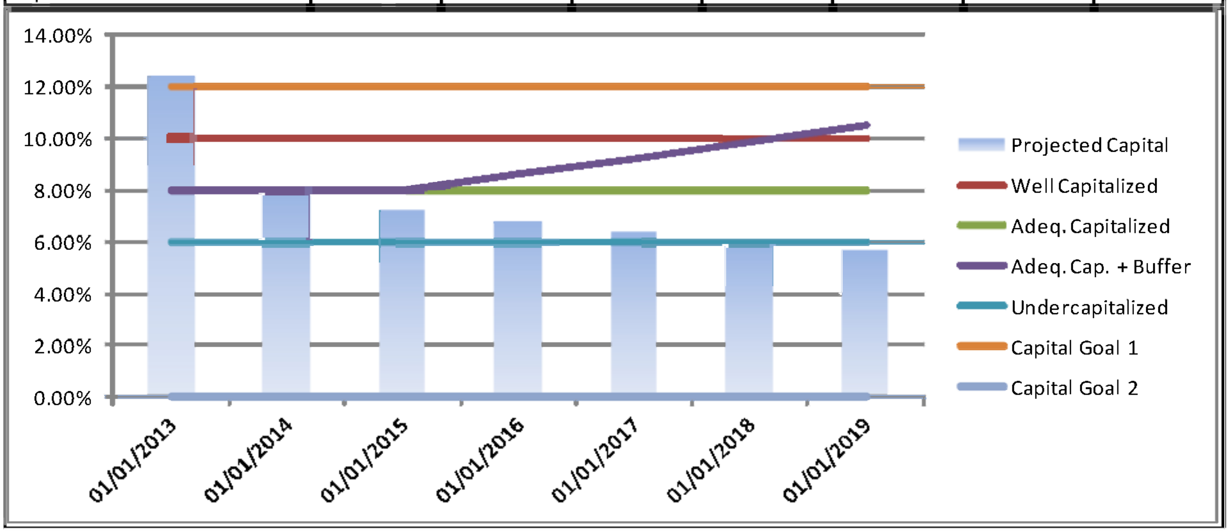
Option 1: Grow Assets and Net Income

In modeling this institution, we held the balance sheet mix constant and assumed ROA of .50%, annual growth of 10%, and a dividend payout of 60% of net income (Sub S). We established capital goals of 2% over regulatory minimum capital requirements. They currently have a netted Surplus and Retained Deficit of $1.3 million available to pay off TARP. In the first example, we pay off the entire TARP by the end of 2013.

Each of the four Basel III capital ratios is challenged in remaining above Well and Adequately Capitalized status during the forecast period. The following graph shows Total Risk Based Capital relative to minimum requirements and the capital goals established for the institution.

Total Risk Based Capital – Falls below Adequately Capitalized in 2014

Total Risk Based	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018	01/01/2019
Projected Capital	12.38%	7.94%	7.18%	6.74%	6.34%	5.98%	5.66%
Well Capitalized	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%
Adeq. Capitalized	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Adeq. Cap. + Buffer	8.00%	8.00%	8.00%	8.63%	9.25%	9.88%	10.50%
Undercapitalized	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Capital Goal 1	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%
Capital Goal 2	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%



Option 2: Raise Capital

This institution is located in a community that has a growing economy and a capital raise is possible. However, given the lack of earnings growth, existing shareholders may be reluctant to infuse additional capital. The dilutive nature of a capital raise is another issue existing shareholders will need to consider. Delaying the capital raise until 2014 or later may prove to be costly. When the minimum capital levels increase in 2014 and 2015, the cost of capital will increase and finding additional investors may prove to be difficult. A well thought out growth plan with additional capital should be created and the management and the board should follow through with the capital raise sooner rather than later.

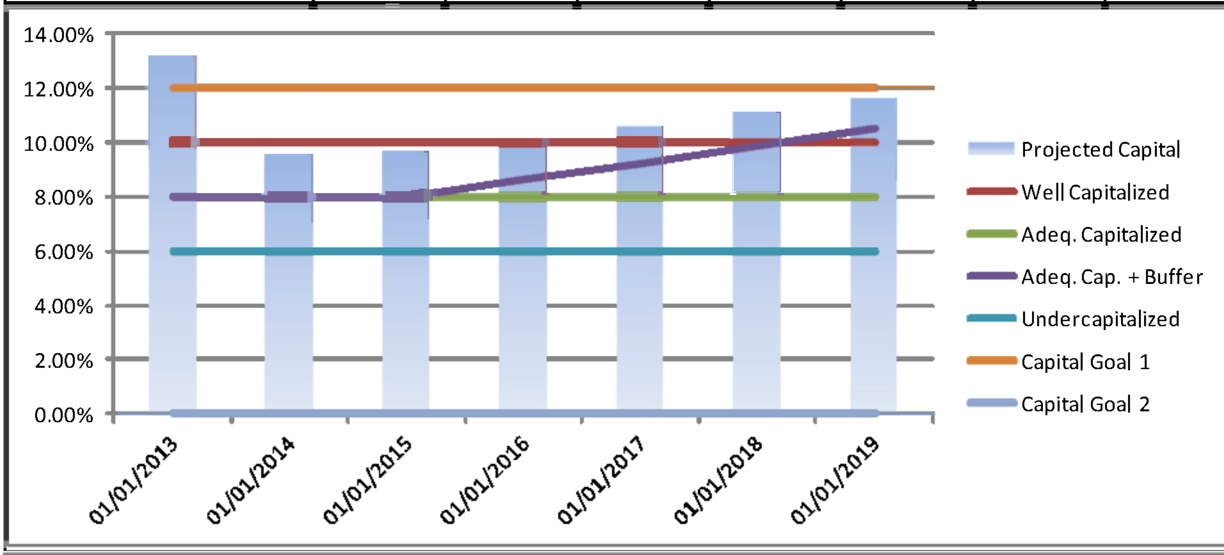
Option 3: Shrink Total Assets and Expenses

In this strategy, we held the balance sheet mix constant and assumed ROA of .60% (increased from .50% because of expense reduction), annual growth of minus 2%, and a dividend payout of 60% of net income (Sub S). We established capital goals of 2% over regulatory minimum capital requirements. They currently have a netted Surplus and Retained Deficit of $1.3 million available to pay off TARP. As in the previous example, we assume the entire TARP is paid off by the end of 2013.

In the following graph, you will notice that the Shrinking Strategy is successful at keeping the bank above the regulatory minimums except for Total Risk Based Capital in 2014 and 2015. In which case, it dips slightly below Well Capitalized. The Shrinking Strategy reduces Total Assets from $138 million (2013) to $121 million (2019)

In the Shrinking Strategy, the bank's Total Risk Based Capital falls below Well Capitalized in 2014 and 2015.

Total Risk Based	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018	01/01/2019
Projected Capital	13.16%	9.49%	9.62%	10.09%	10.57%	11.06%	11.56%
Well Capitalized	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%
Adeq. Capitalized	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Adeq. Cap. + Buffer	8.00%	8.00%	8.00%	8.63%	9.25%	9.88%	10.50%
Undercapitalized	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%	6.00%
Capital Goal 1	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%
Capital Goal 2	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%



In the 10% Growth Strategy, ROE increases from 7.79% to 10.89% during the seven year period compared to the Shrink Strategy in which ROE decreases from 9.06% to 6.74%. The growing bank has $500,000 more in retained earnings by 2019.

The Shrinking Strategy includes cuts in Salary, Benefits and Personal and is impractical in the current banking environment that is saddled with rising compliance and technology costs. In order for this bank to serve its customers and compete in the marketplace, it will need to grow assets, which leads to more income to pay for compliance and technology. If loan problems surface and classified loans increase, a smaller bank has less capital to protect against loan losses. Smaller banks also have a harder time raising additional capital than larger banks.

The Shrinking Strategy also could result in key personal leaving the bank because of the fear of job loss or lack of compensation growth.

As illustrated by this example, the components of the Basel III NPR will make it extremely difficult to pay off TARP funds. Instead, the bank will need to deal with a significant increase in the cost of these funds. This is a particular problem in 2014 and especially in 2015, when Risk-based requirements for Common Equity Tier 1RBC and Tier One RBC are being phased in. In addition, the change in risk weights take effect in 2015, causing risk weighted assets (denominator of the three risk based capital calculations) to increase by an amount across the industry of 20% (as estimated in the Standardized Approach NPR).

Attachment B

MBA Basel III and Standardized Approach Proposals
Impact Survey – Chef Executive Officers Survey results

Composition of Survey Responses:

- ***Asset size***: Responding banks ranged in asset size from $100-250 million to $1-5 billion. The majority of respondents (58%) were banks with assets between $250-500 million.
    - $100-$250 million – (25%)
    - $250 - $500 million – (58%)
    - $500 million - $1 billion – (8%)
    - $1-$5 billion – (8%)

- ***Geographic range***: All Maryland regions were represented (capital region, central region, Western Maryland and Eastern Shore) except Southern Maryland. Responses included a strong showing from the central region and eastern shore areas (42% for both).

Survey Responses:

Survey responses indicated a variety of impacts of the proposed Basel III capital assessments. Below are details on specific impacts on respondent banks:

We looked at what would impact us from a high level. The main items are: Impact of Accumulated Other Comprehensive Income which is good now but will change rapidly once interest rates go up and they will go up. We are looking into Held To Maturity as opposed to Available for Sale as an alternative. The residential mortgages LtV will impact us modestly. We would definitely change behavior if a HELOC would push an existing loan from category 1 to category 2. We are concerned about the mortgage reps and warranties of sold loans impact. We are just ramping this up and it could become a significant number. While delinquent loans aren't an issue now it does concern us. We expect the DTA impact to impact us prior to the full phase in but not so much once it is entirely phased in.
These new changes will adversely affect our ability to grow and support our communities
While we have not done the internal assessment, the requirements of Basel III will have a significant impact on certain types of loans such as construction loans. This will definitely impact credit availability in the market and will have a ripple effect on many industries.
Mortgage lending is greatly impacted. In addition CRA lending where the Bank makes 100% loans increases from 100% capital requirement to 150%. Investor loans will no longer be part of our offerings.
The risk weighting changes affect our bank the most. The percent decrease in total risk based capital is almost 2%. The effects of the tax deferred asset calculations are also significant. Over 60% of our 1-4 family risk weighted assets are in the category one bucket.
Our bank and holding company are currently in excess of the capital required to be considered well-capitalized. If the proposed rules were implemented today with no phase-in period, we estimated that our holding company would not meet the well-capitalized standards. The most onerous impacts are a result of: 1) the disallowance of Trust Preferred Securities as Tier 1 Capital, 2) the deduction of unrealized losses from Common Equity and Tier 1 Capital, and 3) the increased deduction of deferred tax assets from Common Equity and Tier 1 Capital.

We estimate the impact of these items to be a reduction of our Common Equity Capital by 50% and our Tier 1 Capital by 52%. Additionally, we estimate that the impact of the various risk-weighting changes would be to increase our risk-weighted assets by 18%.
Estimate Capital Ratio: • Tier 1 8.01 current; 6.48 as of 1/18 • Tier 1 Risk Based 13.02 current; 8.53 as of 1/18, • Total Risk Based 14.29 current; 9.79 as of 1/18, • decrease of 19%, 34.5% and 31.5% Deferred tax of $340,000 disallowed, 1-4 family Category 1 13.9%; Category 2 86.1% % Risk Assets to total assets 64.4% currently; 76.6% as of 1/18, Net Unrealized Gains presently are $1.0 million; a 300 pb shock result in $1.1 million loss.
• Leverage decreased by 4 basis points; • Tier 1 Capital decreased by 165 basis points or 10.50%; Total Risk Based Capital decreased by 165 basis points or 9.72%. • 94% of 1-4 family residential are in category 1. Or, more importantly, risk weighted assets are increased by $14,727 or 12% under Basel III - a big increase. • Net unrealized gains (losses) will be a major impact.
• Tier 1 Leverage Ratio increased from 17.57 to 17.75 based on proposed inclusion of unrealized gains in AFS securities in common equity Tier 1 capital. • Common Equity Tier 1 Capital(New)decreased from 32.37 to 26.55 largely as a result of a 5.12 decrease in 1-4 Family Residential Mortgages which will now require a 100% risk weighting due their demand feature(presumption of compliance); • 0.63% reduction based on HVCRE which will now require a 150% risk weighting; and 0.40% reduction for unused commitments which will now require a 20% risk weighting. • Tier 1 Risk Based Capital Ratio same impact as Common Tier 1 Capital Ratio. Total Risk Based Capital decreased from 32.71 to 26.82 for reasons cited in Common Tier 1 Capital.
• At first the capital number will only go down slightly but as the rates increase the impact will be much greater which will cause us to drop below well capitalized to adequately capitalized. • The three biggest impacts will be in the Unrealized gains and losses which as rates rise to the 300 bp shock will drop us to the adequately capitalized level. • The loan side (1-4 family and cre) will decrease the capital number by about 10%. And the deferred tax will also lower the Capital by about 5%

83% of survey respondents reported that lending would be severely impacted if Basel III is adopted as proposed. The specific types of lending and the percentage of respondent banks impacted follow:

- 1-4 family residential real estate – (67%)
- HELOC – (67%)
- AD&C Lending – (50%)
- Small Business Lending – (33%)
- Commercial and Industrial Lending – (25%)
- Personal Loans and Lines – (8%)
- Construction Loans, residential & commercial, development loans, and non-owner occupied commercial real estate – (8%)

Commentary on how lending is impacting follow:

Commentary: While perhaps not severely limited, if the presumption of compliance is that our 1-4 residential mortgages with a demand feature are "non traditional" or considered to be a "balloon" product, our risk weighting for this assets class increases by 50 bp. We may have to eliminate the demand feature in our 1-4 family residential mortgage product, which we have offered for over 100 years, and our customer have become accustomed too.
Commentary: If 1-4 family residential loans are risk weighted 100% it will definitely change our strategy in going after those loans. In our market area that is a significant loss to the public.
1-4 Family Residential Real Estate, AD&C Lending, HELOC. Commentary: These products are most impacted by the proposed risk-weighting changes.

83% of respondents reported that product offerings would change as a result of the Basel III capital standards. Examples are listed below.

Lending will have to be curtailed in the 1-4 family, Heloc's and small business. All of this is the backbone of the community bank lending arena. The economy will suffer even greater if this happens.

As we will not be able to write balloon mortgages we will be forced to write 10 and 15 fixed term mortgages. This will result in low production and potential increase in interest rate risk. A&D loans to small real estate developers will not be affordable.

HELOCs will be more limited and we will not extend them to good customers if it took us over the appropriate LtV thresholds. We will focus our secondary market mortgages to investors with the shortest reps and warranty periods. ADC loans will be priced much differently if we do them at all.

We will have to re-evaluate the returns necessary on each product to cover the additional capital to be required on each loan type. Pricing on such products will have to be adjusted, which may result in less availability of those products to our customers. Re-pricing new offerings will do nothing to recoup the impact of the proposed rule changes on the existing loan portfolio.

For certain product types, such as AD&C lending, it may not be practical to make such a loan as the capital requirements will make it unprofitable. Banks will also need to avoid certain types of 1-4 family loans thus reducing credit availability in the market.

I am not sure how we can continue to make certain types of mortgage loans in the future - CRA financing

We will be very careful about all loans going forward if basil three is adopted. We must preserve capital so growth is going to be very carefully measured. We do not want our capital ratios to decrease as a result of asset and loan growth. Therefore it will be several years before we can have a good program of loan and asset growth because the only meaningful way to see Capital increase is the addition of profits. Profits in our market area are hard to come by. Raising capital by stock sale is virtually impossible. Investors who know about these new capital proposals realize that most banks will not be a will to pay any significant cash dividends for some years to come since they will have to accumulate profits, and add profits to capital, to meet higher capital standards. This makes it harder to sell stock, And has had significant adverse effect on the stock price of banks on the Delmarva peninsula

We will lower our LTVR guidelines, which will adversely affect our ability to lend and compete with the Mega-banks.

92% of survey respondents reported that the effects of Basel III would have a negative impact on the availability of credit, cost of services, economic recovery. Examples follow:

Availability of credit

- The capital standards affect our customers by making loans harder to get. Since we do not want to see growth because that would have an adverse impact on our capital ratios, we will not be increasing in either deposits or loans. This has a significant impact on our economic recovery since our area has no large economic driver. There are numerous economic drivers in the Baltimore Washington metropolitan areas that do not exist on the Delmarva peninsula
- Possible re-design of our 1-4 residential mortgage offering(s) and further tightening of already restrictive underwriting criteria.

- These new standards will hurt our ability to lend to small businesses
- Certain types of loans just won't be done. Small businesses are often financed with real estate as collateral. Residential construction is an industry that is an employment backbone of our economy. Until it recovers, the economy will continue to be slow. ADC is the first step and it is being hit hardest. An unintended consequence will be a slower recovery in this segment.
- Small builders and developers will be forced to close shop or seek financing through nonbanks. Low/moderate income consumers, ones with blemishes on credit and irregular properties will have difficulty finding financing. We historically have looked at all credit and property factors when making loans, will not be able to do this due to the rigidness of the capital rules

Cost of services

- We will look to increase fees, reduce employment expenses (through staff reductions and hiring freezes), and increase origination points to offset the natural loss of loan volume. The regulatory environment already dictates a strict underwriting climate.
- Higher interest rates on mortgage offerings and
- Fee income would have to be increased to subsidize earnings
- High capital will require adjustments to pricing.

Impact on Economic Recovery

- Less capital available to fund local economic activity will be the outcome.
- These new standards will hurt our ability to lend to small businesses, which will deliver another blow to an already WEAK economy.
- If we are unable to continue to lend to the small business customer, the 1-4 family (that doesn't qualify on the secondary market) and Helocs then they will start leaving the community banks. The economy cannot recover if this happens
- I believe it will kill the housing industry.
- A likely solution to the increased capital burden will be to reduce the size of our asset base. Not only will this reduce our ability to do new lending, it will reduce our need for customer deposits. Having a significantly smaller asset base will also likely change the size and composition of our workforce. All of these potential actions will hurt our existing customer and employee base and prolong the achievement of a full financial recovery. The retroactive application of the risk-weighting % changes to loans will require a significant effort on the part of the loan servicing staff to research individual loan files in order to populate our core processing system with the information needed to make the risk weighting determinations.

33% of responding banks reported using a balloon payment structure on 1-4 family residential mortgage first liens.

- The extent of institutions using a balloon payment structure varied considerably – some reported using balloons "occasionally" others "extensively."
- One respondent was uncertain if a specific loan product (call or demand loan) would meet the definition of a balloon loan under the proposals.

Survey respondents assessed what percentage of "Category 1" loans they would have (those without balloons) and what percentage of "Category 2" loans (those with balloons) under the proposals:

Percentage of Category 1 Loans	Percentage of Category 2 Loans
42% reported 75% or more of loans as Category 1	8%-- reported 75% or more as Category 2
8% -- reported 50-75% of loans as Category 1	17% -- reported 50-75% as Category 2
8% -- reported 20-30% as Category 1	8% -- reported 40-50% as Category 2
8% -- reported 10-20% as Category 1	17% -- reported 20-30% as Category 2
8% -- reported 5-10% as Category 1	8% -- reported 5-10% as Category 2
	25% - reported less than 2% as Category 2

67% of responding banks reported between 60-90% of their loans fits into the new LTV tables for risk weighting of Category 1 loans. Detailed summary follows.

- 25% of survey respondents reported 80-90% of their loans
- 42% of survey respondents reported 60-80% of their loans
- 25% of survey respondents reported less than 60% of their loans

33% of banks reported between 80-90% of their loans fits into the new LTV tables for risk weighting of Category 2 loans. Detailed breakdown of responses follows.

- 33% of survey respondents reported 80-90% of their loans
- 8% of survey respondents reported less than 90% of their loans
- 50% of survey respondents reported less than 80% of their loans

Banks assessed the effect that the proposal to bump the risk weights on all "High Volatility Commercial Real Estate Loans" up from 100% to 150%. These loans are basically defined as all non 1-4 family acquisitions, construction, and development loans

- 33% reported they would discontinue financing in this area
- 33% reported that they did not offer ACD loans, or had so little in that category that the additional risk weighting would not have a significant impact
- 25% reported that the change would add to their risk weighted assets
    - It will add $5.1 million to our risk weighted assets.
    - Bank would see a .63 bp decrease in Tier 1 and .64 bp decrease in Total risked based capital based on 6.30.12 financials.
    - We estimate that our right weighted assets will increase by approximately 1% because of this change.

Survey respondents reported the impact of the Basel proposal to bump the risk weights on Nonaccural Loans and 90+ day Past Due Loans (excluding 1-4 family and Gvt./FDIC guaranteed loans) up from 100% to 150% have on their banks.

<u>Respondents indicated important impacts to customer service</u>

- Due to the affect on capital ratios from this change we will no longer be able to work with customers to give them extended periods of time or be willing to enter into forbearance agreements.
- We will be forced to dump troubled assets at lower prices, adversely affect profitability and flood the market with more negative comps.

<u>33% reported an impact to capital</u>

- Because we have a larger amount of non accural on our books, it has a significant impact on the overall capital.
- The obvious on required capital levels but should not impact materially.
- About a 2.5% decrease in the risk based calculation.
- It will add $5.4 million to our risk weighted assets.

<u>17% of respondents indicated they would have to reduce lending</u>

- It will reduce lending availability as balance sheets will need to shrink to fit under the new rules.
- Limit us from making new loans until we are able to remove this issue.

<u>25% reported nominal impact</u>

- This would have no effect since we are a conventional residential 1-4 family lender. Our delinquencies over 90-150 are less than 1% of our total portfolio.
- None at this time, but it will.
- Nominal impact based on 6.30.12 financials.

Survey respondents provided detailed concerns about credit admin, reporting, credit availability, borrower impacts or product impacts that the proposed Basel III capital standards will have:

Due to affect on interest rate risk and capital our growth will be severely limited. We will evaluate marginally profitable branches and consider closing them. We may need to hire additional backroom people to comply with the reporting requirements. Many of our historic borrowers will have to go to credit unions, finance companies and other nonbank institutions for their loans.
My concerns are as we try to expand our lending into other areas i.e. Commercial R.E. - it would seem that those rates need to be adjusted to alleviate the inherent risk associated with that type of lending. It will certainly put a stain on the Commercial R.E. market - it may fuel inflation and deals that could or should have been done may not be due to the regulatory environment.
The current capital markets are for the most part not a viable option for most community banks. If even available, it is expensive and dilutive to raise common equity capital in the current environment.
This is an absolute disaster for community banks, especially those less than $1.0 billion in assets. What are you thinking?
Credit availability will most definitely be decreased.
Because the size and complexity of our bank does not justify the resources to be put into Software and labor to do the new basil three calculations, it will result in a dead cost to us and additional labor to calculate capital based upon the new standards. Obviously credit administration will be strained. Credit availability will be lessened. The impact on the borrower will be the credit is harder to come by. We will streamline our products further And may cut back on much of our small business lending. We do not want to see loans risk weighted higher than they already are.
It is another resource drain taking away from our mission to serve the local economy and citizens.

Survey respondents described the challenges to their bank in raising additional or replacement capital in this environment or in the event the Basel III requirements are implemented as proposed

Capital formation in small communities is challenging - almost impossible. If operating under a regulatory order, virtually undoable. It requires outside private assistance and those entities demand board seats, etc. Places a proactive board in unknown territory with few options. It is a mandate to sell and let small communities fend for themselves with the large banks.
We are a non-public company, our stock does not trade. Going to the capital markets will be difficult as we will be competing with public companies that report in the press and are followed by institutional investors. Our shareholders have been paid dividends since 1899 and it will be difficult to project a continuation of dividend payment due to the buffer on top of capital standards. We would only need a couple million in capital and cost to raise small amounts of capital is large on a relative basis.
Ours is a simple process - we are a true mutual - we have no holding company - thus our capital increases via our net income.
Increased capital will have an impact on the returns for community banks and in turn will impact the investment community's interest in the market segment. Capital is difficult to find today - this will only make that problem worse.
As stated previously, it is virtually impossible for a bank on the Delmarva Peninsula to raise additional capital for the sale of stock given the cloud that looms over the head of every community bank. We do not operate under any regulatory order but Stock prices for Community Banks in our area have plummeted. The only meaningful way to increase our capital is a no growth slow growth or even shrinkage strategy. Growing the bank only decreases your capital further. These rules are designed to Shrink or eliminate the community banks operating in my market area
We are a non-public bank and access to capital is already frozen. Now, you are discontinuing Trust preferred securities. The big banks, can excess all kinds of capital markets. Simply put.....No capital equals no future growth which equals No need for lending which hurts small businesses succeed which hurts the overall economy of this once great Nation. If your desire is to eliminate community banks, these changes will do it!!

Attachment C

MBA Basel III and Standardized Approach Proposals
Impact Survey – Chief Finance Officers Survey results

Composition of Survey Responses:

- *Asset range*: Respondents ranged from $50-100million to $10 billion or above categories. The majority of respondents (53%) came from small to mid-sized banks ($250-$500 million)
  - $50-$100 million – (6%)
  - $100 - $250 million – (12%)
  - $250-$500 million – (53%)
  - $500 million - $1 billion – (18%)
  - $1-$5 billion – (6%)
  - $10 billion or above – (6%)
- *Geographic range*: All Maryland regions were represented in survey - including the Capital Region, Central Region, Eastern Shore, Southern and Western Maryland. The bulk of responses came from central Maryland (53%) and the Eastern shore (24%)

Survey Responses:

Impact of Basel III on bank's capital – 65% of survey respondents reported they would face a reduction in capital levels under the Basel III proposals. Below are some examples of the estimated impact:

- In general our capital ratios are stable or slightly improve with Basel III. But when we apply a 3.00% rate shock to our AFS securities our capital ratios fall dramatically by over 2.00% to adequately capitalized. We feel this will cause us to dramatically adjust our investment strategy where we will substantially shorten our duration of our portfolio and most likely shift a significant portion to held to maturity. These actions will reduce our earnings and place unneeded pressure on our liquidity. This will both slow the growth rate of the bank and impair loan growth.
- We currently use our investment portfolio to mitigate the inherent liquidity and interest rate risks within our balance sheet. As a result of this FMV inclusion in our capital calculation we might consider this capital implication in the structure and strategy in our investment decisions which could inhibit our ability to manage other risks.
- Small community bank (asset range $100-$250 million) - $2,166,000 dollar change; decrease capital by 48 basis points (6.3% decrease).
- Our most recent analysis projects a decrease in market value of investments of 12.8% given a 300 bp increase in rates. Carried through to equity, this has a negative impact on our unrealized loss on securities AFS of $4.75 million. Tier 1 capital would decrease by 20.71% and total capital would decrease by 19.38%. According to the capital calculator distributed on 9/24/12, our bank would be reclassified from well capitalized to adequately capitalized.
- It will reduce total regulatory capital by approximately $5.3 million or 12.4% which in turn would lower our total RBC ratio by 36 basis points
- A 300 bp shock increase in interest rates would reduce the economic value of our AFS securities portfolio by approximately $20 million or 8.6%
- Decline of $1,117,000 or 4.71% of capital
- $248 million decrease in investment portfolio value with a 300 bp shock; this would reduce capital by approximately 200 bp.
- The 300 bp shock would decrease our requity by $2,351 or 23.72%
- Decrease capital by $4.3 million which is about 20.8% of reported capital.

100% of survey respondents indicated that their institutions would be affected by the following capital and risk weighting changes. Below is a list of specific changes impacting the banks:

- 10% / 15% threshold – deferred tax assets – temporary timing differences
- 1-4 family loan category 1 and 2 determination
- 1-4 family loan to value determination
- 1-4 family mortgage loans sold risk weighting
- 1-4 family risk weighting
- Conversion buffer and impact on dividends / buybacks/ bonuses
- Deduction of unrealized losses (other than CF hedges)
- Disallowance of deferred tax assets – NOL carryforwards
- Gain on sale of securitization exposure
- Goodwill deduction
- High volatility CRE (HVCRE)
- Mortgage servicing assets
- new common equity RBC ration
- off balance sheet commitments risk weighting
- past due asset risk weighting
- structured securities risk weighting
- Trust Preferred Phase out as Tier 1 Capital – Institutions under $15 billion
- Unrealized gain/loss on cash flow hedges

Following are examples of how the capital and risk weighting changes impact respondent banks:

- To minimize impact - Restrict loan growth and overall balance sheet growth, delay repayment of TARP preferred stock

- 1) Disallowance of Deferred Tax Assets - NOL Carryforwards: (effect $340K disallowed) - no response figured out yet;
  2) 1-4 Family Category 1 and Category 2 Determination: ($34,400K moved to cat. 2) - limit lending in this area;
  3) 1-4 Family Loan to Value Determination: (adds $1,907K to risk rated assets) - limit lending in this area;
  4) High Volatility CRE (HVCRE): (adds $4,400K to risk rated assets) - limit lending in this area;
  5) Past Due Asest Risk Weighting: (adds $1,407 to risk rated assets) - work less with customers - more aggressively pursue delinquent accounts.

- The goodwill and DTA reductions will have a negative effect regarding future merger and acquisition activities. I don't think this can be minimized. The gain on sale is disastrous to our company. We will have to make dramatic changes to our investment strategies which will substantially reduce our earnings to a sub par level

- 1-4 Family category: our $29MM of residential loans are 5 year balloons (for interest rate risk management purposes), so we would have a risk weighting of 100% instead of 50%, reducing our risk weighted capital ratio by approx. .75%. Past due: moving from 100% risk waiting to 150% will impact us. Off balance sheet commitments: our $23MM of commitments at the new risk weighting factor of 20%will reduce our capital ratios by .25%

- Trust preferred - refinance with qualifying capital; High volatility CRE and residential mortgage exposures - revise underwriting criteria

- 1-4 Family risk weighting: Due to lack of regulatory guidance we have assumed that our entire 1-4 family loan portfolio will be deemed non-traditional mortgages and risk weighted @ 100% due to the demand feature (i.e. call option) within all of our mortgage loans. We would no longer include the demand/call in our 1-4 family mortgages which will negatively impact our IRR.

- Every change would negatively impact our capital ratios

- LTV determination and HVCRE will be impacted. Regulators should consider grandfathering existing loan portfolio to minimize impact

100% of survey respondents reported their bank will face new reporting challenges and costs to comply with the Basel III capital proposals? Below are specific examples.

- We have not specifically determined the effect, but the amount of additional time for preparation of the call report and systems changes for loan accounting and reporting will be very substantial and onerous for our bank

- Each 1-4 family loan would have to be individually coded for its appraisal value for loan to value determination and reviewed for a category 1 and 2 classifications. These new classifications and review would require an additional FTE possibly more with the growth of our portfolio

- The most significant challenge is in obtaining the data to accurately calculate the risk weighting for residential mortgage exposures. We have such exposures on two different systems - one for residential mortgages and one for HELOC's; marrying this information to identify multiple exposures to the same borrower will be difficult. Capturing LTV's will also be a challenge. At this point, it is difficult to estimate the cost

- Additional common capital rise in order to exceed equity ratio and still grow balance sheet while replacing TRUPs phase out. LTV and 1-4 family category 1 and 2 will require programming and staffing for call report (costs yet to be determined)

- 1-4 Family Cat 1/2: May require extensive time and expense if existing demand mortgage portfolio is not grandfathered. No estimates available. 1-4 Family LTV: If the existing portfolio not grandfathered the loan department would require significant time to assess the current portfolio and input data into the core system. Minimal time is needed to modify the core system to accept the data. HVCRE: If the current portfolio is not grandfathered we would assume all ACD loans are HVCRE.

- Will take approximately 100 staff hours to input updated appraisals on modified loans in order to determine loan to value percentages. Will take approximately 100 staff hours to input updated appraisals on modified loans in order to determine loan to value percentages. The effect of these loan to value percentages and the off balance sheet commitments risk weighting is the reduction of our RBC ratio to below the buffer zone. Even though we will still be well-capitalized, our dividends/bonuses will be restricted.

- The changes in risk-weighting of mortgage loans and past due assets will require additional time and reporting. The issue of DTA's, however, will change the way we account for that line item entirely. We currently calculate changes in DTA's at year-end with the assistance of our auditors. Calculating these values on a quarterly basis will require more staff time, training and additional audit cost. It will also change our tax expense

- We will have to pay for modifications to our current software to provide the detail needed - we do not know the cost of modification and we would also spend a lot of time inputting the information to get good output after system modifications

Attachment D
MBA Member List, Asset Size and Chartering Agency

Company Name	City	State	Total Assets MstRctQtr ($000)	Chartering Agency
Advance Bank	Baltimore	MD	63,030	Federal
Arundel FSB	Glen Burnie	MD	485,621	Federal
Baltimore County Savings Bank	Baltimore	MD	640,602	State
Bank of America NA	Charlotte	NC	1,445,093,157	Federal
Bank of Delmarva	Salisbury	MD	424,218	State
Bank of Glen Burnie	Glen Burnie	MD	377,583	State
Bank of Ocean City	Ocean City	MD	209,304	State
BankAnnapolis	Annapolis	MD	437,422	State
Bay Bank FSB	Lutherville	MD	126,320	Federal
Bay-Vanguard FSB (MHC)	Baltimore	MD	148,433	Federal
BlueRidge Bank	Frederick	MD	165,519	State
Branch Banking & Trust Co.	Winston-Salem	NC	173,678,238	State
Calvin B. Taylor Bnkg Co MD	Berlin	MD	433,631	State
Capital Bank NA	Rockville	MD	413,943	Federal
Capital One NA	McLean	VA	158,240,417	Federal
Carroll Community Bank	Sykesville	MD	98,485	State
Carrollton Bank	Columbia	MD	359,739	State
CFG Community Bank	Lutherville	MD	468,808	State
Chesapeake B&TC	Chestertown	MD	96,141	State
Chesapeake Bank of Maryland	Baltimore	MD	196,598	Federal
CNB	Centreville	MD	451,864	State
Columbia Bank	Columbia	MD	2,016,401	State
Community Bank of Tri-County	Waldorf	MD	972,383	State
Congressional Bank	Bethesda	MD	332,566	State
County First Bank	La Plata	MD	195,669	State
Damascus Community Bank	Damascus	MD	253,593	State
EagleBank	Bethesda	MD	2,952,334	State
Eastern SB FSB	Hunt Valley	MD	550,996	Federal
Easton B&TC	Easton	MD	153,415	State
Fairmount Bank	Baltimore	MD	79,329	Federal
Farmers and Merchants Bank	Upperco	MD	274,280	State
Farmers Bank of Willards	Willards	MD	329,382	State
First Shore FS&LA	Salisbury	MD	313,351	Federal
First United Bank & Trust	Oakland	MD	1,342,977	State
Fraternity FS&LA	Baltimore	MD	174,828	Federal
Frederick County Bank	Frederick	MD	309,778	State
Glen Burnie Mutual Savings Bk	Glen Burnie	MD	76,353	State
Hamilton Bank	Towson	MD	315,752	Federal
Harbor Bank of Maryland	Baltimore	MD	253,594	State
Harford Bank	Aberdeen	MD	289,722	State
Hebron SB	Hebron	MD	504,765	State
Homewood FSB	Baltimore	MD	73,986	Federal
Howard Bank	Ellicott City	MD	356,082	State
Industrial Bank	Washington	DC	350,762	State
Jarrettsville FS&LA	Jarrettsville	MD	106,399	Federal
Liberty Bank of Maryland	Baltimore	MD	42,705	State
Madison Bank of Maryland	Forest Hill	MD	153,226	Federal
Madison Square FSB	Baltimore	MD	156,961	Federal
Manufacturers & Traders Tr Co.	Buffalo	NY	79,846,314	State

Attachment D
MBA Member List, Asset Size and Chartering Agency

Maryland Financial Bank	Towson	MD	71,617	State
Middletown Valley Bank	Middletown	MD	148,280	State
Monument Bank	Bethesda	MD	392,132	State
National Bank of Cambridge	Cambridge	MD	213,124	Federal
NBRS Financial Bank	Rising Sun	MD	232,364	State
New Windsor State Bank	Taneytown	MD	272,021	State
North Arundel SB FSB	Pasadena	MD	39,412	Federal
OBA Bank	Germantown	MD	392,090	Federal
Old Line Bank	Bowie	MD	839,245	State
Patapsco Bank	Dundalk	MD	254,487	State
Peoples Bank	Chestertown	MD	250,254	State
PeoplesBank A Codorus Valley	York	PA	1,041,866	State
PNC Bank NA	Wilmington	DE	291,824,058	Federal
Presidential Bank FSB	Bethesda	MD	527,468	Federal
Prince George's FSB	Upper Marlboro	MD	102,451	Federal
Provident State Bank Inc.	Preston	MD	291,152	State
Queenstown Bank of Maryland	Queenstown	MD	451,574	State
Regal Bank & Trust	Owings Mills	MD	174,336	State
Revere Bank	Laurel	MD	340,928	State
Rosedale FS&LA	Baltimore	MD	800,304	Federal
Saint Casimir's Savings Bank	Baltimore	MD	104,145	State
Sandy Spring Bank	Olney	MD	3,852,600	State
Severn SB FSB	Annapolis	MD	891,475	Federal
Shore Bank	Onley	VA	307,111	State
Slavie FSB (MHC)	Bel Air	MD	177,378	Federal
SunTrust Bank	Atlanta	GA	172,028,459	State
Susquehanna Bank	Lititz	PA	17,937,233	State
Talbot Bank of Easton MD	Easton	MD	709,114	State
TD Bank NA	Wilmington	DE	195,942,864	Federal
Vigilant FSB	Baltimore	MD	56,963	Federal
Wells Fargo Bank NA	Sioux Falls	SD	1,180,190,000	Federal
Woodsboro Bank	Woodsboro	MD	232,662	State