# CFG Community Bank

October 22, 2012

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

Office of the Comptroller of the Currency
250 E Street, SW
Mail Stop 2-3
Washington, DC 20219

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

Re: Basel III Capital Proposals

Ladies and Gentlemen:

We appreciate the opportunity to comment on the proposed new regulatory capital standards for US banks based on the Basel III international framework for bank capital adequacy, stress testing and market liquidity risk.

While we share the concerns that have been expressed by our colleagues and trade groups about the broad reach of the proposed regulations and its inappropriateness for small community banks, the most serious concern for CFG Community Bank is the proposal to drastically reduce the allowable limit of mortgage servicing rights (MSRs) from 90% to 10% of Tier 1 common capital. This proposal would inaccurately define CFG Community Bank as undercapitalized, despite the fact that the bank is one of the best-capitalized institutions in the region. Were the Basel III Proposal in effect as of June 30, 2012, the Bank's total risk based capital would be reduced from $53.3 million to $24.0 million, and its common equity tier 1 capital would be reduced from $49.2 million to $19.9 million. Given these reductions, the Bank would go from a well-capitalized institution, with a 14.97% common equity tier 1 ratio, 14.97% tier 1 capital ratio, 16.22% total capital ratio, and an 11.73% leverage ratio, to undercapitalized under several of these measures, with a 6.04% common equity tier 1 ratio, 6.04% tier 1 capital ratio, 7.29% total capital ratio, and a 5.09% leverage ratio.

MSRs associated with a residential servicing portfolio have different characteristics than those associated with commercial mortgage servicing. The proposal to limit MSRs as a portion of capital was most likely developed for residential mortgages, which can be paid off at any time. While a change in a person's personal circumstances cause some early pay-offs, the overwhelming majority of early mortgage pay off is lower interest rates.

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In addition to being a community bank serving the central Maryland market, CFG is also a mortgage banker providing financing to long-term care facilities nationwide. Capital Funding, LLC, a wholly-owned subsidiary of CFG Community Bank, provides financing for healthcare facilities primarily under the Federal Housing Administration's (FHA) Section 232 program. These loans are securitized by GNMA and sold to investors with servicing retained by Capital Funding LLC.

These GNMA securities or "project bonds" have unique characteristics. Typically, the borrower cannot pay off the note within the first two years and there are prepayment penalties in years three through ten. This structure affords the holder of the GNMA security (as well as the owner of the servicing rights) a far more protection against prepayments than for holders and servicers of standards residential mortgages. As a result, the related MSRs of GNMA project bonds hold their value much better and for longer than residential mortgages.

The average note rate of CFG Community Bank's servicing portfolio is approximately 5% while rates on current loan production are approximately 3% or less. With an average note of $6 million, the note holders prefer the lower rates currently available. However, the note holders must wait for the prohibition to expire and for the penalty to decline to the point refinancing is economically advantageous. Therefore, unlike residential mortgages, the refinancing of FHA-insured healthcare mortgages is largely predictable. The prepayment safeguards in GNMA project bonds positively impact the value of servicing rights.

Capital Funding, LLC originates these loans and is the lender of record. Currently this subsidiary of CFG Community Bank has a servicing portfolio over $2 billion with related servicing rights of $39 million. There are currently no delinquencies in the portfolio. In fact, Capital Funding, LLC and its predecessor company has never made a claim against the FHA insurance fund.

The vast majority of tangible capital approved by the Federal Reserve Bank and the State of Maryland in the acquisition of AmericasBank Corp, Inc. by Capital Funding Bancorp, Inc. was the value of MSRs. Capital Funding Bancorp, Inc. completed its acquisition of AmericasBank Corp, Inc., the holding company for the severely troubled AmericasBank, in August 2009. Capital Funding Bancorp, Inc. infused approximately $33.6 million of tier 1 tangible capital into AmericasBank in the approved plan of merger. The $33.6 million of contributed capital included $25.8 million of MSRs that were all associated with GNMA agency commercial mortgages as described above. The value of the MSRs was approximately 77% of the value of the contributed capital.

The strength of the new institution is evident when one considers the approximately $13.4 million in additional charge offs since the acquisition yet CFG Community Bank remains well capitalized.

In 2011, the Federal Reserve and State of Maryland accepted CFG Community Bank's plan to orderly reduce the amount of MSRs to be included as Tier 1 capital as part of an overall plan to reduce concentration in healthcare. In the proposed plan, the value in MSRs as a percent of Tier I capital is targeted to reduce to 70% by December 31st, 2012 and to 50% by December

31st, 2013 where it would remain. The current Federal Reserve proposal would supersede this agreement and could negatively impact the perception of CFG Community Bank's soundness despite the fact that there has been no change in the loan portfolio of the bank.

Furthermore, the disposition of the MSRs to monetize their value could affect the liquidity of banks. The bank holds approximately $100 million in deposits associated with commercial mortgage servicing, including P&I accounts, T&I accounts and replacement reserves as required by FHA regulations. Loss of these deposits will have a significant impact on the liquidity of CFG Community Bank.

The severe limit on the value of MSRs in the proposed rule would also likely negatively impact credit availability for healthcare facilities nationwide. FHA mortgage insurance is vital to the long-term care community and other communities as well, such as multifamily housing. Capital Funding, LLC services its FHA-insured loans both because of the complexity of dealing with federal regulations and to provide increased efficiency and value to its customers, many of whom have several FHA-insured loans throughout the life of a property.

By limiting MSRs to 10% of Tier 1 capital, healthcare facility owners and operators across the country will find financing increasingly difficult when the number of seniors and their families seeking decent, safe and sanitary facilities is growing rapidly. Limiting the availability of credit to these institutions will harm local economies and leave families without viable healthcare and housing alternatives.

Once again, we thank you for the opportunity to comment on these proposed regulations. We trust that as you consider the implications of the proposal on small, community-based institutions such as ours that you will recognize the need for serious changes. Clearly, the health of the economy and the ability of healthcare institutions and other businesses to have access to capital must be maintained.

Sincerely,

A. Gary Rever

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Chief Executive Officer