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NORTH SHORE BANK

David J. LaFlamme
President and Chief Executive Officer

October 18, 2012

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

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

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

Re: Basel III Capital Proposals

Ladies and Gentlemen:

Thank you for the opportunity to provide comment on the Basel III proposals that were recently approved by the Federal Reserve Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (collectively the "banking agencies").

<u>Background of North Shore Bank</u>

North Shore Bank, a Co-operative Bank was founded in 1888 as a mutual cooperative bank under the name Peabody Cooperative Bank to serve the citizens of Peabody, Massachusetts. Its mission, typical for a cooperative bank, was to meet the banking needs of the community with mortgage and consumer loans, along with savings and share accounts. As the community's needs grew, so did North Shore Bank where now the Bank has seven locations in surrounding communities serving the needs of consumers and small businesses through various commercial and consumer products and services. North Shore Bank is the sole remaining bank that was originated in the City of Peabody, which has a current population of 52,000 as of 2011. North Shore Bank, as a mutual cooperative bank, is very active in the communities we serve through staff volunteering at civic events, serving on Boards of non-profit organizations, funding various civic endeavors, and contributing funding to various charitable organizations. The Bank's funding to small businesses, along with consumer lending to mid-lower income individuals is reflected in our consistently strong CRA results.

On behalf of North Shore Bank, I am commenting on two components of the Regulatory Capital Rules referred to as Basel III. I am in support of increasing the capital requirements for all financial institutions in our country to protect our financial system and citizens from future economic downturns. This, I believe is a common goal you will hear from most in our industry. North Shore Bank, like many community banks in our country, wants to continue serving and helping our communities. A strong economy is a function of strong demand for goods and services, which businesses produce when capital is available to assist business growth. Capital availability is key to sustain economic expansion. I am concerned that the proposed capital rules will limit available capital to support growth, especially for the community banks.

The following areas are my main concerns with the proposed capital rules:

The impact of unrealized gains or losses on available for sale securities will now flow through regulatory capital versus Accumulated Other Comprehensive Income (AOCI).

This capital change will positively benefit most banks today in this unprecedented period of low interest rates, as most banks have material gains in their investment portfolio. When interest rates begin to rise, the unrealized gains in the portfolio will quickly turn into unrealized losses for no credit reasons, just for interest rate risk purposes. (Most community banks invest in fixed Treasury or GSE income securities.) There is no change to the banks' pure capital. The regulatory capital ratios will decrease in some cases substantially. This piece of the proposal is counter-intuitive, in my opinion, to what the goal should be.

Under a rising rate scenario, to compensate for a lower capital levels, banks may be forced to reduce the size of their balance sheets. This could undermine an economic recovery as banks are forced to reduce lending to shrink the balance sheets to maintain capital ratios. Our small business customers and consumer customers will be negatively impacted by this and not to mention the lost business opportunity for North Shore Bank.

Through the Bank's balance sheet simulation modeling, a 400 basis point rate increase (this will bring the Fed Funds rate back to a historical average since 1990) will negatively impact our capital ratio by 26 basis points or approximately $1 million, which based on a 10% leverage capital ratio equates to $10 million of reduced credit opportunities for our customers. An alternative approach could be to exempt Treasury and Government Agency (GSE) issued securities from this provision, since there is no credit risk concern, but be applicable to all other investments where there could be credit risk exposure.

The impact of increasing the risk weighting for residential mortgage loans.

North Shore Bank serves a significant number of citizens in our market area with mortgage loans. The proposed risk-based weighting of loans by loan-to-value ratios (LTV) and some of the proposals considered by the Consumer Financial Protection Bureau threaten a sizeable portion of our business. One of the purest banking products offered is a home mortgage. By penalizing banks that lend to individuals that do not have 20% or more for a down-payment, you may force banks to charge more for mortgages just to cover the negative capital impact, which would limit home buying opportunities. In addition, the administrative challenge for North Shore Bank is that the majority of our mortgage portfolio's LTVs are not on our loan applications. This would be a laborious exercise at best. We project it may require the Bank to devote one-half of an FTE just to assign correct risk weighting on all loans affected by the proposal. This is not a one-time assignment, you will need to re-evaluate the risk weightings based on changes of the collateral value, past-due status, and other risk factors. It appears that the "one size fits all" approach to this proposal will have a much greater negative impact to the community banks than the large banks that have a greater level of resources. Again, the community banks are being penalized for the mortgage crises that they did not create.

In conclusion, the proposal will negatively impact North Shore Bank and the industry by:

- Require a greater level of capital beyond the increase, which would occur as a result of the increased "capital ratios". The proposal either increases our risk-based assets or it will decrease our capital levels. This occurs with no change in the way we conduct our business.

- Currently, there is no way to quantify the impact to the Bank with respect to the training and staff allocation needed to implement the requirements, but we are certain there will be an ongoing cost. In addition to operating system costs to capture the required information and programming costs to produce the required reports, there may be also be consulting cost.

While I agree with the general concept of increasing the capital requirement for banks, the impact to community banks seems unfair. I urge you to look at the community banks differently or exempt them entirely from these complex and burdensome requirements that appear to be developed for large complex organizations.

Thank you for your consideration.

Sincerely,

David J. LaFlamme

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