Union Savings Bank
Francis G. Dattalo
President & Chief Executive Officer

October 22, 2012

The Honorable Thomas J. Curry, Comptroller
Office of the Comptroller of the Currency
regs.comments@occ.treas.gov
Docket ID OCC-2012-0008, -0009 & -0010

The Honorable Ben S. Bernanke, Chairman
Board of Governors of the Federal Reserve System
regs.comments@federalreserve.gov
Docket No. 1442

The Honorable Martin J. Gruenberg, Acting Chairman
Federal Deposit Insurance Corporation
comments@FDIC.gov
RIN 3064-AD95, -AD96 & -AD97

Re: Regulatory Capital Rules:
Regulatory Capital, Implementation of Basel III, Minimum Regulatory Capital Ratios, Capital Adequacy, Transition Provisions, and Prompt Corrective Action

Standardized Approach for Risk-Weighted Assets; Market Discipline and Disclosure Requirements

Advanced Approaches Risk-Based Capital Rules; Market Risk Capital Rule

Heads of the Agencies:

Union Savings Bank is pleased to comment on the Agencies' three joint notices of proposed rulemaking ("proposed rules") to implement agreements reached by the *Basel Committee on Banking Supervision in Basel III: A Global Regulatory Framework for More Resilient Banks and Banking Systems*, December 2010 ("Basel III Accord").

For background, Union Savings Bank is a $2.5 billion mutual bank headquartered in Danbury, Connecticut. The Bank serves western Connecticut with its network of 29 branch offices. The Bank is a market leader in terms of attracting retail deposits and providing financing to businesses and families. Like all community banks, we operate under a relationship-based model that is structured and managed to serve our customers and the communities in which we operate over the long-term. We are understandably proud of our practical and common-sense approach to managing the various business risks we are confronted with—not the least of which is capital risk management. Our mutual ownership structure is worth reinforcing here because our mutuality, we believe, is a true market differentiator. As we outline below, if the proposed rules are implemented, our ownership structure could become a significant liability—chiefly because as a mutual we have no way of growing capital other than through earnings, which limits our ability to respond to the proposed capital requirements.

We appreciate the opportunity to provide our perspective on the real-world consequences of the proposed rules and be part of a constructive process on the implementation of Basel III. We fully acknowledge and appreciate the difficulty of conforming the Basel III rules to our market, where we have substantially more banking organizations with a wider range of business strategies and economic concerns. We are of the view that the "one size fits all" approach of the proposed rules needs to be significantly sharpened and clarified to facilitate the practical implementation of Basel III in a way that enhances the quality and quantity of capital without the unnecessary drag on our operating efficiency and profitability.

At the risk of over stating the obvious, the implementation of rules as proposed will have a chilling effect on our business and by natural extension our customers and, in turn, economic activity in our market area, principally through decreased credit availability and increased credit costs. The sheer breadth and scope of the proposed rules warrants a comprehensive comment that addresses the totality of the proposals; however, other comment letters have been extremely effective in doing exactly that[1]. Therefore, we have limited our discussion to two of the more toxic proposals within the whole of the proposed rules: 1) the risk-weighting rules pertaining to residential mortgage exposures and 2) the change in the recognition of defined benefit pension plan liabilities in regulatory capital.

Residential Mortgage Market

As virtually every market observer/participant knows, the continued recovery of this sector of the economy is all but critical to sustaining a broad economic recovery. Yet the requirements of Basel III will clearly retard the recovery in the residential mortgage market. Among these requirements is the introduction of higher risk weights for residential mortgage loans reflecting borrower credit profiles based on various criteria that could cause a loan not to be characterized as a "Category 1" loan. As we are largely a portfolio lender, we are concerned that under the proposed methodology, a single loan criterion could trigger an unnecessary "Category 2" characterization, even though the overall credit profile is clearly of very high quality and therefore worthy of Category 1 risk weighting. While the vast majority of our residential mortgage originations meet the Category 1 standard, we nevertheless originate a significant volume of loans that would be Category 2 loans. Most of these Category 2 loans are derived from our propriety First Time Homebuyer (FTHB) program. At origination, these loans typically have loan-to-value (LTV) ratios greater than 80% and may also have terms beyond 30 years—either one of which criteria would lead to a Category 2 designation. Three facts to consider:

1) over the last 19 years, we have originated more that $260 million of such loans;
2) the credit performance of these loans is not materially different than that of under 80% loan to value and 30-year or less term loans; and,
3) realized losses as well as the current estimated credit exposure for such assets have been effectively and efficiently managed through our loan loss reserve.

As a real world example of just how punitive to regulatory capital ratios the proposed risk weighting changes could have on an institution, consider the following table which shows our as-stated and *pro forma* risk-weighting of our residential loan portfolio—as of March 31, 2012:

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[1] We respectfully request that the Agencies refer to the two comment letters submitted by Sandler O'Neill + Partners (dated September 6th and 20th, respectively). Collectively, these letters address every aspect of the proposed rules and provide outstanding business perspective and contain requests for (i) clarification, (ii) changes in implementation, and (iii) for non-implementation. Our goal mirrors that of Sandler O'Neill + Partners which is to contribute constructively to a rulemaking process that enhances the safety and soundness of the banking system without sacrificing efficiency and competitiveness or damaging the nascent economic recovery that we hope is under way.

As Stated

Current Residential Mortgage Portfolio:	Amount	Risk Weight	Risk Weight
1-4 Family First Lien	$1,026,666	50%	$513,333
1-4 Family Home Equity	133,543	100%	133,543
1-4 Family Junior Lien	17,011	100%	17,011
Total	$1,177,220		$663,887

Pro Forma Under Basel III

Category 1:	Amount	% of Category 1	Risk Weight	Risk Weight
< 60%	$240,240	30%	35%	$84,084
60 to 80%	304,304	38%	50%	152,152
80 to 90%	216,216	27%	75%	162,162
>90%	40,040	5%	100%	40,040
Sub-total	$800,799			$438,438

Category 2:	Amount	% of Category 2	Risk Weight	Risk Weight
< 60%	$0	0%	100%	$0
60 to 80%	56,463	15%	100%	56,463
80 to 90%	301,136	80%	150%	451,705
>90%	18,821	5%	200%	37,642
Sub-total	$376,421			$545,810
Total	**$1,177,220**			**$984,247**
Change				***$320,360***

As shown in the above table, the $320.4 million estimated increase in risk-weighted assets on the residential loans represents a staggering percentage increase of more than 48%. This is before we contemplate any other changes to risk-weighted assets (for example the High Volatility Commercial Real Estate loans. This risk-weighting, along with the impact of the recognition of the pension liability (see next item), serve to shave more than 200 basis points off our risk-weighted regulatory capital ratios. More specifically, our total capital ratio declines from an as-stated 12.16% to 10.01%. As noted above this is an estimate (albeit an accurate one we think), the secondary issues of complexity and cost of regulatory compliance while not capital constraining per se is nevertheless a huge issue for filers.

If the rules become final as currently proposed it would significantly weaken the economics of our FTHB program—which incidentally is one of the pillars of our Community Reinvestment Act program. It will, more succinctly, turn the financial economics upside down. To be sure, and to amplify an earlier point, less credit would be made available and at a higher credit cost. For this and other reasons, we respectfully suggest that a methodology for the overall credit profile be developed that takes into account (i) all relevant credit factors and (ii) loan seasoning rather than rely on a single factor for determining risk-weighting. This profile should also recognize high quality and properly underwritten loans with private mortgage insurance (PMI) in the determination of the LTV ratio for residential mortgage exposures.

Pension Liabilities

Generally accepted accounting principles require a banking organization that sponsors a single-employer defined benefit pension plan to recognize the overfunded or underfunded status of such a plan on its balance sheet as an asset or liability, with corresponding adjustments recognized in accumulated other comprehensive income ("AOCI"). However, for regulatory reporting purposes such tax-effected amounts are derecognized resulting in the exclusion from regulatory capital of any amounts recorded in AOCI. The proposal to recognize fully in common equity tier 1 capital defined benefit pension plan liabilities but to derecognize defined benefit pension plan assets except to the extent that a bank has "unrestricted and unfettered access" to such assets. Absent this exception, the proposed rules would result in the punitive capital treatment of pension plan assets and liabilities, reducing capital by the amount of recognized assets as well as liabilities. However, because the FDIC has unfettered access to the excess assets of an insured bank's pension plan in the event of receivership, the agencies have determined that generally a bank would not be required to deduct any assets associated with a defined benefit pension plan from common equity tier 1 capital.

That aside, whether a pension plan is overfunded or underfunded depends materially on the discount rate applied to very long-duration future cash flows. We believe that the assets and liabilities that the rule proposes to recognize in regulatory capital arise from temporary economic and market fluctuations—which are currently being heavily influenced by current monetary policy. We therefore believe that the current exclusion from regulatory capital of such assets and liabilities is more consistent with safety and soundness than their proposed inclusion. Reinforcing our belief is the fact that in receivership the claims of the FDIC would be senior to those of the beneficiaries of underfunded defined benefit pension plans, who would have the status of unsecured general creditors of a bank sponsor. In addition, we point out the regulatory agencies decision to exclude from regulatory capital any amounts recorded in AOCI resulting from the initial adoption and application of FAS 158 (ASC 715), *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans.* The very same logic that was applicable then is applicable today. It is our view that the inclusion in regulatory capital of pension assets and liabilities recognized in AOCI would only introduce unnecessary and counterproductive capital volatility that would in no way further protect the insurance fund in the event of a receivership. For this reason, we urge the Agencies not to implement this provision of the proposed rules.

Naturally, we would be pleased to further discuss our thinking with the Agencies.

Sincerely,

Francis G. Dattilo

cc: The Honorable Richard Blumenthal
United States Senator

The Honorable Joseph I. Lieberman
United States Senator