

BROOKLINE BANCORP INC  
Form 10-K  
March 01, 2013

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

**FORM 10-K**

ý **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934,**

**for the Fiscal Year Ended December 31, 2012,**

or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934,**

**for the transition period from N/A to .  
Commission File Number: 0-23695**

**BROOKLINE BANCORP, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation of organization)

**04-3402944**

(I.R.S. Employer Identification No.)

**131 Clarendon Street, Boston, Massachusetts**

(Address of principal executive offices)

**02117-9179**

(Zip Code)

**(617) 425-4600**

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

**Title of Each Class**

Common Stock, par value of \$0.01 per share

**Name of Each Exchange on Which Registered**

Nasdaq Global Market

Securities registered pursuant to Section 12 (g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1934. YES o NO ý

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Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Act of 1934. YES  NO

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirement for the past 90 days. YES  NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendments to this Form 10-K.

Indicate by check mark whether the registrant (1) has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12-b of the Exchange Act (Check one).

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark if the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES  NO

The number of shares of common stock held by nonaffiliates of the registrant as of February 27, 2013 was 70,093,202 for an aggregate market value of \$634.1 million. This excludes 333,918 shares held by Brookline Bank Employee Stock Ownership Plan and Trust.

At February 27, 2013, the number of shares of common stock, par value \$0.01 per share, issued and outstanding were 75,744,445 and 70,370,712, respectively.

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**BROOKLINE BANCORP, INC. AND SUBSIDIARIES  
2012 FORM 10-K**

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**FORWARD-LOOKING STATEMENTS**

Certain statements contained in this Annual Report on Form 10-K that are not historical facts may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and are intended to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve risks and uncertainties. These statements, which are based on certain assumptions and describe Brookline Bancorp, Inc.'s (the "Company's") future plans, strategies and expectations, can generally be identified by the use of the words "may," "will," "should," "could," "would," "plan," "potential," "estimate," "project," "believe," "intend," "anticipate," "expect," "target" and similar expressions. These statements include, among others, statements regarding the Company's intent, belief or expectations with respect to economic conditions, trends affecting the Company's financial condition or results of operations, and the Company's exposure to market, liquidity, interest-rate and credit risk.

Forward-looking statements are based on the current assumptions underlying the statements and other information with respect to the beliefs, plans, objectives, goals, expectations, anticipations, estimates and intentions of management and the financial condition, results of operations, future performance and business are only expectations of future results. Although the Company believes that the expectations reflected in the Company's forward-looking statements are reasonable, the Company's actual results could differ materially from those projected in the forward-looking statements as a result of, among other factors, adverse conditions in the capital and debt markets; changes in interest rates; competitive pressures from other financial institutions; the effects of continuing weakness in general economic conditions on a national basis or in the local markets in which the Company operates, including changes which adversely affect borrowers' ability to service and repay their loans and leases; changes in the value of securities and other assets in our investment portfolio; changes in loan and lease default and charge-off rates; the adequacy of allowances for loan and lease losses; deposit levels necessitating increased borrowing to fund loans and investments; changes in government regulation; the risk that goodwill and intangibles recorded in the Company's financial statements will become impaired; and changes in assumptions used in making such forward-looking statements, as well as the other risks and uncertainties detailed in Item 1A, "Risk Factors." Forward-looking statements speak only as of the date on which they are made. The Company does not undertake any obligation to update any forward-looking statement to reflect circumstances or events that occur after the date the forward-looking statements are made.

**PART I**

**Item 1. Business**

**General**

Brookline Bancorp, Inc. (the "Company"), a Delaware corporation, operates as a multi-bank holding company for Brookline Bank and its subsidiaries; Bank Rhode Island ("BankRI") and its subsidiaries; First Ipswich Bank ("First Ipswich" and formerly known as the First National Bank of Ipswich) and its subsidiaries; and Brookline Securities Corp.

Brookline Bank, which includes its wholly-owned subsidiaries, BBS Investment Corp. and Longwood Securities Corp., and its 84.8%-owned subsidiary, Eastern Funding LLC ("Eastern Funding"), operates 22 full-service banking offices in Brookline, Massachusetts and the greater Boston metropolitan area. Brookline Savings Bank was established as a savings bank in 1871. The Company was organized in November 1997 for the purpose of acquiring all of the capital stock of Brookline Savings Bank upon completion of the reorganization of Brookline Savings Bank from a mutual savings bank into a mutual holding company structure. In January 2003, Brookline Savings Bank changed its name to Brookline Bank.

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On February 28, 2011, the Company acquired First Ipswich Bancorp, the holding company for First Ipswich, headquartered in Ipswich, Massachusetts. First Ipswich, which includes its wholly-owned subsidiaries, First Ipswich Securities II Corp., First Ipswich Insurance Agency, First Ipswich Realty and FNBI Realty, operates six full-service banking offices on the north shore of eastern Massachusetts and in the Boston metropolitan area. In June 2012, the First National Bank of Ipswich changed its name to First Ipswich Bank.

On January 1, 2012, the Company acquired Bancorp Rhode Island, Inc., a Rhode Island corporation and holding company for BankRI, headquartered in Providence, Rhode Island. BankRI, which includes its wholly-owned subsidiaries, BRI Investment Corp., Macrolease Corporation ("Macrolease"), Acorn Insurance Agency and BRI Realty Corp., operates 18 full-service banking offices in Providence County, Kent County and Washington County, Rhode Island.

As a commercially focused financial institution with 46 full-service banking offices throughout Greater Boston, the North Shore of Massachusetts, and Rhode Island, the Company, through Brookline Bank, BankRI and First Ipswich (individually and collectively, the "Banks"), offers a wide range of commercial, business and retail banking services, including a full complement of cash management products, on-line banking services, consumer and residential loans and investment services designed to meet the financial needs of small- to mid-sized businesses and individuals throughout central New England. Specialty lending activities include indirect automobile loans as well as equipment financing in the New York/New Jersey metropolitan area and elsewhere.

The Company focuses its business efforts on profitably growing its commercial lending businesses, both organically and through acquisitions. The Company's customer focus, multi-bank structure, and risk management are integral to its organic growth strategy and serve to differentiate the Company from its competitors. As full-service financial institutions, the Banks and their subsidiaries focus on the continued acquisition of well-qualified customers, the deepening of long-term banking relationships through a full complement of products and excellent customer service, and strong risk management. The Company's multi-bank structure retains the local-bank orientation while relieving local bank management of the responsibility for most back-office functions which are consolidated at the holding company level. Branding and pricing remain largely local in order to better meet the needs of bank customers and further motivate the Banks' commercial, business and retail bankers.

The Company, has, from time to time, acquired other business lines or financial institutions that it believes share the Company's relationship and customer service orientations and provide access to complementary markets, customers, products, and/or services. To this end, the two recent acquisitions of First Ipswich and BankRI complement Brookline Bank's existing commercial and retail portfolios, provide the Company's customers greater access to products and services, and expand the Company's market opportunities and potential for future growth in earnings and market share.

The Company's headquarters and executive management are located at 131 Clarendon Street, Boston, Massachusetts 02117-9179 and its telephone number is 617-425-4600.

The Company continued to expand its geographic footprint with the acquisitions of First Ipswich in February 2011 and BankRI in January 2012. Total loans and leases increased \$1.5 billion, or 53.6%, at December 31, 2012, compared to 2011. Loan and lease growth from 2011 was driven by organic growth of 11.8% and the addition of \$1.1 billion in loans and leases from the BankRI acquisition. The loans and leases acquired from BankRI at the time of acquisition included \$520.6 million in commercial real estate loans, \$282.4 million in commercial loans and leases and \$332.8 million in consumer loans. Excluding these acquired loans and leases, organic growth in commercial real estate loans was \$214.4 million or 16.9%, organic growth in commercial loans and leases was \$121.1 million, or 27.3%, and organic growth in consumer loans was \$17.8 million or 4.1%. Indirect automobile loans declined \$31.0 million or 5.4% as a result of the Company's unwillingness to originate such loans at very low interest rates.

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During the year ended December 31, 2012, the Company's total deposits increased \$1.4 billion, or 60.6%, as compared to December 31, 2011. Growth from December 31, 2011 was driven by organic growth of 10.2% and the addition of \$1.1 billion in deposits from the BankRI acquisition. The year-over-year increase in total deposits was driven by an increase in commercial and municipal deposits as the Company continues its efforts to expand customer relationships by offering a full suite of products. Core (non-certificate of deposit) deposits increased \$1.2 billion, or 80.1%, to \$2.6 billion as the Company strategically shifts from certificates of deposit to money market accounts in an effort to reduce its cost of funds.

Throughout 2012, the Company added \$16.0 million to its allowance for loan and lease losses and experienced net charge-offs of \$6.6 million to bring the balance to \$41.2 million at December 31, 2012. The ratio of the allowance for loan and lease losses to total loans and leases was 0.98% at December 31, 2012, down from 1.17% at December 31, 2011. This decrease reflects the elimination of BankRI's \$18.1 million allowance for loan and lease losses at December 31, 2011 in accordance with generally accepted accounting principles ("GAAP"). The ratio of the allowance for loan and lease losses related to originated loans to originated loans and leases was 1.33% at December 31, 2012. Nonperforming assets at December 31, 2012 were \$23.7 million, up from \$8.8 million at the end of 2011. This increase includes the addition of \$4.1 million in nonperforming assets due to the BankRI acquisition and \$2.0 million in nonperforming assets related to two short-term commercial loans made by BankRI shortly after the Company's acquisition of BankRI (the "two BankRI commercial loans"), as discussed in the "Allowance for Credit Losses Allowance for Loan and Lease Losses Commercial Loans and Leases" section beginning on page 44. Nonperforming assets were 0.46% of total assets at the end of 2012, compared to 0.27% at the end of 2011. Credit quality is solid and compares favorably to its peers, and remains a top priority within the Company.

Net interest income increased in 2012 by \$67.2 million or 61.0% to \$177.4 million compared to \$110.2 million in 2011. This improvement drove the net interest margin to 3.85%, up 9 basis points from 2011. Net income for 2012 increased \$9.5 million, or 34.6%, to \$37.1 million from \$27.6 million for 2011. Basic and fully diluted earnings per common share ("EPS") increased from \$0.47 for 2011 to \$0.53 for 2012. Net income for 2012 includes \$4.0 million (after-tax) of expenses related to the acquisition of BankRI.

**Competition**

The Company provides banking alternatives in the greater Boston, Massachusetts and Providence, Rhode Island metropolitan marketplaces, each of which are dominated by several large national banking institutions. Based on total deposits at June 30, 2012, the Company ranks eleventh in deposit market share among bank holding companies in the combined Massachusetts-Rhode Island market area, with six of the top ten bank holding companies headquartered outside the state. The Company faces considerable competition in its market area for all aspects of banking and related service activities. Competition from both bank and non-bank organizations is expected to continue with the Company facing strong competition in generating loans and attracting deposits.

In addition to other commercial banks, the Company's main competition for generating loans includes savings banks, credit unions, mortgage banking companies, insurance companies, and other financial services companies. Competitive factors considered for loan generation include product offerings, interest rates, terms offered, services provided and geographic locations. Lending services for the Company are concentrated in the greater Boston, Massachusetts and Providence, Rhode Island metropolitan areas, eastern Massachusetts, southern New Hampshire, and Rhode Island, while the Company's equipment financing activities are concentrated in New York and New Jersey.

In attracting deposits, the Company's primary competitors are savings banks, commercial banks, credit unions, and other non-depository institutions such as securities and brokerage firms and

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insurance companies. Competitive factors considered in attracting and retaining deposits include product offerings and rate of return, convenient branch locations and automated teller machines and, more recently, online access to accounts. Deposit customers are generally in communities where banking offices are located.

**Market Area and Credit Risk Concentration**

As of December 31, 2012, the Company, through its Banks, operated 46 full-service banking offices in greater Boston, Massachusetts and greater Providence, Rhode Island. The Banks' deposits are gathered from the general public primarily in the communities in which its banking offices are located. The Banks' lending activities are concentrated primarily in the greater Boston, Massachusetts and Providence, Rhode Island metropolitan areas, eastern Massachusetts, southern New Hampshire and Rhode Island. In addition, the Company conducts equipment financing activities in the New York/New Jersey metropolitan area and elsewhere.

While historically, the Company has not experienced significant losses from commercial real estate and residential mortgage lending, current economic conditions could cause an increase in loan delinquencies and further declines in property values, culminating in higher loan losses. To mitigate the potential for such losses, the Company has consistently applied conservative underwriting criteria in originating commercial real estate and residential mortgage loans. Construction lending has not been a significant part of the Company's lending activities.

Although commercial lending carries a higher risk profile than commercial real estate and residential mortgage lending, in general the Company has avoided significant losses in this market segment. However, during the second quarter of 2012, a \$4.2 million provision for credit losses was recorded in connection with two short-term commercial loans made by BankRI shortly after the Company's acquisition of BankRI. See the "*Allowances for Credit Losses Allowance for Loan and Lease Losses Commercial Loans and Leases*" section of Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" below for more information on these two problem credits.

***Brookline Bank and First Ipswich***

The Banks' urban and suburban market area is characterized by a large number of apartment buildings, condominiums and office buildings. As a result, multi-family and commercial real estate mortgage lending has been a significant part of the Banks' activities for many years. These types of loans typically generate higher yields, but also involve greater credit risk. Many of the Banks' borrowers have more than one multi-family or commercial real estate loan outstanding. The Company manages this credit risk, in part, by limiting loan-to-value ratios at loan origination, lending to seasoned real estate owners/managers, using reasonable capitalization and vacancy ratios, cross-collateralizing loans to one borrower when deemed prudent, and limiting the amount and types of construction lending. At December 31, 2012, the largest commercial real estate loan in Brookline Bank's portfolio was for \$16.6 million, while the largest commercial real estate loans in First Ipswich's portfolio was for \$3.8 million.

The Banks also originate commercial loans and leases for working capital and other business-related purposes, and are concentrating such lending to companies located primarily in Massachusetts, and, in the case of Eastern Funding, in New York and New Jersey. Since commercial loans are typically made on the basis of the borrower's ability to make repayment from the cash flow of the business, the availability of funds for the repayment of commercial and industrial loans may be significantly dependent on the success of the business itself. Further, the collateral securing the loans may be difficult to value, may fluctuate in value based on the success of the business and may deteriorate over time. For this reason, these loans and leases involve greater credit risk. Loans and



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leases originated by Eastern Funding generally earn higher yields because the borrowers are typically small businesses with limited capital such as coin-operated laundries, dry cleaners, fitness centers, convenience stores and tow truck operators. The Banks manage the credit risk inherent in commercial lending through limits on industry concentrations, strong debt service coverage ratios at origination and, in many cases, the procurement of personal guarantees of the borrowers. At December 31, 2012, the largest credit in Brookline Bank's commercial lending portfolio was for \$20.0 million, while the largest credit in First Ipswich's commercial lending portfolio was for \$2.1 million.

In general, the success of Brookline Bank's indirect automobile lending portfolio depends on many factors, the more significant of which include the policies established for loan underwriting, the monitoring of portfolio performance, and the effect of economic conditions on consumers and the automobile industry. For regulatory purposes, Brookline Bank's indirect automobile loan portfolio is not classified as "subprime lending." Most of Brookline Bank's indirect automobile loans are originated through automobile dealerships in Massachusetts, Connecticut, Rhode Island and New Hampshire. At December 31, 2012, the largest single loan in Brookline Bank's indirect automobile portfolio was for \$27,000. First Ipswich does not engage in indirect automobile lending.

The Banks' retail customers live and work in the Boston metropolitan area, are financially active and value personalized service and easy branch access. The Banks' consumer loan portfolio, which includes residential mortgage loans, home equity loans and lines of credit, and other consumer loans, caters to the borrowing needs of this customer base. Credit risk in these portfolios is managed by limiting loan-to-value ratios at loan origination and by requiring strong credit histories. At December 31, 2012, the largest loan in Brookline Bank's consumer portfolio was for \$4.0 million, while the largest loan in First Ipswich's consumer portfolio was for \$2.1 million.

The deposit market in Massachusetts is highly concentrated. The five largest banks in the state have an aggregate market share of approximately 62% (based on June 30, 2012 FDIC statistics). As a result, competition for deposits is intense and price-sensitive.

***BankRI***

BankRI concentrates its business efforts in three main areas: lending to commercial customers, growing its core deposits, and the development of related lines of business including equipment financing and consumer lending. BankRI offers a variety of loan facilities to serve both commercial and consumer borrowers primarily within the State of Rhode Island and nearby areas of Massachusetts.

The majority of Rhode Island residents, jobs and businesses are located in Providence and Kent Counties, and more than 95% of Rhode Island businesses have fewer than 100 employees. The high concentration of small to mid-size businesses in the Bank's predominately urban franchise makes deployment of funds in the commercial lending area practicable. Moreover, BankRI believes it can attract commercial customers from larger competitors through a higher level of service and its ability to set policies and procedures, as well as make decisions, locally. BankRI's business banking practice focuses on commercial loans to businesses with annual revenue between \$0.5 million to \$3.5 million and with five to 25 employees. BankRI's branch network also plays a role in developing business lending relationships. These relationships also provide BankRI with a source of deposit accounts and cash management business. Commercial loans are often made for real estate purchases. At December 31, 2012, the largest loan in BankRI's commercial real estate portfolio was for \$11.9 million. Many of BankRI's commercial real estate customers have other commercial borrowing relationships with BankRI.

BankRI also originates commercial loans and lines of credit for various business-related purposes, and engages in equipment financing through its wholly-owned subsidiary, Macrolease. Consistent with lending practices at the Company's other Banks, BankRI manages this credit risk by limiting the duration of loan maturities, employing adjustable rates without interest rate caps, and by securing

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personal guarantees from borrowers. The Macrolease equipment financing portfolio is comprised of small- to medium-sized businesses such as fitness centers, restaurants and woodworking shops. Macrolease manages credit risk by lending to known franchisees, limiting loan-to-value ratios and franchisee concentrations, and requiring strong debt service coverage ratios. At December 31, 2012, the largest loan in BankRI's commercial portfolio was for \$7.5 million.

BankRI's retail customers live and work in the Providence, Rhode Island metropolitan area and value easy branch access, personalized service, and knowledge of local communities. The Bank satisfies a variety of consumer credit needs by providing home equity term loans and lines of credit, residential mortgage loans and other consumer loans. Credit risk in the consumer portfolio is managed by limiting loan-to-value ratios at loan origination and by requiring strong credit histories. At December 31, 2012, the largest loan in BankRI's consumer portfolio was for \$1.4 million.

BankRI seeks to grow its deposits by stressing the development of full relationships with customers, including its commercial customers, who tend to be more relationship-oriented than those who are seeking stand-alone or single transaction products. Like Massachusetts, the banking market in Rhode Island is highly concentrated. The three largest banks in the state have an aggregate deposit market share of approximately 72% (based on June 30, 2012 FDIC statistics).

**Economic Conditions and Governmental Policies**

Repayment of multi-family and commercial real estate loans made by the Company generally is dependent on sufficient income from the properties to cover operating expenses and debt service. Repayment of commercial loans and equipment financing loans and leases generally is dependent on the demand for the borrowers' products or services and the ability of borrowers to compete and operate on a profitable basis. Repayment of residential mortgage loans, home equity loans and indirect automobile loans generally is dependent on the financial well-being of the borrowers and their capacity to service their debt levels. The asset quality of the Company's loan and lease portfolio, therefore, is greatly affected by the economy.

Economic activity in the United States has shown continuous improvement since the latter half of 2009 after slowing significantly as a result of the 2008 financial crisis. According to the Department of Labor, the national unemployment rate peaked at 10.0% in October 2009. In December 2012, the unemployment rate was 7.8% nationally, down from 8.5% at the end of 2011.

The Company's primary geographic footprints are the Boston, Massachusetts and Providence, Rhode Island metropolitan areas. According to the Bureau of Labor Statistics, the largest employment sectors in both Massachusetts and Rhode Island are, in order, education and health services, business and professional services, and trade, transportation and utilities, a sector that includes wholesale and retail trade. The unemployment rate in Massachusetts decreased from 6.9% in December 2011 to 6.7% in December 2012, and has consistently remained lower than the national average. The unemployment rate in Rhode Island decreased from 11.0% in December 2011 to 10.2% in December 2012, but remains among the highest for any state in the nation.

Despite the positive trends in recent years, the economy has not fully recovered from the effects of the 2008-2009 recession, and unemployment rates remain elevated in relation to historic trends. Should there be any setback in the economy or increase in the unemployment rates in the Boston, Massachusetts or Providence, Rhode Island metropolitan areas, the resulting negative consequences could affect occupancy rates in the properties financed by the Company and cause certain individual and business borrowers to be unable to service their debt obligations.

The earnings and business of the Company are affected by external influences such as general economic conditions and the policies of governmental authorities, including the Board of Governors of the Federal Reserve System (the "FRB"). The FRB regulates the supply of money and bank credit to

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influence general economic conditions throughout the United States of America. The instruments of monetary policy employed by the FRB affect interest rates earned on investment securities and loans and interest rates paid on deposits and borrowed funds. The rate-setting actions of the Federal Open Market Committee (the "FOMC") of the Federal Reserve System have a significant effect on the Company's operating results and the level of growth in its loans and leases and deposits.

**Personnel**

As of December 31, 2012, the Company had 622 full-time employees and 40 part-time employees. The employees are not represented by a collective bargaining unit and the Company considers its relationship with its employees to be good.

**Access to Information**

As a public company, Brookline Bancorp, Inc. is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith, files reports, proxy and information statements and other information with the Securities and Exchange Commission (the "SEC"). The Company makes available on or through its internet website, without charge, its annual reports on Form 10-K, proxy, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the SEC. The Company's reports filed with, or furnished to, the SEC are also available at the SEC's website at [www.sec.gov](http://www.sec.gov) and on the Company's website at [www.brooklinebank.com](http://www.brooklinebank.com). Press releases are also maintained on the Company's website. Additional information for BankRI and First Ipswich can be found at [www.bankri.com](http://www.bankri.com) and [www.firstipswich.com](http://www.firstipswich.com), respectively. Information on the Company's website is not incorporated by reference into this document and should not be considered part of this Report.

The Company's common stock is traded on the Nasdaq Global Select Market<sup>SM</sup> under the symbol "BRKL."

**Supervision and Regulation**

The following discussion addresses elements of the regulatory framework applicable to bank holding companies and their subsidiaries. This regulatory framework is intended primarily to protect the safety and soundness of depository institutions, the federal deposit insurance system, and depositors, rather than the protection of shareholders of a bank holding company such as the Company.

As a bank holding company, the Company is subject to regulation, supervision and examination by the FRB under the Bank Holding Company Act of 1956, as amended (the "BHCA") and by the Massachusetts Division of Banks (the "MDOB") and the Massachusetts Board of Bank Incorporation (the "BBI") under Massachusetts General Laws Chapter 167A. The FRB is also the primary federal regulator of the Banks. In addition, Brookline Bank and First Ipswich are subject to regulation, supervision and examination by the MDOB, and BankRI is subject to regulation, supervision and examination by the Banking Division of the Rhode Island Department of Business Regulation (the "RIBD").

The following is a summary of certain aspects of various statutes and regulations applicable to the Company and its subsidiaries. This summary is not a comprehensive analysis of all applicable law. Refer to the applicable statutes and regulations for more information. In addition, these statutes and regulations may change, or additional statutes or regulations could be adopted in the future, and the Company cannot predict what effect these changes or new statutes or regulations, if any, could have on the Company's business.

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***The Dodd-Frank Act***

The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") comprehensively reformed the regulation of financial institutions, products and services. Among other things, the Dodd-Frank Act:

granted the FRB increased supervisory authority and codified the source of strength doctrine, as discussed in more detail in "Regulation of the Company Source of Strength" below;

established new corporate governance and proxy disclosure requirements, as discussed in "Regulation of the Company Corporate Governance and Executive Compensation" below;

provided for new capital standards applicable to the Company, as discussed in more detail in "Capital Requirements" below;

modified the scope and costs associated with deposit insurance coverage, as discussed in "Regulation of the Banks Deposit Insurance" below;

permitted well capitalized and well managed banks to acquire other banks in any state, subject to certain deposit concentration limits and other conditions, as discussed in "Regulation of the Banks Acquisitions and Branching" below;

permitted the payment of interest on business demand deposit accounts;

established new minimum mortgage underwriting standards for residential mortgages, as discussed in "Consumer Protection Regulation Mortgage Reform" below;

established the Bureau of Consumer Financial Protection (the "CFPB"), as discussed in "Consumer Protection Regulation" below;

barred banking organizations, such as the Company, from engaging in proprietary trading and from sponsoring and investing in hedge funds and private equity funds, except as permitted under certain circumstances, as discussed in "Regulation of Other Activities Volcker Rule Restrictions on Proprietary Trading and Sponsorship of Hedge Funds and Private Equity Funds" below; and

established the Financial Stability Oversight Council to designate certain activities as posing a risk to the U.S. financial system and recommend new or heightened standards and safeguards for financial institutions engaging in such activities.

***Regulation of the Company***

The Company is subject to regulation, supervision and examination by the FRB, which has the authority, among other things, to order bank holding companies to cease and desist from unsafe or unsound banking practices; to assess civil money penalties; and to order termination of non-banking activities or termination of ownership and control of a non-banking subsidiary by a bank holding company.

*Source of Strength*

Under the Dodd-Frank Act, the Company is required to serve as a source of financial strength for the Banks in the event of the financial distress of the Banks. This provision codifies the longstanding policy of the FRB. This support may be required at times when the bank holding company may not have the resources to provide it.



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*Acquisitions and Activities*

The BHCA prohibits a bank holding company from acquiring substantially all the assets of a bank or acquiring direct or indirect ownership or control of more than 5% of the voting shares of any bank, or increasing such ownership or control of any bank, or merging or consolidating with any bank holding company without prior approval of the FRB. Further, as a Massachusetts bank holding company, the Company must obtain the prior approval of the BBI to acquire more than 5% ownership or control of any voting stock in any other banking institution, acquire substantially all the assets of a bank, or merge with another bank holding company.

The BHCA prohibits a bank holding company from engaging directly or indirectly in activities other than those of banking, managing or controlling banks or furnishing services to its subsidiary banks. However, a bank holding company may engage in and may own shares of companies engaged in certain activities that the FRB determines to be so closely related to banking or managing and controlling banks so as to be a proper incident thereto.

*Limitations on Acquisitions of Company Common Stock*

The Change in Bank Control Act prohibits a person or group of persons from acquiring "control" of a bank holding company unless the FRB has been notified and has not objected to the transaction. Under a rebuttable presumption established by the FRB, the acquisition of 10% or more of a class of voting securities of a bank holding company, such as the Company, with a class of securities registered under Section 12 of the Exchange Act, would, under the circumstances set forth in the presumption, constitute the acquisition of control of a bank holding company. In addition, any company would be required to obtain the approval of the FRB under the BHCA before acquiring 25% (5% in the case of an acquirer that is a bank holding company) or more, or otherwise obtaining control or a controlling influence over a bank holding company. In 2008, the FRB released guidance on minority investments in banks that relaxed the presumption of control for investments of greater than 10% of a class of outstanding voting securities of a bank holding company in certain instances discussed in the guidance.

*Corporate Governance and Executive Compensation*

Under the Dodd-Frank Act, the SEC adopted rules granting proxy access for shareholder nominees and grants shareholders a non-binding vote on executive compensation and "golden parachute" payments. Pursuant to modifications of the proxy rules under the Dodd-Frank Act, the Company is required to disclose the relationship between executive pay and financial performance, the ratio of the median pay of all employees to the pay of the CEO, and employee and director hedging activities. As required by the Dodd-Frank Act, the stock exchanges have amended their listing rules to require that each member of a listed company's compensation committee be independent and be granted the authority and funding to retain independent advisors and to prohibit the listing of any security of an issuer that does not adopt policies governing the claw back of excess executive compensation based on inaccurate financial statements. Finally, the federal regulatory agencies have proposed new regulations which prohibit incentive-based compensation arrangements that encourage executives and certain other employees to take inappropriate risks.

***Regulation of the Banks***

Brookline Bank and First Ipswich are subject to regulation, supervision and examination by the FRB and the MDOB. BankRI is subject to regulation, supervision and examination by the FRB and the RIBD. The enforcement powers available to federal and state banking regulators include, among other things, the ability to issue cease and desist or removal orders to terminate insurance of deposits; to assess civil money penalties; to issue directives to increase capital; to place the bank into receivership; and to initiate injunctive actions against banking organizations and institution-affiliated parties.

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*Deposit Insurance*

The Banks pay deposit insurance premiums to the FDIC based on an assessment rate established by the FDIC. For most banks and savings associations, including the Banks, FDIC rates depend upon a combination of CAMELS component ratings and financial ratios. CAMELS ratings reflect the applicable bank regulatory agencies' evaluation of the financial institution's capital, asset quality, management, earnings, liquidity and sensitivity to risk. Pursuant to the Dodd-Frank Act, deposit premiums are based on assets rather than insurable deposits. To determine their actual deposit insurance premiums, the Banks compute their base amount on its average consolidated assets less its average tangible equity (defined as the amount of Tier 1 capital) and its applicable assessment rate. The Company's FDIC deposit insurance costs totaled \$4.2 million in 2012. The FDIC has the power to adjust the assessment rates at any time.

Pursuant to an FDIC rule issued in November 2009, each of the Banks prepaid its quarterly risk-based assessments to the FDIC for the fourth quarter of 2009 and for all of 2010, 2011, and 2012 on December 30, 2009. The Banks recorded the entire amount of its prepayment as an asset (a prepaid expense), which bears a zero-percent risk weight for risk-based capital purposes. Each quarter the Banks record an expense for its regular quarterly assessment for the quarter and a corresponding credit to the prepaid assessment until the asset is exhausted. The FDIC will not refund or collect additional prepaid assessments because of a decrease or growth in deposits; however, if the prepaid assessment is not exhausted after collection of the amount due on June 30, 2013, the remaining amount of the prepayment will be returned to the Banks.

The Dodd-Frank Act permanently increased the FDIC deposit insurance limit to \$250,000 per depositor. Additionally, the Dodd-Frank Act provided temporary unlimited deposit insurance coverage for non-interest-bearing transaction accounts from December 31, 2010 to December 31, 2012. This replaced the FDIC's Transaction Account Guarantee Program, which expired on December 31, 2010. See also the Overview section of Note 1, "Basis of Presentation," to the consolidated financial statements for discussion of insurance coverage by the Depositors Insurance Fund.

*Cross-Guarantee*

Similar to the source of strength doctrine discussed above in "*Regulation of the Company Source of Strength*," under the cross-guarantee provisions of the Federal Deposit Insurance Act, as amended (the "FDIA"), the FDIC can hold any FDIC-insured depository institution liable for any loss suffered or anticipated by the FDIC in connection with (i) the "default" of a commonly controlled FDIC-insured depository institution; or (ii) any assistance provided by the FDIC to a commonly controlled FDIC-insured depository institution "in danger of default."

*Acquisitions and Branching*

The Banks must seek prior regulatory approval from the FRB to acquire another bank or establish a new branch office. Brookline Bank and First Ipswich must also seek prior regulatory approval from the MDOB to acquire another bank or establish a new branch office and BankRI must also seek prior regulatory approval from the RIBD to acquire another bank or establish a new branch office. Well capitalized and well managed banks may acquire other banks in any state, subject to certain deposit concentration limits and other conditions, pursuant to the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 and the Dodd-Frank Act. In addition, the Dodd-Frank Act authorizes a state-chartered bank to establish new branches on an interstate basis to the same extent a bank chartered by the host state may establish branches.

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*Activities and Investments of Insured State-Chartered Banks*

Section 24 of the FDIA generally limits the investment activities of FDIC-insured, state-chartered banks when acting as principal to those that are permissible for national banks. Further, the Gramm-Leach-Bliley Act of 1999 (the "GLBA") permits state banks, to the extent permitted under state law, to engage through "financial subsidiaries" in certain activities which are permissible for subsidiaries of a financial holding company. In order to form a financial subsidiary, a state-chartered bank must be well capitalized, and such banks would be subject to certain capital deduction, risk management and affiliate transaction rules, among other things.

*Brokered Deposits*

Section 29 of the FDIA and federal regulations generally limit the ability of an insured depository institution to accept, renew or roll over any brokered deposit unless the institution's capital category is "well capitalized" or, with regulatory approval, "adequately capitalized." Depository institutions, other than those in the lowest risk category, that have brokered deposits in excess of 10% of total deposits will be subject to increased FDIC deposit insurance premium assessments. Additionally, depository institutions considered "adequately capitalized" that need regulatory approval to accept, renew or roll over any brokered deposits are subject to additional restrictions on the interest rate they may pay on deposits. At December 31, 2012, the Company did not have any brokered deposits.

*The Community Reinvestment Act*

The Community Reinvestment Act ("CRA") requires the FRB to evaluate each of the Banks' performance in helping to meet the credit needs of the entire communities it serves, including low and moderate-income neighborhoods, consistent with its safe and sound banking operations, and to take this record into consideration when evaluating certain applications. The FRB's CRA regulations are generally based upon objective criteria of the performance of institutions under three key assessment tests: (i) a lending test, to evaluate the institution's record of making loans in its service areas; (ii) an investment test, to evaluate the institution's record of investing in community development projects, affordable housing, and programs benefiting low or moderate income individuals and businesses; and (iii) a service test, to evaluate the institution's delivery of services through its branches, ATMs, and other offices. Failure of an institution to receive at least a "Satisfactory" rating could inhibit the Banks or the Company from undertaking certain activities, including engaging in activities newly permitted as a financial holding company under GLBA and acquisitions of other financial institutions. Each Bank has achieved a rating of "Satisfactory" on its most recent CRA examination. Rhode Island and Massachusetts have enacted substantially similar community reinvestment requirements.

*Lending Restrictions*

Federal law limits a bank's authority to extend credit to its directors, executive officers and 10% shareholders, as well as to entities controlled by such persons. Among other things, extensions of credit to insiders are required to be made on terms that are substantially the same as, and follow credit underwriting procedures that are not less stringent than, those prevailing for comparable transactions with unaffiliated persons. Also, the terms of such extensions of credit may not involve more than the normal risk of repayment or present other unfavorable features and may not exceed certain limitations on the amount of credit extended to such persons, individually and in the aggregate, which limits are based, in part, on the amount of the bank's capital. The Dodd-Frank Act explicitly provides that an extension of credit to an insider includes credit exposure arising from a derivatives transaction, repurchase agreement, reverse repurchase agreement, securities lending transaction or securities borrowing transaction. Additionally, the Dodd-Frank Act requires that asset sale transactions with insiders must be on market terms, and if the transaction represents more than 10% of the capital and surplus of the bank, be approved by a majority of the disinterested directors of the bank.



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A bank holding company and its subsidiaries are subject to prohibitions on certain tying arrangements. These institutions are generally prohibited from extending credit to or offering any other service on the condition that the client obtain some additional service from the institution or its affiliates or not obtain services of a competitor of the institution.

**Capital Requirements**

The FRB has issued risk-based and leverage capital guidelines applicable to the Company and the Banks. In addition, the FRB may from time to time require that a banking organization maintain capital above the minimum levels, whether because of its financial condition or actual or anticipated growth.

The FRB's capital adequacy guidelines generally require bank holding companies to maintain total capital of at least 8% of total risk-weighted assets, including off-balance sheet items, with at least 50% of that amount consisting of Tier 1 (or "core") capital and the remaining amount consisting of Tier 2 (or "supplementary") capital. Tier 1 capital for bank holding companies generally consists of the sum of common shareholders' equity, perpetual preferred stock and trust preferred securities (both subject to certain limitations), and minority interests in the equity accounts of consolidated subsidiaries, less goodwill and other non-qualifying intangible assets. Future issuances of trust preferred securities have been disallowed as Tier 1 qualifying capital by the Dodd-Frank Act, although the Company's currently outstanding trust preferred securities have been grandfathered for Tier 1 eligibility. Under the proposed Basel III capital rules discussed below, the Company's currently outstanding trust preferred securities would be phased out from the calculation of Tier 1 capital over a ten-year period. Tier 2 capital generally consists of hybrid capital instruments, perpetual debt and mandatory convertible debt securities, perpetual preferred stock and trust preferred securities, to the extent not eligible to be included as Tier 1 capital, term subordinated debt and intermediate-term preferred stock; and, subject to limitations, general allowances for loan losses. Assets are adjusted under the risk-based guidelines to take into account different risk characteristics. In addition to the risk-based capital requirements, the FRB requires most bank holding companies, including the Company, to maintain a minimum leverage capital ratio of Tier 1 capital to its average total consolidated assets of 4.0%. The Dodd-Frank Act requires the FRB to establish minimum risk-based and leverage capital requirements that may not be lower than those in effect on July 21, 2010. As of December 31, 2012, the Company's total risk-based capital ratio was 11.8%, its Tier 1 capital ratio was 10.9% and its leverage ratio was 9.4%. The Company is currently considered "well capitalized" under all regulatory definitions. The FRB's capital adequacy guidelines also apply to each of the Banks as a member of the Federal Reserve System.

The Company has not elected, and does not currently expect, to calculate its risk-based capital requirements under either the "advanced or standard" approach of the Basel II capital accords. In 2010 and 2011, the members of the Basel Committee on Banking Supervision agreed to new global capital adequacy standards, known as Basel III. These standards provide for higher capital requirements, enhanced risk coverage, a global leverage ratio, liquidity standards and a provision for counter-cyclical capital. The federal banking agencies issued three joint proposed rules (the "Proposed Capital Rules") that implement the Basel III capital standards and establish the minimum capital levels for banks and bank holding companies required under the Dodd-Frank Act. The Proposed Capital Rules establish a minimum common equity Tier 1 capital ratio of 6.5% of risk-weighted assets for a "well capitalized" institution and increase the minimum total Tier 1 capital ratio for a "well capitalized" institution from 6% to 8%. Additionally, the Proposed Capital Rules require an institution to establish a capital conservation buffer of common equity Tier 1 capital in an amount equal to 2.5% of total risk weight assets above the 6.5% minimum risk-based capital requirement. The Proposed Capital Rules revise certain other capital definitions and, generally, impose more stringent capital requirements. Further, the Proposed Capital Rules increase the required capital for certain categories of assets, including higher-risk residential mortgages, higher-risk construction real estate loans and certain exposures

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related to securitizations. Under the Proposed Capital Rules, the amount of capital held against residential mortgages is based upon the loan-to-value ratio of the mortgage. Additionally, the Proposed Capital Rules remove the filter for accumulated other comprehensive income in the current capital rules which currently prevents unrealized gains and losses from being included in the calculation of the institution's capital. This change would result in the need for additional capital to be held against unrealized gains and losses on "available for sale" securities, hedges and any adjustments to the funded status of defined benefit plans, which could result in increased volatility in the amount of required capital. As noted above, the Proposed Capital Rules also eliminate the treatment of trust preferred securities as Tier 1 capital over a ten-year period.

The financial services industry, members of Congress and state regulatory agencies provided extensive comments on the Proposed Capital Rules to the federal banking agencies. In response to such commentary, the federal banking agencies extended the deadline for the Proposed Capital Rules to go into effect and indicated that a final rule would be issued in 2013. The final capital rule may differ significantly in substance or in scope from the Proposed Capital Rules. Accordingly, the Company is not yet in a position to determine the effect of Basel III and the Proposed Capital Rules on its capital requirements.

*Prompt Corrective Action*

The FRB has promulgated regulations to implement the system of prompt corrective action established by Section 38 of the FDIA. Under the regulations, a bank is "well capitalized" if it has: (i) a total risk-based capital ratio of 10.0% or greater; (ii) a Tier 1 risk-based capital ratio of 6.0% or greater; (iii) a leverage ratio of 5.0% or greater; and (iv) is not subject to any written agreement, order, capital directive or prompt corrective action directive to meet and maintain a specific capital level for any capital measure. A bank is "adequately capitalized" if it has: (1) a total risk-based capital ratio of 8.0% or greater; (2) a Tier 1 risk-based capital ratio of 4.0% or greater; and (3) a leverage ratio of 4.0% or greater (3.0% under certain circumstances) and does not meet the definition of a "well capitalized bank." The FRB must take into consideration: (a) concentrations of credit risk; (b) interest-rate risk; and (c) risks from non-traditional activities, as well as an institution's ability to manage those risks, when determining the adequacy of an institution's capital. This evaluation will be made as a part of the institution's regular safety and soundness examination. As of December 31, 2012, each Bank's capital ratios placed it in the well capitalized category.

Generally, a bank, upon receiving notice that it is not adequately capitalized (i.e., that it is "undercapitalized"), becomes subject to the prompt corrective action provisions of Section 38 of FDIA that, for example, (i) restrict payment of capital distributions and management fees, (ii) require that the FRB monitor the condition of the institution and its efforts to restore its capital, (iii) require submission of a capital restoration plan, (iv) restrict the growth of the institution's assets and (v) require prior regulatory approval of certain expansion proposals. A bank that is required to submit a capital restoration plan must concurrently submit a performance guarantee by each company that controls the bank. A bank that is "critically undercapitalized" (i.e., has a ratio of tangible equity to total assets that is equal to or less than 2.0%) will be subject to further restrictions, and generally will be placed in conservatorship or receivership within 90 days.

*Dividend Restrictions*

*Restrictions on Bank Holding Company Dividends*

The FRB has authority to prohibit bank holding companies from paying dividends if such payment is deemed to be an unsafe or unsound practice. The FRB has indicated generally that it may be an unsafe or unsound practice for bank holding companies to pay dividends unless the bank holding company's net income over the preceding year is sufficient to fund the dividends and the expected rate

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of earnings retention is consistent with the organization's capital needs, asset quality and overall financial condition. The Company's revenues consist primarily of cash dividends paid to it by the Banks.

*Restrictions on Bank Dividends*

The FRB has the authority to use its enforcement powers to prohibit a bank from paying dividends if, in its opinion, the payment of dividends would constitute an unsafe or unsound practice. Federal law also prohibits the payment of dividends by a bank that will result in the bank failing to meet its applicable capital requirements on a pro forma basis. Payment of dividends by a bank is also restricted pursuant to various state regulatory limitations.

*Transactions with Affiliates*

Under Sections 23A and 23B of the Federal Reserve Act and Regulation W thereunder, there are various legal restrictions on the extent to which a bank holding company and its nonbank subsidiaries may borrow, obtain credit from or otherwise engage in "covered transactions" with any bank to the extent that such transactions do not exceed 10% of the capital stock and surplus of the bank (for covered transactions between the bank and one affiliate) and 20% of the capital stock and surplus of the bank (for covered transactions between the bank and all affiliates). The Dodd-Frank Act amended the definition of affiliate to include an investment fund for which a bank or one of its affiliates is an investment adviser. A "covered transaction" includes, among other things, a loan or extension of credit; an investment in securities issued by an affiliate; asset purchases; the acceptance of securities issued by an affiliate as collateral for a loan or extension of credit to any person or company; the issuance of a guarantee, acceptance, or letter of credit on behalf of an affiliate; a securities borrowing or lending transaction with an affiliate that creates a credit exposure to such affiliate; or a derivatives transaction with an affiliate that creates a credit exposure to such affiliate. Covered transactions are also subject to certain collateral security requirements. At December 31, 2012, there were no such transactions with affiliates.

*Consumer Protection Regulation*

The Company and the Banks are subject to a number of federal and state laws designed to protect consumers and prohibit unfair or deceptive business practices. These laws include the Equal Credit Opportunity Act, Fair Housing Act, Home Ownership Protection Act, Fair Credit Reporting Act, as amended by the Fair and Accurate Credit Transactions Act of 2003 (the "FACT Act"), GLBA, Truth in Lending Act, the CRA, the Home Mortgage Disclosure Act, Real Estate Settlement Procedures Act, National Flood Insurance Act and various state law counterparts. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must interact with customers when taking deposits, making loans, collecting loans and providing other services. Further, the Dodd-Frank Act established the CFPB, which has the responsibility for making rules and regulations under the federal consumer protection laws relating to financial products and services. The CFPB also has a broad mandate to prohibit unfair or deceptive acts and practices and is specifically empowered to require certain disclosures to consumers and draft model disclosure forms. Failure to comply with consumer protection laws and regulations can subject financial institutions to enforcement actions, fines and other penalties. The FRB will examine the Banks for compliance with CFPB rules and enforce CFPB rules with respect to the Banks.

*Mortgage Reform*

The Dodd-Frank Act prescribes certain standards that mortgage lenders must consider before making a residential mortgage loan, including verifying a borrower's ability to repay such mortgage loan. The CFPB issued a final rule that requires creditors, such as the Banks, to make a reasonable good faith determination of a consumer's ability to repay any consumer credit transaction secured by a

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dwelling. The rule provides creditors with minimum requirements for making such ability-to-repay determinations. Creditors are required to consider the following eight underwriting factors: (1) current or reasonably expected income or assets; (2) current employment status; (3) the monthly payment on the covered transaction; (4) the monthly payment on any simultaneous loan; (5) the monthly payment for mortgage-related obligations; (6) current debt obligations, alimony and child support; (7) the monthly debt-to-income ratio or residual income; and (8) credit history. While the Dodd-Frank Act provides that qualified mortgages are entitled to a presumption that the creditor satisfied the ability-to-repay requirements, the final rule provides a safe harbor for loans that satisfy the definition of a qualified mortgage and are not "higher priced." Higher-priced loans are subject to a rebuttable presumption. A "qualified mortgage" is a loan that does not contain certain risky features (such as negative amortization, interest-only payments, balloon payments, a term exceeding 30 years), has a debt-to-income ratio of not more than 43%, and for which the creditor considers and verifies the consumer's current debt obligations, alimony, and child support. The rule becomes effective on January 10, 2014.

The Dodd-Frank Act also allows borrowers to assert violations of certain provisions of the Truth-in-Lending Act as a defense to foreclosure proceedings. Under the Dodd-Frank Act, prepayment penalties are prohibited for certain mortgage transactions and creditors are prohibited from financing insurance policies in connection with a residential mortgage loan or home equity line of credit. The Dodd-Frank Act requires mortgage lenders to make additional disclosures prior to the extension of credit, in each billing statement and for negative amortization loans and hybrid adjustable rate mortgages. Additionally, the CFPB has issued rules governing mortgage servicing, appraisals, escrow requirements for higher-priced mortgages and loan originator qualification and compensation.

*Privacy and Customer Information Security*

The GLBA requires financial institutions to implement policies and procedures regarding the disclosure of nonpublic personal information about consumers to nonaffiliated third parties. In general, the Banks must provide their customers with an annual disclosure that explains its policies and procedures regarding the disclosure of such nonpublic personal information, and, except as otherwise required or permitted by law, the Banks are prohibited from disclosing such information except as provided in such policies and procedures. The GLBA also requires that the Banks develop, implement and maintain a comprehensive written information security program designed to ensure the security and confidentiality of customer information (as defined under GLBA), to protect against anticipated threats or hazards to the security or integrity of such information; and to protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer. The Banks are also required to send a notice to customers whose "sensitive information" has been compromised if unauthorized use of this information is "reasonably possible." Most of the states, including the states where the Banks operate, have enacted legislation concerning breaches of data security and the duties of the Banks in response to a data breach. Congress continues to consider federal legislation that would require consumer notice of data security breaches. Pursuant to the FACT Act, the Banks must also develop and implement a written identity theft prevention program to detect, prevent, and mitigate identity theft in connection with the opening of certain accounts or certain existing accounts. Additionally, the FACT Act amends the Fair Credit Reporting Act to generally prohibit a person from using information received from an affiliate to make a solicitation for marketing purposes to a consumer, unless the consumer is given notice and a reasonable opportunity and a reasonable and simple method to opt out of the making of such solicitations.

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***Anti-Money Laundering***

*The Bank Secrecy Act*

Under the Bank Secrecy Act ("BSA"), a financial institution is required to have systems in place to detect certain transactions, based on the size and nature of the transaction. Financial institutions are generally required to report to the United States Treasury any cash transactions involving more than \$10,000. In addition, financial institutions are required to file suspicious activity reports for transactions that involve more than \$5,000 and which the financial institution knows, suspects or has reason to suspect involves illegal funds, is designed to evade the requirements of the BSA or has no lawful purpose. The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the "USA PATRIOT Act"), which amended the BSA, is designed to deny terrorists and others the ability to obtain anonymous access to the U.S. financial system. The USA PATRIOT Act has significant implications for financial institutions and businesses of other types involved in the transfer of money. The USA PATRIOT Act, together with the implementing regulations of various federal regulatory agencies, has caused financial institutions, such as the Bank, to adopt and implement additional policies or amend existing policies and procedures with respect to, among other things, anti-money laundering compliance, suspicious activity, currency transaction reporting, customer identity verification and customer risk analysis. In evaluating an application under Section 3 of the BHCA to acquire a bank or an application under the Bank Merger Act to merge banks or effect a purchase of assets and assumption of deposits and other liabilities, the applicable federal banking regulator must consider the anti-money laundering compliance record of both the applicant and the target. In addition, under the USA PATRIOT Act financial institutions are required to take steps to monitor their correspondent banking and private banking relationships as well as, if applicable, their relationships with "shell banks."

*Office of Foreign Assets Control ("OFAC")*

The United States has imposed economic sanctions that affect transactions with designated foreign countries, nationals and others. These sanctions, which are administered by OFAC, take many different forms. Generally, however, they contain one or more of the following elements: (i) restrictions on trade with or investment in a sanctioned country, including prohibitions against direct or indirect imports from and exports to a sanctioned country and prohibitions on "U.S. persons" engaging in financial transactions relating to making investments in, or providing investment-related advice or assistance to, a sanctioned country; and (ii) a blocking of assets in which the government or specially designated nationals of the sanctioned country have an interest, by prohibiting transfers of property subject to U.S. jurisdiction (including property in the possession or control of U.S. persons). Blocked assets (for example, property and bank deposits) cannot be paid out, withdrawn, set off or transferred in any manner without a license from OFAC. Failure to comply with these sanctions could have serious legal and reputational consequences for the Banks. At December 31, 2012, the Company did not have any transactions with sanctioned countries, nationals, and others.

***Regulation of Other Activities***

*Volcker Rule Restrictions on Proprietary Trading and Sponsorship of Hedge Funds and Private Equity Funds*

The Dodd-Frank Act bars banking organizations, such as the Company, from engaging in proprietary trading and from sponsoring and investing in hedge funds and private equity funds, except as permitted under certain limited circumstances, in a provision commonly referred to as the "Volcker Rule." Under the Dodd-Frank Act, proprietary trading generally means trading by a banking entity or its affiliate for its own account. Hedge funds and private equity funds are described by the Dodd-Frank Act as funds that would be registered under the Investment Company Act but for certain enumerated exemptions. The Volcker Rule restrictions apply to the Company, the Banks and all of their subsidiaries and affiliates.

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**Item 1A. Risk Factors**

Before deciding to invest in us or deciding to maintain or increase your investment, you should carefully consider the risks described below, in addition to the other information contained in this report and in our other filings with the SEC. The risks and uncertainties described below and in our other filings are not the only ones facing us. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business. If any of these known or unknown risks or uncertainties actually occur, our business, financial condition and results of operations could be seriously harmed. In that event, the market price for our common stock could decline and you may lose your investment.

*We operate in a highly regulated industry, and laws and regulations, or changes in them, could limit or restrict our activities and could have an adverse impact in our operations.*

We and our banking subsidiaries are subject to regulation and supervision by the FRB. Our banking subsidiaries are also subject to regulation and supervision by state banking regulators and the FDIC. Federal and state laws and regulations govern numerous matters, including changes in the ownership or control of banks and bank holding companies, maintenance of adequate capital and the financial condition of a financial institution, permissible types, amounts and terms of extensions of credit and investments, permissible non-banking activities, the level of reserves against deposits and restrictions on dividend payments. The FRB, the FDIC and the state banking regulators have the power to issue cease and desist orders to prevent or remedy unsafe or unsound practices or violations of law by banks subject to their regulation, and the FRB possesses similar powers with respect