UNITED LABOR BANK f.s.b.

EXECUTIVE OFFICES

May 20, 2010

To: Our United Labor Bank Clients

Structured Defaults

On Sunday, May 9, 2010, I watched a CBS *60 Minutes* program on the rise of "structured defaults". Having been in the banking and lending business for over 25 years, I was naturally interested in this new phenomenon that has become popular with borrowers whose property has devalued in the current economic cycle.

A structured default is when a borrower defaults because the current value of their home is less than the balance owed. It is not due to financial hardship: the borrower has the capacity to meet the monthly obligation of the loan.

The borrower that was interviewed on *60 Minutes* stated that his neighborhood had devalued to a point that there were foreclosures at every fourth house, and the value of his home was well below the amount that was owed to the bank. This borrower stated that he was working, could afford the house payment, but was choosing to default. He rationalized that he could live in the house "rent free" during the foreclosure process, then move to a rental for a period of time to save funds and repair his credit from the default. This borrower essentially said that he considers his contract with the lender to be one sided in his favor. If the value changes, the borrower can walk without recourse. Who would want to enter into a one sided contract like that?

What the *60 Minutes* segment did not cover was the potential ramifications of structured defaults. The borrower who defaults may be subject to more trouble as a result of their actions. Their FICO score may be negatively affected by about 80 points, which may not be sufficient to qualify in the future. The borrower may also be subject to a tax liability for the loss that the lender may take when they sell the foreclosed property.

The potential greater risk will come from the lending industry. Lenders may look at a borrower who had a structured default as a higher risk. Lenders may require all borrowers to have higher levels of equity when purchasing as a protection against the risk of a structured default. Lenders may charge higher interest rates to further protect against loss. Or, lenders may look at prior structured default borrowers as an unacceptable risk for future loans.

Lenders recognize that there is an inherent risk in lending. Borrowers may fall on hard times, lose jobs, get divorced, or even have deaths in the family. Lenders reserve for these situations. But a structured default is a default of character, not a default of need or economic circumstance. We should remember that an appraisal is only a snapshot in a specific time period, and most experts believe that real estate values should return to prior or normal levels in 5 to 7 years.

With Regards,

Malcolm F. Hotchkiss
President & Chief Executive Officer