



## HERITAGE BANK of the Ozarks

WHAT A BANK SHOULD BE

November 5, 2008

To: Federal Deposit Insurance Corporation (FDIC)

From: Bill Lewis, President/CEO

Subject: RIN 3064-AD35

I appreciate the opportunity to comment on the FDIC's proposal to raise premiums in order to recapitalize the insurance fund and to change the risk-based premiums classification system. A strong FDIC insurance fund is important to maintaining depositor confidence and I support changes to the premium calculation that truly reflect the risk of loss to the FDIC. However, as a healthy bank that had nothing to do with the current problems, I believe that the aggressive recapitalization proposed would be counterproductive and would limit my bank's ability to meet local credit needs.

The proposal would significantly raise premium assessments to aggressively recapitalize the insurance fund in five years to over 1.25 percent of insured deposits. Yet the Federal Deposit Insurance Reform Act requires the FDIC to rebuild the fund to 1.15 percent in five years and to take longer when there are "extraordinary circumstances." There is no question that these are extraordinary circumstances and excessively high premiums only reduces the resources that I have available to lend in my community. It is also counter to other efforts by Congress and the Treasury to stimulate lending. Premium rates should be substantially less than what is proposed.

As a new locally owned bank, there are at least three other areas where the plan is particularly unfair to banks like mine. These areas concern planned treatment of 1) banks that use FHLB advances, 2) high growth De Novo banks, and 3) banks that use the CDARS program. All of these issues are particularly sensitive to a new bank that may rely on each strategically to maximize their opportunities to become profitable as quickly as possible. Rather than discourage start-ups, the FDIC should recognize that regulators supervise de novos very carefully. In this way, the examination process already recognizes risks posed by de novos, and that is already included in the premium calculation.

### *Federal Home Loan Bank Advances-*

I am extremely concerned about the penalty assigned to use of Federal Home Loan Bank advances greater than 15 percent of deposits. We have used advances for several reasons. Most importantly, it's a stable source of liquidity that allows us to manage the overall cost of funding. In this volatile environment, there are often weaker institutions that have bid up the cost of local

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retail deposits. FHLB advances often provide a lower cost of funding than local deposits. Without advances, we would be forced to rely on these deposits more heavily during these periods. In fact, the availability of advances was particularly useful during the last six months. If the FDIC added a significant penalty, this would do nothing more than raise the cost of funding – with no change in the risk of the assets that I fund – and end up reducing my bank’s profitability. Thus, raising the cost of funding by FDIC is not consistent with safe and sound banking.

Second, we use advances to match-fund longer term loans. This allows community banks like mine to effectively manage our interest rate risk. This type of funding is not available elsewhere. Seasoned members of the Federal Home Loan Banks, like me, naturally maintain advance balances higher than the industry average. Comparing seasoned and regular users of advances to the entire industry (as the 15 percent threshold does) does not pick up “outliers” in any meaningful sense of the word. Rather, that 15 percent threshold is capturing normal use of advances and unduly penalizes banks that have used advances in a safe and sound manner for many years. If the FDIC adopts a threshold approach, it must measure outliers relative to the normal advance levels maintained by members that routinely use advances to maintain flexible liquidity and to lower enterprise risk.

The FDIC should not inhibit good, stable sources of funding. Rather, the focus should be on the risk of the assets that the bank has funded, regardless of the source of funds. Moreover, the Federal Home Loan Banks themselves police the use of advances so that the exposure does not become excessive. The FDIC should remove the use of Federal Home Loan advances from the rule or, at a minimum, move the threshold to truly capture outliers and not normal use of advances.

#### *High Growth De Novo Banks-*

Another area of concern is that this proposal targets de novo banks by penalizing banks through higher premiums that grow more than 20 percent in four years. Start-up banks like mine naturally expect faster growth and we use many sources of funding to fuel the loan growth necessary to hit breakeven and become profitable. Alternative sources of funds are critical as we work to build up our core deposit base. It is always a challenge to reach profitability for a de novo bank, but this additional premium cost represents an enormous burden on banks like mine.

#### *Use of CDARS-*

In addition, I believe that the proposal should remove the Certificate of Deposit Account Registry Service (CDARS) from inclusion in the brokered deposits ratio as these deposits allow my bank to retain customers and keep funding local.

While I too am troubled that some recent failed or troubled banks have used brokered deposits to grow rapidly and fund risky assets, it is unfair to include CDARS deposits in with other, more volatile, forms of brokered deposits. We use CDARS to satisfy the needs of our depositors that want the surety of deposit insurance protection, but maintain the relationship with our bank. CDARS allows us to meet that need and to keep the funding within our community. Without this, these depositors are likely to withdraw money from our bank and spread it on their own or through brokers to banks that truly are higher risk and paying high interest rates. Moreover, some of our depositors will use the Internet to find high rates around the country – and these types of volatile deposits are not even covered by the proposed rule.

Thus, the FDIC should exclude CDARS from the calculation of brokered deposits. This method of funding is not risky and any concerns should be raised as part of the examination process –

which is included in the premium calculation. It is patently unfair to penalize banks like mine that use these stable sources of funding.

Thank you for the opportunity to comment. I hope you will give serious consideration to my thoughts as you finalize the program details. These are indeed extraordinary times with significant challenges requiring all of our best cooperative efforts.

Sincerely,

Bill Lewis  
President/CEO