HERITAGE BANK

Always in your best interest.

July 17, 2009

Mr. Robert E. Feldman, Executive Secretary
Attn: Comments
Federal Deposit Insurance Corporation
550 17th Street, Northwest
Washington, DC 20429

Dear Mr. Feldman:

Enclosed please find a Comment on the Proposed Rulemaking regarding Possible Amendment of the Temporary Liquidity Guarantee Program to Extend the Transaction Account Guarantee Program with Modified Fee Structure. The enclosed Comment is being submitted on behalf on Heritage Bank.

Sincerely,

Michael S. Ives
President and CEO

enclosure(s): 1

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COMMENT ON PROPOSED RULEMAKING REGARDING POSSIBLE AMENDMENT OF THE TEMPORARY LIQUIDITY GUARANTEE PROGRAM TO EXTEND THE TRANSACTION ACCOUNT GUARANTEE PROGRAM WITH MODIFIED FEE STRUCTURE

SUMMARY

The elimination of the Transaction Account Guarantee (TAG) program would be destabilizing to the community bank system until such time as the economy has clearly improved and the Federal Deposit Insurance Corporation (FDIC) has ceased regular closures of community banks.

ABOUT OUR BANK

Heritage Bank is a Virginia chartered bank and is a member of the Federal Reserve System. Our Bank is a traditional community bank with considerable liquidity. As of March 31, 2009, our Bank had assets of $270,000,000, and deposits of $217,000,000, with no brokered deposits. Also, as of March 31, 2009, our Bank had a loan-to-deposit ratio of 81%; noninterest-bearing deposits constituted 27% of total deposits; total transaction deposits (i.e. checking, savings and money market deposit accounts), were 75% of total deposits; and certificates of deposit were only 25% of total deposits. Nonperforming assets as a percentage of total assets were 0.07%, and our holding company, Heritage Bankshares, Inc., had a tangible common equity ratio in excess of 9%, both as of March 31, 2009.

COMMENT

Because of the impact of the recession on commercial real estate values, community banks throughout the country have been trying to move away from real estate finance into business lending. For community banks to succeed at business banking, existing and potential customers must have confidence in the safety of their business deposits. The public now believes that the largest financial institutions have been designated as de facto "Too Big To Fail" (TBTF), and this perception gives these banks an extreme competitive advantage over community banks for business deposits exceeding FDIC insurance coverage. However, so far, the TAG Program has allowed community banks to compete effectively for these business deposits by eliminating any perceived safety advantage for the TBTF banks.

When the TAG Program expires, small businesses that are corporations, partnerships or limited liability companies will only have the benefit of $250,000 in FDIC insurance coverage at any bank, large or small. Many very small businesses and professional firms often have daily deposit balances that exceed the $250,000 FDIC insurance coverage limit. The elimination of the TAG Program creates one more business risk for small businesses that are already struggling in a severe recession. Many of these businesses would react by moving their deposits to TBTF banks. This disintermediation of business deposits from community banks to the TBTF banks will force community banks to rely primarily on consumer certificates of deposit for funding and liquidity.

The current FDIC insurance coverage of $250,000 for corporations, partnerships and limited liability companies is insufficient for even very small businesses and compares unfavorably with the potential FDIC insurance coverages for individuals. For example, the FDIC's own web site has an example under which a husband and wife can obtain $2,000,000 of FDIC insurance coverage using payable on death (POD) accounts in addition to other potential FDIC insurance coverage. In addition, consumers can easily spread their deposits among several financial institutions. Unlike consumers, it is extremely difficult for a small business to use more than one financial institution for its operating accounts because of the frequency of transactions causing substantial swings in deposit balances.

This disparity in potential FDIC insurance coverage between consumers and small businesses is unfair and needs study and appropriate resolution by the FDIC prior to the elimination of the TAG Program. Otherwise, there will be substantial disintermediation from community banks that would cause many community banks to retreat back to commercial real estate lending financed by high-yield certificates of deposit and brokered deposits.

PROPOSAL

The proposed Rule regarding the extension of the TAG Program should be amended as follows:

1. The FDIC should extend the TAG Program through at least December 31, 2010 and be prepared to extend the TAG Program further if the economy has not markedly improved and the FDIC has not ceased regular closures of community banks;

2. The FDIC should charge fees for the additional FDIC insurance coverage under the TAG Program but such fees should be assessed on the same risk-based formula now utilized for the basic FDIC insurance assessment; and

3. The FDIC should initiate a study to determine the appropriate level of FDIC insurance coverage for businesses operating as corporations, partnerships, and limited liability companies to provide effective FDIC insurance coverage for these entities.