

The Meeting of the Advisory Committee on Community Banking

of the

Federal Deposit Insurance Corporation

Held in the Board Room

Federal Deposit Insurance Corporation Building

Washington, D.C.

Open to Public Observation

February 17, 2012 8:42 – A.M.

The meeting of the Federal Deposit Insurance Corporation (“FDIC”) Advisory Committee on Community Banking (“Committee”) was called to order by Martin J. Gruenberg, Acting Chairman, FDIC Board of Directors.

The members of the Committee present at the meeting were: Robert F. Baronner, Jr., President and Chief Executive Officer (“CEO”), Bank of Charles Town, Charles Town, West Virginia; R. Daniel Blanton, President and CEO, Southeastern Bank Financial Corporation and Georgia Bank & Trust Company of Augusta, Augusta, Georgia; Charles G. Brown, III, Chairman and CEO, Insignia Bank, Sarasota, Florida; Deborah A. Cole, President and CEO, Citizens Savings Bank and Trust Company, Nashville, Tennessee; Carolyn “Betsy” Flynn, President and CEO, Community Financial Services Bank, Benton, Kentucky; James H. Gray, Chairman, Beach Business Bank, Manhattan Beach, California; Jack E. Hopkins, President and CEO, CorTrust Bank, National Association, Sioux Falls, South Dakota; Ann Marie Mehlum, President and CEO, Summit Bank, Eugene, Oregon; Joseph G. Pierce, President and CEO, Farmers State Bank, Lagrange, Indiana; Rebecca Romero Rainey, Chairman and CEO, Centinel Bank, Taos, New Mexico; Dorothy A. Savarese, President and CEO, Cape Cod Five Cents Savings Bank, Orleans, Massachusetts; Alan Thian, President and CEO, Royal Business Bank, Los Angeles, California; and Ignacio Urrabazo, Jr., President, Commerce Bank, Laredo, Texas.

Walter E. Grady, President and CEO, Seaway Bank and Trust Company, Chicago, Illinois, and Matthew Williams, Chairman and President, Gothenburg State Bank & Trust Company, Gothenburg, Nebraska, were absent from the meeting.

Members of the FDIC Board of Directors present at the meeting were: Martin J. Gruenberg, Acting Chairman and Thomas J. Curry, Director (Appointive).

Corporation staff who attended the meeting included: Ruth R. Amberg, Valerie Best, Michelle Borzillo, John E. Bowman, Richard A. Brown, Kathleen S. Brueger, Kymberly K. Copa, Carolyn D. Curran, Christine M. Davis, Bret Edwards, Robert E. Feldman, George French,

Alice C. Goodman, Kenyon T. Kilber, Alan W. Levy, Susan Lovelace, Christopher Lucas, Rae-Ann Miller, Arthur J. Murton, Paul Nash, Christopher J. Newbury, Mark Pearce, Sylvia H. Plunkett, Stephen A. Quick, Claude A. Rollin, Barbara A. Ryan, Maureen E. Sweeney, Sandra L. Thompson, James C. Watkins, Cottrell L. Webster, John D. Weier, and Mindy West.

William A. Rowe, III, Deputy to the Director (Acting Comptroller of the Currency) was also present at the meeting.

Acting Chairman Gruenberg welcomed the Committee, including its new members. He said that the previous day's FDIC-hosted conference, "The Future of Community Banking," had been an excellent start for the upcoming year of community banking focused initiatives, and that he hoped the issues raised there could be used to deepen the FDIC's understanding of the evolving challenges and opportunities facing community banks. After providing an overview of the day's discussion topics, Acting Chairman Gruenberg introduced Paul Nash, Deputy to the Chairman for External Affairs, who moderated the day's proceedings. In turn, Mr. Nash introduced the leaders of the panel, "Review: Community Banking by the Numbers," Arthur J. Murton, Director of the Division of Insurance and Research ("DIR"), and Richard A. Brown, Chief Economist and Associate Director, DIR. Mr. Murton said that, at the previous day's conference, the FDIC had tried to describe a variety of trends that occurred over the last 25 years and noted that deeper investigation into data often revealed complexities not apparent on the surface. He invited the Committee to respond to the FDIC's information, including how to define a "community bank," banks' business models, their ability to raise capital, and the effect of technology. Mr. Brown added that the Committee, now familiar with types of data to which the FDIC has access, could help guide the FDIC's research agenda by assisting with articulating the important questions and how they should be asked. The discussion at several points referred to a slide presentation presented the previous day, "Community Banking by the Numbers."

Member Pierce said that he applauded the FDIC's efforts to dig deeper into the data; he also noted that he appreciated the revised community bank definition because a definition limited to "assets less than one billion dollars" was inadequate. Member Urrabazo recommended that the FDIC further explore the relationship between profitability and bank size; he said that he was curious to see if community banks can compete with large banks on cost and noted that he was concerned about having to devote more personnel to "backroom" tasks rather than customers. Member Blanton observed that many analysts discuss what size banks are most efficient but that the FDIC has more data to help address the question; he suggested that the FDIC explore the issue at a variety of asset size levels. Mr. Murton noted that the FDIC had addressed the issue somewhat the previous day when it discussed the components of bank profitability and banks' efficiency ratio (in reality, an inefficiency ratio, he said). He said that the researchers had been struck that it was the revenue side (which included non-interest fee income) rather than the expense side that differentiated community and non-community bank profitability.

Member Hopkins suggested that the research make comparisons based on size after excluding large banks' trading revenues, which he viewed as skewing revenue data comparability. Member Savarese observed that net interest margins continued to drive the business models of many community banks and that, historically, one would expect that the yield curve would return to more normalized levels. However, she continued, because of other issues

that are occurring (including disintermediation, nontraditional competitors, migration of deposits to larger institutions) the historical spread normalization may not occur and it would be important to understand the non-interest income component in the retail banking model. Member Savarese added that she appreciated the resources that the FDIC was applying to the research because it would be easy to draw false correlations based on inadequate research.

Member Brown observed that although fee income was an important differentiating factor between community and large banks, the Call Report does not currently break out fee income into many components and suggested that more detailed Call Report information would be analytically helpful. Member Pierce had earlier recommended that the FDIC further explore the proper classification of loans that had both commercial real estate (“CRE”) and commercial and industrial (“C&I”) loan characteristics. Member Brown later agreed, noting that many loans were actually C&I loans but were misleadingly classified as CRE because they used CRE as collateral. Mr. Murton and Mr. Brown agreed that a better classification was important and that different definitions could result in a different view of business line concentrations among community banks.

Member Mehlum noted that the relationship of a bank’s ownership model and its risk management would be a useful research area. Mr. Murton agreed and said that the FDIC was looking into outside data resources, including S-corporation information. Member Urrabazo suggested that it would be useful to review failed banks to determine at what point the regulator had missed an opportunity to take action that may have avoided failure. Acting Chairman Gruenberg said that the FDIC Office of Inspector General (“OIG”) had produced a summary of its failed bank reports which concluded that failed banks often had three common characteristics: rapid growth, CRE concentrations and reliance on brokered deposits. He added that, generally, examiners had recognized the trends and brought them to bank management attention but that institutions often failed to address the problems, thus leading the OIG to suggest that examiners could have been more forceful in requiring bank management to address their problems. Member Brown recommended that the FDIC explore differences in S-corporation and C-corporation banks, including their failure rates. He observed that the S-corporation model could encourage banks to operate as dividend investments for their owners compared to the C-corporation model which may have encouraged more rapid growth strategies. Member Brown noted that a current legislative proposal would increase the maximum number of shareholders allowed for S-corporation status (from 100); he suggested that increasing that threshold would encourage a more stable banking industry. Member Blanton indicated that for the last 25 years, banks had been viewed as an “equity play” involving rapid growth, which was not a good reason for creating new banks; going forward, he thought that banks would return to being viewed as an income producing stock.

Member Baronner suggested that an area of inquiry regarding failed banks could be how many customers they had; he suggested that failed *de novo* banks may have focused on just commercial customers whereas the more customers a bank had might indicate a more stable deposit base in case of a liquidity problem. He also recommended considering the number of failed bank customers to whom the bank had lent the legal maximum, since, if those customers could not repay, it would drain a bank’s capital faster. Member Savarese observed that, because of the severity of the recent economic collapse, even community banks that consistently adhered

to a prudent business model may have failed (for example, due to an unavoidable geographic concentration), as well as banks that pursued a riskier model which would have failed even in a more moderate economic downturn. She noted concern about “throwing out the baby with the bathwater” and drawing conclusions against prudent models that nonetheless resulted in failure. Member Gray suggested that it would be useful if *de novo* banks’ proposed business plans were subjected to stress testing; regulators reviewing the applications could inquire what the *de novo* banks’ backup business plans would be.

Member Savarese commented that headlines tended to misleadingly imply that community banks failed disproportionately because the headlines often reported merely the absolute number of small and large bank failures; however, when failures were viewed as a percentage of banks of their size, it became clearer that there was not a disproportionate loss of community banks. Acting Chairman Gruenberg said that a statistic from the FDIC research that he found notable was that, of the community banks that were continuing to operate after 25 years (at the end of 2010), the bank size most likely to be continuing had assets of under \$100 million at year-end 1985. Committee members discussed possible other characteristics of those small banks, including whether they were family-owned, S-corporations, or located in rural areas. Acting Chairman Gruenberg indicated that further research was warranted. He noted that the FDIC regulates many small institutions and that these sustainability statistics tended to be inconsistent with the notion that a bank needed a billion dollars of assets to be viable. He further noted that failure statistics based on size could be misleading because not all big institutions that could have failed in 2008-9 were allowed to fail. Regarding the interaction of size and future viability, Member Mehlum said that a concern of hers was the increase in compliance costs. She noted that her bank was spending much more today on compliance and that, in a recent examination, her bank was encouraged to engage third parties to audit areas in which her bank’s performance was already strong. Member Cole agreed that compliance costs were a primary challenge and that customers should be a bank’s priority since, without customers, there would be no bank and no need for compliance.

Member Cole also indicated that it was important that the positive information about the viability of community banking should be communicated more broadly into communities and not limited to a technical report. Member Brown observed that the FDIC’s work needed to be detailed because of the scrutiny that it would receive but that effective communication through the media required some simplification. He suggested using short communications such as press releases or emails that bankers could forward to local media and then to make speaking points available for press interviews. Members Savarese, Cole and Brown further suggested that: the information be presented positively (for example, focusing on the success rate rather than the failure rate); that bankers and their trade associations should be used to carry the message; that repetition of important points was key; and that the effort be sustained for the full year of the FDIC’s initiative.

Member Hopkins suggested that it would be worthwhile to clarify that small bank failures were not “breaking” the Deposit Insurance Fund (“DIF”) by providing statistics that compared the impacts on the DIF of failures of banks over and under \$10 billion in assets. Member Savarese noted that the research presented the previous day indicated that S-corporation banks and mutual banks had shown adherence to a community banking model and a lower

failure rate and commented that the financial system would benefit if more mutual banks were encouraged. Member Urrabazo commented on statistics indicating that there had been substantially more asset growth in non-community banks than in community banks; he said that community banks no longer competed on various business types (such as mortgages, retail business and credit cards) and suggested that regulations were one causal factor. Mr. Murton said that it was unclear how much of future financial intermediation would be done using the regulated banking system and how much would be done through capital market securitization; he observed that policy decisions being made in the coming years would affect the outcome. Member Flynn observed that she was surprised that BB&T was on a community banking panel at the previous day's conference; she commented that BB&T is not a community bank in her view.

Acting Chairman Gruenberg said that, although a tremendous amount of research remained to be done, he felt that the results would be instructive and would tell a positive story about the future of community banking. He said that the communications aspect of the FDIC's initiative would be important and carefully considered and that he hoped that it would dispel any myth that regulators were not supportive of community banks. Acting Chairman Gruenberg said that small institutions had been viable over time and that the public interest was in maintaining as many institutions serving their communities as possible.

Mr. Nash then introduced the FDIC staff that led the second panel, "Discussion: Challenges and Opportunities for Community Banks," Sandra Thompson, Director, Division of Risk Management Supervision ("RMS"), James Watkins, Deputy Director, RMS, and Sylvia Plunkett, Senior Deputy Director, Division of Depositor and Consumer Protection ("DCP"). Ms. Thompson focused her introductory comments on the challenges and opportunities associated with the current examination process. Mr. Watkins described efforts during 2012 to gather information at the conclusion of examinations on topics related to the FDIC's community bank initiative -- ownership structure, capital-raising activities, the current competitive environment, succession management, use of technology and the regulatory process. Based on information from this project, Mr. Watkins reported that banks' capital-raising efforts have focused on retained earnings and offerings, among other strategies. Mr. Watkins also observed that community banks are tied to their local communities, and the majority of their shareholders, accountholders and lending activity are in their local area. He noted that banks are taking positive steps regarding recruitment and retention of human talent and succession management and are reasonably well staffed to meet regulatory requirements. Mr. Watkins said examiners noted relatively few community banks try to be "first to market" in technology, but these institutions do remain current on emerging products and technologies. Turning to challenges, bankers have responded that earnings and retaining staff are issues of concern.

Ms. Plunkett then discussed internal DCP and RMS reviews of their examination processes which identified five common areas for consideration. The first area was the pre-examination planning process which might be made more efficient by tailoring the request list for the bank and increasing communication throughout the process. The second area involved ensuring that there is good interaction between examiners and bank representatives throughout the exam process to avoid surprises at the end. The third area she described concerned leveraging technology so that more examination work can be done offsite; if banks and

examiners can share more information electronically, it could reduce the time spent on the bank premises. A fourth area of opportunity was FDIC technical assistance and outreach to banks; for example, explaining new and changing regulations and hot topics as they develop. Ms. Plunkett said that the final area of consideration was the post-examination process, in which examiners confirm that any needed corrections had been successfully made, and may also include contact between exams. Ms. Plunkett then reviewed a variety of topics that had been discussed by a panel in the previous day's conference. Among the subjects were the most beneficial aspects of the examination process which included: interactions with the examiner; meetings in advance of the examination and the relationship/partnership between the bank and examiners. The least beneficial aspects included: risk scoping; the perceived change in examination focus from safety and soundness to compliance and consumer protection; the perceived decoupling of risk management and compliance examination with the advent of the Consumer Financial Protection Bureau; the lack of standardized training for bank employees about new regulations; and, the tiering of examination procedures based on bank size and complexity. Ms. Plunkett then invited feedback on these and other issues.

Member Flynn said that her bank had just had examinations in all areas but compliance and that the FDIC examiners were professional, helpful, and had excellent communication skills. Ms. Thompson said that she was pleased to hear that report, that RMS and DCP intentionally tried to take a balanced approach to supervision, asking examiners to call situations the way they see them while being professional in their deliberations and communications. Member Cole observed that bankers may complain about examinations, when in reality, the examination process is merely implementing the law's requirements, which may be the real source of their frustration. Member Blanton suggested that, while regulations are being drafted, bankers would welcome guidance from regulators about compliance expectations rather than leaving it to banks to make the determination and find out later whether they were right or wrong. Members Baronner, Flynn and Cole and Mr. Nash then discussed how bankers could provide feedback to legislators about the practical impacts of the legislation under consideration.

Member Baronner inquired about the review of regulations and laws that existed but may no longer be useful. Members Flynn and Blanton discussed an example of limits on the number of electronic transactions in certain accounts although there were not limits on similar in-bank transactions; they noted that the limits frustrated good customers without good reason. Director Curry suggested that it would be important to consistently define what "compliance" means and then gather information about banks' actual costs for compliance, however it is defined. A process of identifying the benefits of the law or regulation would also need to occur, which could then be used to analyze whether a particular provision is cost-effective. Member Savarese agreed that a more empirical cost-benefit analysis would be useful and suggested that such an analysis also consider the scalability of compliance relative to bank size.

Member Savarese described some examination concerns that had been raised at a bankers' conference she attended. One problem was that, at the end of compliance examination, examiners indicate that they are unable to share the results because it had to be sent to Washington first. A second concern was the length of time between the end of a compliance exam and the receipt of the written report. Member Savarese also indicated that oral comments made during an examination, which tended to be more favorable, often diverged from more

critical written reports. She also noted that it occasionally took too much time to obtain an answer about how to implement a legal requirement as it applied to a customer situation, especially when more than one agency was involved in enforcing a law. Member Mehlum suggested that, when examiners tier an examination, that they consider a bank's past performance as well as size; if a bank was consistently strong in an area for example, then a third party audit on that subject might not be necessary.

Member Hopkins expressed some frustration that examiners appeared to impose higher Bank Secrecy Act ("BSA") requirements on small banks that were not imposed on larger ones. He reported that, although his bank had invested substantial resources into BSA compliance software, the examiner indicated that the bank should conduct an additional manual process that Member Hopkins felt could not be imposed on a very large bank. Member Brown said that his bank felt it was necessary to request a large amount of BSA compliance information from a customer and that the customer perceived it would not have to provide as much if it moved its business to a much larger bank where its transactions would be less noticeable. He said that the regulators should ensure that banks of different sizes receive the same levels of scrutiny. In response to the BSA observations, Mr. Watkins said the FDIC instructs examiners to evaluate how the practices conform to the regulation and share best practices when possible. He also noted that articles regarding examination-related topics, including BSA, are available to bankers and the public in the FDIC's *Supervisory Insights*.

Member Brown said that there seemed to be an increase in examiner "flyspecking" fair lending and Community Reinvestment Act examinations. He also reported that there appeared to be a change in regulatory requirements where a bank uses a mortgage wholesaler to originate a loan and that the change shifted the primary compliance burden from the wholesaler to the bank. He said that if his bank was going to be held responsible for the wholesaler's compliance, his bank would need to add an additional procedure to double-check the wholesaler's work. Ms. Plunkett said that she would follow up on this issue.

Ms. Thompson noted that bankers had reported that earnings had been their primary challenge and inquired if, in considering their expenses, community bankers had considered sharing back-office processing or technology costs among multiple banks. Member Savarese said that there was a lot of discussion on the subject now, including at a meeting of America's Community Bankers. She said that a group of Connecticut-based banks are cooperating to provide core back-office systems but that scalability had presented challenges and that there had been a product cycle issue. She added that there could be cost efficiencies if a trade association or commercial outsourcer provides infrastructure for regulatory compliance, if not the entire core system. Member Urrabazo said that the Texas Bankers Association set up a department to provide services and legal opinions on compliance matters and that the cost to join was reasonable. He added that he perceived that examiners were developing a "gotcha" attitude on fair lending and Home Mortgage Disclosure Act reporting; and that bankers' fear of violating those laws caused them to be less flexible in their lending.

The Committee stood in recess at 10:24 a.m. and reconvened at 10:46 a.m. that same day.

Mr. Nash introduced Mark Pearce, Director, DCP, and Jonathan Miller, Deputy Director, DCP, who led the discussion of “Why Community Banks Matter: Customer Perspectives.” Mr. Miller began by discussing five key observations about community banks from the previous day’s panel discussion of the same title. The first observation was the nimbleness of community banks in meeting consumer needs; for example, their ability to make faster decisions on affordable housing deals. The second observation Mr. Miller discussed was their flexibility in underwriting consumer or community development loans; for example, being willing to work with businesses that larger banks would not find worthwhile. The third observation, he said, was their better understanding of the local economy and market, which allowed, for example, innovative programs for first-time home buyers and first-time farm loan borrowers in North Dakota. Mr. Miller also noted that community banks have a better understanding of local circumstances in difficult economic times, such as the farm crisis of the 1980’s. The fourth observation, he said, was the importance of relationship banking, which was involved in all of his previous examples. Finally, Mr. Miller noted that community banks were especially important in rural areas where big banks may not be interested in operating. Mr. Pearce said that another topic he would be interested in hearing Committee opinion on was the role of mobile banking in the future of community banking and economic inclusion. He observed that mobile banking is the wave of the future and may not be cost prohibitive but that it also raised the question of how it would impact the face-to-face relationships that have been a feature of community banking.

Member Rainey observed that it would be a challenge, especially in rural areas, for community banks to invest in technology while maintaining the infrastructure of “high-touch” relationship banking. Member Blanton agreed and noted that there was a challenge in the transition from current generation business customers, who preferred to meet with their banker, and new generation ones, who do not. Member Mehlum said that current customers already relied on technology for part of their banking relationship, such as transfers among accounts, but still wanted to meet with their banker for bigger or unusual financing issues; the key, she said, was to learn how to do both cost-effectively. Member Pierce agreed and added that using technology for transactions actually gives bankers more time for customers who need guidance. Members Urrabazo and Savarese indicated that the customer’s experience of the bank and its use of technology were key, and that customers prefer technology for some purposes but want to be able to reach a banker easily in other situations, such as when they encounter a problem. Member Savarese observed that technology allows much more frequent contact between customers and their bank and that banks should view each contact as an opportunity to reinforce a good relationship; in addition, when customers call with a problem, she suggested that bankers should leap at the personal contact opportunity to strengthen customer bonds.

Member Urrabazo described a situation where there was demand for lower cost housing constructed by an organization that he belonged to but that none of the applicants conformed to the secondary market lending standards; he said that his organization had converted the housing into rentals and would try to improve the renters’ credit eligibility. Member Thian said that his bank served many first-generation Asian immigrants and that a challenge that he saw in the next 10 to 20 years was the transition of their businesses to their American-born children who are more computer savvy and may not feel that a niche bank is necessary to their needs. Knowing that his client profile would change, he said that infrastructure investment decisions were a

challenge; his bank currently offers remote capture but not mobile banking. Member Baronner said that his bank offered mobile banking and also had a totally electronic account which helped drive down costs; he said that the bank also provides customers with incentives to use their debit card, and that the debit card interchange fee the bank earned helped cover costs. He continued that customers who use multiple electronic services stay with the bank longer and noted that, while young people may prefer to conduct all their business electronically, they moved toward preferring a personal relationship as they mature. Member Flynn suggested that banks needed to offer electronic services to succeed and added that half of her customer communications were via texting. She said that, while a building would always be necessary to build relationships, the vast majority of customers preferred electronic transactions.

Member Savarese said that a focus group her bank did indicated that younger people did not care about a bank's community focus, but that it mattered a lot to people aged 45 to 50. She suggested that it was important to keep young people engaged long enough until they saw the bank's community focus as different and valuable. Mr. Miller agreed and inquired how community banks could encourage young people's continued engagement such that, when they were older, they considered working with a community bank. Member Savarese said that encouraging financial education and literacy was important and that there was public openness in the wake of the financial crisis. She said that her bank had a financial literacy director who used web-based resources, including FDIC's "Money Smart" program, to provide instruction at all grade levels and college. Member Savarese said that her bank was thus positioning itself to be a trusted financial advisor and viewed financial education as an opportunity for community banks to build relationships with young people.

Mr. Pearce said that the FDIC worked to expand Money Smart and keep it up-to-date and inquired if there were additional things the FDIC could do to better support financial literacy efforts. Member Urrabazo said that the FDIC software was outstanding and that he appreciated the various languages offered. Member Mehlum said that her bank was part of a consortium spearheaded by United Way that was considering the FDIC system in its curriculum development; she noted that, by being part of a consortium, her bank could participate in financial education in a way that it could not do on its own. Member Savarese suggested that the FDIC could identify and publicize best practices in financial education, and that the FDIC could encourage states to embed financial education in state curricula so that the younger generation does not repeat the mistakes that led to the recent crisis.

Speaking about cyber-security, Member Urrabazo described a situation where a customer's computer was hacked and used to initiate several thousand illegitimate money transfers valued at almost one million dollars. He said that his bank was able to intervene so that losses were greatly minimized, but noted that the customer later questioned the bank's security. Member Savarese agreed that customers can blame banks merely because the bank has put a product into the electronic marketplace; she said that the problem raised an issue of confidence in banks as well as imposing a significant cost. Member Baronner noted that insurance companies offered cyber-security insurance that seemed reasonably priced. Mr. Nash noted that, in an interconnected world, cyber-security is only as strong as the weakest link; he also said that cyber-security was an issue that might see Congressional action this year.

Ms. Thompson, Mr. Watkins, and Ms. Plunkett returned to ask the Committee for insights on topics related to the future of community banking, including succession planning and use of social media. Regarding succession planning, Member Brown noted that his bank uses internships in association with area universities. Member Hopkins said his bank and the state banking association encourage students to pursue technical school and college degrees in banking through scholarships and by assisting schools with curriculum development. Member Mehlum said her bank makes concerted efforts to include younger adult area business leaders on the bank's board, is involved with a local university banking program, and supports various award programs for young people. Member Flynn said that every officer and supervisor at her bank has designated short-term and long-term successors, and the bank ensures the designees receive appropriate education for future assignments.

Ms. Thompson asked about community banks' practices and plans regarding the use of social media. Member Blanton said his bank's adoption of mobile banking has been well received, but that the bank was not pursuing social media, such as Facebook, texting, or Twitter due to the potential reputation risk. Member Flynn said a section of her bank's marketing department is dedicated to social media, allowing the bank to be proactive when positive and negative comments are made about the bank. Member Savarese said her bank recognizes a generational shift is occurring and notes that younger people are less inclined to go to bank branches. Her bank is on Facebook and has seen opportunities for communicating quickly and broadly. Member Pierce said his bank maintains a Facebook presence, primarily to communicate information about the institution's community involvement. Members Cole, Hopkins, Brown, Rainey, Mehlum, Barronner, Thian and Urrabazo said their banks do not have a social media presence, but most indicated they are monitoring and considering the issue. Members Hopkins and Brown discussed the issue of who would want to "friend" a bank and whether there could be a backlash against a business using a medium intended to be "social." Member Rainey noted that the ongoing expense of having a social media presence was an issue. Member Mehlum agreed that social media raises a resource issue and observed that her customers had expressed more interest in mobile banking which her bank is launching soon. Member Thian said his bank, a *de novo*, does not view social media as a priority. Member Brown said that his bank was also cautiously approaching mobile banking and Facebook.

Ms. Thompson also inquired about the Committee members' views on extending the Transaction Account Guarantee Program, pursuant to the *Dodd-Frank Wall Street Reform and Consumer Protection Act* ("Dodd-Frank Act"). This program will expire at year-end 2012 unless extended by Congress. Member Brown said he favored extending the program for one or two years to preserve liquidity until the economy normalizes. Member Rainey agreed, adding there is now excess liquidity, but the next couple years are unknown and that the program helped level the playing field for problem banks that may still be struggling. Member Blanton indicated the program had been vitally important when the financial system needed to be stabilized, but it ultimately costs the banking industry more because more funds are insured; he said that, although he was "on the fence" on the issue, he thought an additional year of the program made sense. Member Mehlum reported that a consensus at a recent meeting of the Oregon State Bankers Association was that it would be helpful to extend the program for another year. Member Baronner agreed and added that the program was an important liquidity tool. Member Savarese said that, although also "on the fence," she is inclined to favor a short-term extension

but not a long-term one, which would provide an imprimatur to less-sound institutions. Member Flynn said the program is very important to her bank, which has significant municipal deposits; she added that the extension should be for three years at a minimum, and preferably for five years. Members Thian, Pierce and Cole agreed the program should be extended.

Member Urrabazo recommended cutting the program because banks were misusing the insurance and acquiring funds for the wrong purposes. Further, he said the Texas Bankers Association discussed an opt-in version of the program so banks that do not want to pay for additional FDIC insurance would not have to subsidize those who do. Member Hopkins said that a problem with an opt-in program would be that “too big to fail” banks would opt-out, thereby shifting the costs to smaller banks. Member Gray said he favored an extension, but also recommended that the FDIC stress test the past three to five years to estimate how much banks had paid for the program (which he believed had been relatively expensive). Mr. Nash said the FDIC would inquire further into the costs of the program. He also noted that the extension or non-extension of the program was the only likely outcome, that Congress is unlikely to change the program’s operation.

Mr. Nash inquired about the future of community banking and banking products and services in the next five to ten years. Member Blanton said a major challenge is transitioning to the next generation of customers and understanding how to deliver products to them. Member Savarese said the future changes to the payments system are either a tremendous opportunity for the banking industry or an obstacle because of disintermediation. She suggested the community banking industry could differentiate itself by leveraging its regulated nature, transparency, and trusted position to offer electronic transactions that are as safe and secure as the current face-to-face ones. Member Cole said the future also involves managing the cyberspace platform.

The Committee discussed various aspects of mortgage banking. Member Flynn said mortgage banking remains important in her market. Member Hopkins indicated he was concerned about the secondary mortgage market, and his bank is experiencing “push-backs” from Government Sponsored Enterprises (“GSE”) on foreclosed loans. Members Blanton and Pierce expressed concern that community banks’ ability to originate mortgages is in jeopardy because big players who formerly aggregated and then sold loans are leaving the market. Member Gray added that mortgage lending to the next generation would be complicated by their expectation of always using Internet resources to obtain the best deal. Member Savarese said her bank is committed to mortgage lending, and the recent crisis had allowed it to regain market share because other lenders had retrenched. However, she observed that GSE pushbacks and compliance burden are threats. Member Baronner said his bank had found a niche in portfolio mortgage lending, for example, providing construction loans for custom homes. He agreed secondary market loans are hard to accomplish and create a negative customer experience for which the local bank was blamed.

Member Thian said that focus of his bank, which has a high percentage of Asian immigrants, would be on international trade. He said a challenge during the last couple of years had been customers who did not use their full credit lines because of broader economic uncertainties; on one hand the bank was happy about the resulting lower risk, but also was unhappy about the lack of interest being paid. Member Thian said his bank closely monitors

customers using high percentages of their credit lines and covered some of its risk by participating in Small Business Administration (“SBA”) programs.

The panel titled “Lessons Learned and Successful Strategies: The Community Bank of the Future,” was not separately convened at this meeting.

The Committee stood in recess at 12:02 p.m. and reconvened at 1:37 p.m. that same day.

Mr. Nash then began the “Roundtable Discussion” of the day’s meeting by asking the Committee members to discuss their local and regional economic and banking conditions and expectations; he also invited the new Committee members to describe their institutions. Member Mehlum, of Summit Bank, Eugene, Oregon, said that her bank started in 2004, was a locally-owned and business-focused bank with about \$130 million of assets and 300 shareholders, of whom, about 99 percent live in the local area. Her view was that the Eugene area continued to face difficulties, but that Portland real estate values and employment were doing better. Member Baronner, of Bank of Charles Town, Charles Town, West Virginia, reported that his bank, begun in 1871, has about \$300 million of assets in a diverse mix and about 1,100 shareholders. He said that his area, not far from Washington, D.C., had been a center of subprime lending for tract developments by big banks, that there had been a steep housing price decline and that building trade employees had been hard hit. Member Baronner said he believed the area economy was at the bottom, that there had been a recent increase in loan volume, that Marcellus shale drilling was doing well while southern coal fields were not, and that state finances were sound.

Member Savarese, of Cape Cod Five Cents Savings Bank, Orleans, Massachusetts, said that her bank, formed in 1855, had a traditional focus on savings deposits and residential mortgages but had changed over the last 20 years to adapt to its customers’ needs; three-quarters of its balance sheet was in residential mortgages but it also has substantial commercial lending, as well as other business lines. The bank has a quasi-philanthropic aspect, she said, with a foundation that donated money as well as employees devoted to financial literacy and assisting non-profit organizations. Member Savarese said that the bank’s local economy, which was very seasonal and focused on lodging, had seen a recent uptick in residential real estate purchases. Massachusetts has a diversified economy, she said, which had not experienced high growth and did not see as significant diminution in values as other areas; still, she did not see much economic traction going forward. Member Savarese said that the state was generally overbanked which resulted in very low interest margins. Member Thian, of Royal Business Bank, Los Angeles, California, noted that his bank, which opened in late 2008, had achieved profitability along with significant capital growth. He described his bank as a niche bank intended to serve Asian immigrants, with a focus on Pacific Rim trade activities, as well as engaging in C&I and CRE lending. He said that his bank was a minority depository institution (“MDI”) and complimented the MDI program and the FDIC’s responsive assistance. Member Thian noted he belonged to the National Association of Chinese Immigrant Bankers, which has about 30 members from smaller banks, and said that many of them needed more support from regulators to improve their compliance operations.

Member Flynn, of Community Financial Services Bank, Benton, Kentucky, said that her bank was 123 years old and that employees owned half the stock; she said that, by utilizing

technology, the bank had grown significantly in the last couple years without increasing the number of employees. She said that Kentucky had experienced only two percent depreciation in collateral value and that its unemployment rate was 8.46 percent; she said that her bank's area economy was doing pretty well, in part because there were two universities in its market. Member Pierce, of Farmers State Bank, Lagrange, Indiana, said that his bank has assets of about \$480 million and functioned as a traditional community bank with about 40 percent of its loan portfolio in residential lending and 20 percent in agricultural lending. He noted that over 40 percent of the local population is Old Order Amish and that many of them work in the manufactured housing and recreational vehicle industries, and also engage in woodworking. Member Pierce said that he believed that the economy had reached a turning point, although it would be a long, tough road to recovery; he said that area housing prices had started upward, customers were fairly optimistic, loan demand was relatively strong, and that farmers were doing well (although he felt that some recent agricultural land prices seemed too high). Member Pierce said that he had had a good experience using the FDIC Ombudsman's office and encouraged others to use it if they had examination or other problems.

Member Cole, of Citizens Savings Bank and Trust Company, Nashville, Tennessee, noted that her bank, with about \$100 million in assets, was also an MDI which focused on lending to churches in Tennessee and in other nearby states. She said that the Tennessee economy was doing well and that substantial investment was expected in Memphis in the coming year. Member Urrabazo, of Commerce Bank, Laredo, Texas, described his \$560 million asset bank as a "border bank." He said that the Texas economy was doing well generally, with a recent decrease in unemployment to 8 percent. Member Urrabazo said that the area economy was doing well because of the increase in import-export business across the Mexican border and the drilling of 300 new oil and gas wells in the Eagle Ford shale area. He said that the real estate market remained terrible with almost no new home construction occurring, but that C&I lending had improved substantially; he expected a difficult but profitable year in 2012. Member Gray, of Beach Business Bank, Manhattan Beach, California, said that his bank, formed in 2004, has about \$300 million in assets. He said that, being in an urban center, it was necessary for his bank to determine what it could do well and concentrate on those areas. Member Gray described a division of the bank, Doctors Bank, which serves doctors and dentists across the United States. He said that the economy where his bank operates was affected by very large banks cutting their business customers' credit lines; his bank obtains many of these former big bank customers through personal referrals. He said that his bank was successful in 2011, noting that it had a large SBA loan program and does substantial C&I lending, but does not provide mortgage or consumer lending.

Member Hopkins, of CorTrust Bank, National Association, Sioux Falls, South Dakota, said that his bank has assets of \$675 million and branches in a wide variety of communities in order to diversify the economies in which it operates and its loan portfolio. He said that agriculture was doing exceptionally well and that the Sioux Falls area was doing well in part because it is a medical center and because large financial services have operations there. Regarding employment, Member Hopkins said that the problem was finding employees to fill jobs. The Minneapolis-St. Paul area continued to suffer, he said, but had reached the bottom; he expected a drawn-out improvement that required four to five years to reach previous employment levels. Member Brown, of Insignia Bank, Sarasota, Florida, said that his five year

old bank has about \$145 million in assets and was profitable in 2011. He noted that his market had experienced 50-60 percent drops in property values but said that homes are now being purchased and that, over the last year, the residential loan pipeline had substantially increased. Member Brown said that recent economic presentations he attended discussed a trough effect which indicated a period of bumpy improvement in southwest Florida and the state as a whole. He said that his concerns included potential global banking problems and the foreclosure backlog.

Member Rainey, of Centinel Bank, Taos, New Mexico, said that loan demand was historically low and that the loan-to-deposit ratio had dropped below 50 percent. Member Blanton, of Southeastern Bank Financial Corporation and Georgia Bank & Trust Company of Augusta, Augusta, Georgia, reported that his bank, with \$1.6 billion in assets, had merged two charters in 2011, thus saving over \$300,000 per year. He noted that the bank had a good return on investment and built up reserves last year. Member Blanton said that the economy in his part of Georgia has good employment and housing markets and that construction loan volume was good. Atlanta, however, was still facing very difficult circumstances, with housing prices still falling; he said that Georgia had a long distance to travel to recovery and that a substantial number of banks could still fail.

Director Curry thanked the Committee members for their valuable input. Acting Chairman Gruenberg said that he thought the meeting and the previous day's activities had been very productive and thanked the Committee. He noted that the FDIC was continuing its community banking research and that there would be a significant amount of information to discuss at the next meeting.

There being no further business, the meeting was adjourned at 2:24 p.m.



Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
And Committee Management Officer
FDIC Advisory Committee on Community Banking

Minutes
of the
Meeting of the FDIC Advisory Committee on Community Banking
of the
Federal Deposit Insurance Corporation
Held in the Board Room
Federal Deposit Insurance Corporation Building
Washington, D. C.
Open to Public Observation
February 17, 2012 - 8:42 A. M.

I hereby certify that, to the best of my knowledge, the attached minutes are accurate and complete.

Martin J. Gruenberg
Acting Chairman
Board of Directors
Federal Deposit Insurance Corporation

Dated: May 16, 2012