From: Steve Bridges [mailto:steve@cbaofga.com]
Sent: Tuesday, December 16, 2008 2:17 PM
To: Comments
Subject: Comments for RIN 3064-AD35

The comment letter is pasted in below:

Robert E. Feldman
Executive Secretary
FDIC
550 17th Street NW
Washington, D. C. 20429

SUBJECT: RIN 3064-AD35- Notice of Proposed Rulemaking on Deposit Insurance Assessments

Dear Mr. Feldman:

The Community Bankers Association of Georgia (CBA) appreciates the opportunity to submit comments on the Federal Deposit Insurance Corporation's (FDIC's) proposed rulemaking which changes the deposit insurance premium assessment system. CBA is a non-profit trade association representing community financial institutions in the state of Georgia. CBA has over 310 member institutions, including state and nationally chartered commercial banks and thrift institutions. The average size of member institutions is approximately $270 million, but member institutions range in size from less than $50 million up to several billion dollars in asset size. The institutions represented by CBA are geographically dispersed throughout the state of Georgia.

First, we would like to state for the record that the members of CBA are supportive and understand the extreme importance of maintaining a strong deposit insurance system. However, there are a number of specific issues in this proposal and request for comment that we would like to address. We will make some general comments first, followed by more specific comments on certain of the proposed, new risk-based adjustments to the deposit insurance assessment system.

Restoration of the Deposit Insurance Fund within Five Years

Under the proposal the FDIC projects that the proposed plan would restore the reserve ratio to 1.26 by the end of the five year plan. We realize that FDIC's plan was to restore the fund to a higher level than the minimum reserve ratio of 1.15 as a hedge against greater losses due to bank failures, and we realize that the events which have occurred since the issuance of the proposal may support this position. However, the law provides the FDIC with the authority to extend beyond five years the time in which to restore the Deposit Insurance Fund (DIF) to a minimum insurance reserve ratio of 1.15 "due to extraordinary circumstances." Given the happenings of the past twelve months and especially the last 120 days, it would be difficult not to characterize these times as "extraordinary." We realize the DIF must be restored, but such substantial increases in deposit insurance premium assessments at this time, coupled with the new risk-based adjustments will further add to the stress the industry is experiencing. It could further weaken the industry and will result in reduced lending, which runs counter to many of the other recent initiatives of Congress,

the Treasury, the Federal Reserve (FRB) and the FDIC. Therefore, we would urge the FDIC Board to consider using its authority to extend the restoration period beyond five years.

Risk-Based Adjustments are likely to Decrease Prudent Lending

Marketplace developments and responses from the federal government to the current credit crisis have been occurring at a breakneck speed in the weeks since and just prior to this proposal being issued for comment. Among other developments, Congress passed and the President signed the Emergency Economic Stabilization Act on October 3, 2008 and the FDIC invoked its systemic authority under the FDIC Improvement Act of 1991 to establish its Temporary Liquidity Guarantee Program. One of the primary goals of these programs was to stabilize the credit markets, restore the flow of prudent credit, and stabilize the economy of the United States and the world. Additionally, the federal banking agencies issued an Interagency Statement on Meeting the Needs of Creditworthy Borrowers on November 12, 2008 stating that, "The agencies expect all banking organizations to fulfill their fundamental role in the economy as intermediaries of credit to businesses, consumers, and other creditworthy borrowers." The new risk-based adjustments to the assessment rules, especially those relating to brokered deposits and secured liabilities, will discourage many community bankers from continuing to lend in their communities contrary to the intent of all the government initiatives mentioned above and others. We at the trade association (CBA) have already had community bankers contact us and say they have plans to shrink their bank by several million dollars over the next year constricting new lending and allowing brokered deposits and Federal Home Loan Bank (FHLB) borrowings to run off as loan payments will allow, in order to be sure they will not exceed the risk-based benchmarks included in this proposal for brokered deposits and secured liabilities. Since this constriction of lending runs contrary to most other recent government initiatives and because liquidity management is one of the most significant challenges facing the community banking industry today, we encourage the FDIC Board to consider if now is the appropriate time to institute such risk-based adjustments.

Risk-Based Adjustment Benchmarks likely to Become Caps

If this proposal is adopted, the thresholds or benchmarks in this proposal of 10% for brokered deposits and 15% for secured liabilities are likely to become de facto caps for these liability categories. While we realize the proposal does not prohibit a bank from exceeding the risk-based adjustment benchmarks, as mentioned in the previous section, community bankers are already viewing these benchmarks as caps and are already working to get within what they view as the "new guidelines." The fact is that the decision of community bankers to manage to these benchmarks is being reinforced by the field examination staff of the FDIC. FDIC field examiners have already begun using these benchmark levels in their discussions with community bankers, indicating to them verbally, if not in writing, that for instance they expect the bank to reduce its reliance on brokered deposits to no more than 10%. This is happening and the proposed rule is not even final yet. When it becomes final, we believe even greater use of these benchmarks as caps is likely to occur.

In view of this tendency for the benchmarks in this proposal to become de facto caps, we urge the FDIC Board to consider whether it would be more effective to address their concerns with the additional risk they perceive in banks who make heavy use of brokered deposits and secured liabilities in a supervisory policy separate from the deposit insurance

assessment rule. This would allow the issue to be addressed but with greater flexibility than is possible through the deposit insurance assessment rule. For example, such a supervisory policy could allow examiners to make a distinction between two banks carrying the same level of brokered deposits and/or secured liabilities, but with one doing a superior job of integrating these types of funding into the bank's overall liquidity management program in a safe and sound manner. When the examiner makes such a judgment, it would be reflected in the CAMELS rating of the bank and in turn would affect the deposit insurance assessments through the risk category assigned to the bank. So, while benchmark levels would not directly be a part of the assessment rule, a bank making excessive use of brokered deposits and/or secured liabilities, especially in an unsafe and unsound manner, would still pay higher insurance premiums.

Community Banks Need Flexibility in Meeting their Liquidity Management Challenges

In the current environment, one of the most significant challenges facing community bankers is safe and sound management of the bank's liquidity. While larger banks have various sources for obtaining non-core funding to support their operations, beyond federal funds purchased, brokered deposits and FHLB borrowings are about the extent of what is available to the average community bank to manage their funding needs. While we recognize that there have been abuses (i.e. banks obtaining over 80% of their funding from brokered deposits), there are community banks that have prudently managed levels of brokered deposits and secured liabilities above the benchmark levels included in the proposal for many years, withstanding strict regulatory scrutiny during that timeframe. Many community banks have periodically used these sources of funding to avoid getting involved in imprudent local deposit bidding wars. In other cases community bankers have used a laddered maturity of brokered deposits going out to four and five year maturities or FHLB borrowings of three to five year maturities to match fund certain loans. It is critical that community banks be able to maintain reasonable flexibility in managing the bank's funding. If the risk-based adjustment benchmarks for brokered deposits and secured liabilities are included in the final rule and they become de facto caps (which we already see evidence of with field examiners), the needed flexibility will be gone. We recognize that some additional guidelines, including perhaps some upper limits, need to be established, but, as previously mentioned, a separate supervisory policy addressing these issues would be a more effective approach. Also, a new supervisory policy would allow the FDIC to phase in the new guidelines.

Brokered Deposits

There are a number of issues related to the brokered deposits provisions in the proposed rulemaking we would like to address:

Network Reciprocal Deposits: For the purposes of this proposed rule, FDIC has used the statutory definition of brokered deposits, which includes deposits received through a network on a reciprocal basis (i.e. reciprocal CEDARS deposits). Many Georgia community banks use the deposit placement services of CEDARS to accommodate established local customers who have requested full FDIC insurance coverage. As you know, these funds are placed with other banks in the network at levels which maintain deposit insurance coverage and equal sums of funds from other banks are received by the original bank. While we know FDIC has interpreted the statute that these deposits are included in brokered deposits, in practice, these deposits have characteristics more similar to core deposits. For

example, such deposits are built on local customer relationships and are almost always obtained from within the geographic footprint of the community bank's normal market area, they have shown a high degree of "stickiness" (i.e. There is a high reinvestment rate on these deposits.), and the rates on these deposits are set by the individual community bank based upon that bank's funding needs and its local market.

The concern expressed in the proposal regarding brokered deposits is that, in the event of failure, brokered deposits detract from the franchise value of the failed institution. In view of the core deposit characteristics of network reciprocal deposits, they should enhance the franchise value of the failed institution similar to other local deposits. Also, FDIC has noted that currently such deposits are not separately identified on the Call Report making it impossible to separate these out from other brokered deposits. Community bankers in Georgia have indicated it would not create a burden for them to include this information separately on the Call Report. Therefore, we would strongly encourage the FDIC Board to exclude reciprocal deposits obtained through a network from the definition of brokered deposits for the purposes of this proposed assessment rule. In fact, the core deposit characteristics of these deposits should encourage the FDIC to support legislation to exclude such deposits from brokered deposits in the Federal Deposit Insurance Act.

Brokered Deposit Thresholds for Risk Category I Banks: The proposal would require a surcharge to the base deposit insurance premiums for a Risk Category I bank, if the institution's brokered deposits exceed 10% of domestic deposits and the institution's total assets are "more than 20 percent greater than they had been four years previously." As we understand it, Risk Category I banks consist of sound financial institutions with no major weaknesses. We would assume that a bank must be properly managing its funding strategies, including its brokered deposit funding, in order to be a Risk Category I bank. Therefore, it would not seem necessary to charge an insurance premium surcharge related to brokered deposits for Risk Category I banks. We encourage you to consider dropping the brokered deposit surcharge for Risk Category I banks.

Brokered Deposit Threshold of 10%: The proposal would establish a benchmark for brokered deposits at 10% of domestic deposits. As mentioned above, for Risk Category I banks this 10% threshold is coupled with another threshold of 20% for aggregate growth over the last four years. For all other Risk Categories the 10% of domestic deposits threshold stands alone. The proposal would require banks exceeding these thresholds to pay an insurance premium surcharge for being too heavily reliant on brokered deposits for funding.

This 10% threshold seems to have been established at a very low level. Many community banks have operated in a safe and sound manner for many years with considerably higher volumes of brokered deposits. During those timeframes these community banks received considerable regulatory scrutiny of their funding strategies, without receiving regulatory criticism. We realize that the FDIC feels a need to reduce the risk of loss upon failure of a bank with brokered deposits; however, we believe it is possible to operate a community bank in a very safe and sound manner with brokered deposits of at least a twenty to twenty-five percent. Assuming the risk-based benchmarks for brokered deposits are adopted, we strongly encourage the FDIC to consider a higher threshold for brokered deposits.

Rapid Asset Growth Threshold of 20%: As mentioned above, the proposal combines the brokered deposits benchmark or threshold of 10% of domestic deposits with a threshold of

20% aggregate growth over the last four years for Risk Category I banks. This 20% growth rate is defined in the proposal as "rapid asset growth." Obviously, if an institution averages more than 5% annual growth, it would exceed this growth threshold. On page 59, the proposal itself, states that the average growth in total insured deposits of all FDIC insured financial institutions has been 5% per year, "for the most recent five and ten year" periods, and estimated insured deposits increased by 5.4% for the twelve months ending June 30, 2008. Generally, community banks can support asset growth equivalent to their deposit growth, assuming the bank has adequate capital to support such growth. Surely asset growth at the rate of the average deposit growth for the entire banking system should not be defined as "rapid asset growth." Also, there have been interest rate environments in the not-too-distant past where growth strictly from the compound interest rate on deposit accounts could cause a community bank to grow almost at that rate. Assuming the risk-based benchmarks for brokered deposits are adopted, we urge the FDIC to raise the threshold for defining "rapid asset growth."

Deposit Listing Services: So-called "internet deposits" or deposits generated through a deposit listing service do not meet the statutory definition of brokered deposits. However, the proposal asks for comments on the merits of inclusion of such deposits in the definition of brokered deposits for purposes of the calculation of the "adjusted brokered deposits ratio."
Deposits generated through a deposit listing service provide a beneficial supplement, as well as, an alternative to a community bank's local market deposit funding. Further, such deposits are frequently a significant component of community banks' contingency funding plans.

Advertising rates on a listing service seems little different than advertising rates through media sources, such as the newspaper, television, or radio. The listing service does not refer depositors to a particular listing institution and makes no representations regarding the amount of deposits which may be obtained from the listing. Finally, the deposits result from a direct communication between the bank and the customer. On a case by case basis, the bank establishes an individual relationship with each depositor. In view of the nature of these deposits as described above, they do not seem to have the same characteristics as brokered deposits and should not be included in the definition of brokered deposits for the purposes of this proposal.

Secured Liabilities

The proposal would require an upward adjustment of the base insurance premium rate, if an insured institution's ratio of secured liabilities to domestic deposits exceeds 15%. This surcharge would be assessed with respect to institutions in all risk categories. While the proposal includes other types of loans in the definition of secured liabilities, FHLB advances are the primary type of secured liability used by community banks in Georgia. FHLB advances have provided many community banks in Georgia with access to a reliable and stable source of low-cost funding over the years. These advances help community banks to serve the credit needs of their communities, support local home ownership and assist with local community development. The additional charges when the threshold is exceeded would increase the cost of a vital source of liquidity, when liquidity risk is one of the most significant challenges facing community banks in our state today. It would also result in an increase in the cost of borrowing money, and perhaps result in many institutions extending less credit, at a time when many of the recent government initiatives have been directed at

thawing the credit markets and stimulating lending. Reductions in prudent lending would also impede the recovery efforts of the local economies where community banks operate, as well as, impeding the recovery of the broader economy as a whole. We encourage you to carefully re-examine this proposal in light of the above discussion.

Phase in of Risk-Based Adjustments to Deposit Insurance Assessments

If FDIC proceeds with the adoption of the risk-based adjustments to deposit insurance assessments, especially those relating to brokered deposits and secured liabilities, we would encourage you to delay the effective date of the resulting surcharges to be added to the base rate of deposit insurance premiums. Many community banks have operated for years with considerably higher volumes of brokered deposits and secured liabilities, integrated safely into their funding strategies, than the proposed benchmarks would allow without a surcharge. They have operated in this manner with scrutiny from both state and federal regulators without criticism. It is not reasonable to expect many of these community banks to change their funding strategies and reduce reliance on these alternative sources of funding overnight.

For example, many community banks have employed a laddering of maturities strategy, which may stretch out to four or five years, in regard to the brokered deposits they have obtained. They have made loans based upon the availability of these deposits at the stated interest cost. If a surcharge is added to the base insurance premium for these deposits, this increases the cost of the funds supporting those loans. This adds an operating cost that the bank could not have reasonably anticipated and will, in effect, further squeeze already tight net interest margins. Further, there is little, if any, opportunity for the bank to mitigate this additional cost since it has a deposit contract with the depositor of these brokered time deposits with a stated maturity date (The deposits cannot be paid off early.). Such additional cost would place additional strain on many community banks that are already stressed.

Therefore, assuming the risk-based premium adjustments for brokered deposits and secured liabilities are adopted, we believe it would be reasonable for the FDIC to delay the effective date to allow banks time to adjust strategies and minimize the impact of the increased cost. Given the laddered maturity of brokered deposits example provided above, the delay would need to be at least two years to provide adequate time for adjustment.

Conclusion

In conclusion, we want to thank the FDIC for the opportunity to comment on the proposed rulemaking to change the deposit insurance assessment system, adding certain risk-based adjustments. The community banks of Georgia support the efforts of the FDIC to restore the Deposit Insurance Fund; however, we urge you to consider all comments carefully before adopting this proposal.

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