



FINANCIAL MANAGEMENT SERVICES, INC.

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December 15, 2008

Robert E. Feldman, Executive Director
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, DC 20429

Dear Mr. Feldman:

We appreciate the opportunity to comment on the proposed changes to the FDIC insurance assessment methodologies. Financial Management Services, Inc. (FMSI) is an asset/liability--interest income management firm that assists community banks in the management of their balance sheet. Our clients utilize the Federal Home Loan Bank (FHLB) and broker deposits to manage their balance sheet funding costs and interest rate risk management. These products have been extremely valuable tools for our clients, but also for other community banks.

They have proven to provide:

- 1) **Liquidity, both for short term and longer term needs**
- 2) **Liability cost management, such as marginal cost of funds analysis**
- 3) **Interest Rate Risk Management Tools**

Liquidity

A) Both the FHLB and broker deposits have provided a source of liquidity to allow banks to manage their cash flow needs on a short-term basis. These sources allow banks to make loans while they adjust liability cash flows to balance asset needs.

These funding sources also provide longer-term liabilities to match longer-term asset maturities.

Effective Cost of Funds

B) FHLB and Broker deposits often provide effective cost of funds relative to bank CD costs. The alternative funding is substantially more cost effective when applying a marginal cost of funds analysis. The current market conditions are a good example. Currently, the market has many new institutions (Goldman, Morgan Stanley, American Express, insurance companies) that have converted to banks. These companies are aggressively in the retail community bank markets absorbing / contesting for retail CDs at very high rates. New market players' CD rates are above broker deposit rates (or FHLB rates) that community banks can obtain. The new assessment methodology would penalize community banks for their past, prudent management practices and limit or penalize their use of alternative funding sources (when it is prudent to do so).

Interest Rate Risk Management Tools

C) FHLB and brokered deposits provide types of liabilities that are not available through their retail CD deposit base. These include longer-term liabilities to offset longer term fixed rate assets. Secondly,

banks can issue liabilities wherein the bank owns the call option on the liability. This allows the bank to offset callable assets (assets that can prepay in lower rate environments, assets without floors, or assets with no prepayment penalties). For the most part, retail bank CD maturities do not exceed 1 year. Given the current low rate environment (30 yr single family loans at 4.50%), interest rate risk could well be a major issue on a going forward basis.

DTC broker deposits do not have a withdrawal option. They cannot be withdrawn (except for death or adjudication of incompetence). Therefore, they cannot be allowed to have a run on a bank. They are a known, and fixed term.

We encourage the FDIC to not discourage the effective use of alternative funding sources to manage the income and price risk of a bank's balance sheet.

Secured liabilities don't necessarily increase the risk to the Deposit Insurance Fund (DIF) unless managed in a non-prudent fashion. We could make a strong case that FHLB and broker deposit markets provide invaluable sources of liquidity and assists in the mitigation of interest rate risk. We would suggest that these liquidity sources have been effective in supporting the financial system under current stressed conditions. In contrast, liquidity sources provided from inter-bank lending and the capital markets have disappeared in a time of extraordinary need. FMSI believes the FDIC would be dealing with many more failures without the support provided from the FHLB system.

We understand the timing of the increase in assessments given the current stressed conditions of the DIF and the likelihood of further deterioration of the reserve fund in future months. As you are aware, the U.S. financial system is in the process of de-leveraging. The "pay-to-play" assessment methodology may work well under normal conditions, but the current environment wouldn't be characterized as normal. An assessment system encouraging further de-leveraging seems contradictory to current government policies/programs encouraging banks to expand their balance sheets and lend money in their communities. For example, the FHLB provides a funding source for banks to utilize a program such as the recently introduced Treasury Capital Purchase Program to lend money in their communities.

An assessment system penalizing banks with secured liabilities exceeding 15% of deposits isn't consistent with trying to improve the flow of credit. We would suggest eliminating this component of the assessment calculation due to current economic/liquidity conditions and the belief that the FHLB is an important backstop to the financial system. The FHLB balance sheet is an important support valve to the financial system in a time when many balance sheets are contracting. The FHLB is a cooperative that returns a portion of its earnings to its membership base. It is important to recognize that the volume of FHLB advances on a bank's balance sheet requires a corresponding capital investment into the FHLB. In summary, the FHLB is an important resource to banks and the economy in this challenging environment. FHLB utilization for balance sheet / interest risk management should not be discouraged.

FMSI would also recommend that broker deposits be more clearly defined when determining assessments. The current definition leaves much to be desired. Many of our clients currently utilize the Certificate of Deposit Account Registry Service (CDARS) reciprocal deposits. These deposits provide a valuable service to depositors and historically have provided a stable funding source to financial institutions. The deposits generated from this program are typically local and could be considered part of a bank's core funding. The current proposal doesn't differentiate between these deposits as they are

considered broker deposits for call report purposes. **We would recommend differentiating between these types of deposits and out of market broker deposits.**

10% Broker Deposit / 20% Growth Threshold

FMSI is concerned with 1) an arbitrary % being an absolute maximum and 2) applying the same % to all size banks. An arbitrary % becoming a maximum for community banks could well hurt their current mode of operation for prudently managing the bank's balance sheet as discussed above. Secondly, smaller community banks can be placed at competitive disadvantage, if the same growth % is applied to smaller community banks vs. large regional and national banks. **Community banks should not be placed at a competitive disadvantage.**

We recognize the FDIC is facing many challenges with managing the DIF. The government has implemented many new programs that will expire in 2009. It may be appropriate to re-structure the assessment system following the expiration of these programs. A re-structuring may be more plausible when the credit markets and economy have stabilized.

We feel the assessment system should be structured in a manner that is consistent with current government policies promoting lending in local communities. Further, banks should have the freedom to prudently and effectively manage their interest rate risk with the above tools. The proposed assessment changes may discourage financial institutions from maintaining or expanding their balance sheets at an inopportune time. Some FMSI clients are currently shrinking their balance sheet due to the above proposal. The current proposal may result in unintended consequences and may deter banks from expanding lending programs at a time the economy needs this stimulus the most.

Sincerely,

Douglas Williams, President / CPA
Chuck Crouch, CFA