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November 5, 2008

To Federal Deposit Insurance Corporation (FDIC)

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. In addition, I believe that the proposal is particularly punitive to banks that use Federal Home Loan Bank advances. My bank has relied on these for many years as an important complement to deposit funding and have used these in a safe and sound manner.

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.

I am also writing to comment particularly on the penalty assigned to use of Federal Home Loan Bank advances greater than 15 percent of deposits. We use 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 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. Adding an additional cost is not consistent with safe and sound banking.

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

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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.