April 1, 2009

Federal Deposit Insurance Corporation
Attention: Mr. Robert E. Feldman, Executive Secretary
550 17th Street, NW.
Washington, DC 20249

Re: FDIC Assessments; Interim Rule; RIN 3064—AD35

In February, Federal Regulators facing a cascade of bank failures depleting the deposit insurance fund began looking at increasing the fees paid by U.S. financial institutions for replenishment. Although the FDIC intended on charging more from higher risk banks, it was also suggested levying a hefty emergency premium in a bid to collect $27 billion this year. The higher premiums being assessed were originally set for 20 cents for every $100 of insured deposits levied equally on the 8,305 federally insured institutions. To put that in perspective, for a $250 million dollar community bank, the "one-time tax" would constitute a $500,000 hit, which could wipe out 20% to 40% of a bank's annual profits. At the Independent Community Banking Association Conventions last week, FDIC Chairman Sheila Bair predicted that the assessment will probably be lower. She went on to say that the FDIC is seeking comments by April 2nd on whether the agency should use total assets or some other base for the special assessment, which would have consequences for how the burden is distributed.

Upon further research, our teams have concluded, certain parties within the banking industry were more exposed to complicated and unregulated credit default swaps (CDS). We believe that the institutions with the most exposure should be held responsible for their portion of posing systemic risk, locking up credit markets and eventually causing bank failures by allocating assessments not just on toxic assets, but exposure to credit derivatives such as CDS. Notably, Commercial Banks with $10 billion or more in assets fund only 63% of their assets with deposits. Because Community Banks fund 73% of their assets with deposits and have less exposure to credit derivatives, they are unfairly impacted by the above assessment when it is based on deposits as a percent of assets. Developed by the consultants at BancVue, the formula is being forwarded as a directional answer to the call for comments to the FDIC's proposed 10 to 20 basis points levy against all bank deposits.

Proposed Formula

Step 1: Estimate anticipated annual losses due to assets (A) and credit derivatives (D) as a percentage of total anticipated losses from those 2 categories: (A/total losses)+(D/total losses) = 100% of total losses due to toxic assets and credit derivatives.

Step 2: Allocate the total premium needed by FDIC by those percentages (A*Premium) and (D*Premium). As an example, a 20bp assessment on the $9 trillion on deposit in FDIC institutions as of 12/08 would raise roughly $18 billion. If 80% of anticipated losses are caused by on-the-book assets and 20%
by credit derivatives, a total of $14.5 billion would come from assets and $3.5 billion from credit derivatives.

Step 3: Convert the total premium needed in each category to a per-dollar amount that can be assessed against each institution. For example, $14.5 billion over $13.8 trillion in assets = 10.5 bp asset assessment, and $3.5 billion over $15.9 trillion in credit derivatives = a 2.2 bps credit derivative assessment.

BancVue's analysis, based on FDIC data as of 12/2008, shows that commercial banks $10 billion or larger have just over $24 worth of credit derivatives for each dollar of equity. By comparison, the rest of the industry has essentially one-tenth of a penny of CDS for each dollar of equity. Those numbers translate to the larger banks having roughly 23,000 times as much credit derivative exposure versus all other community financial institutions.

Based on these findings, we believe this suggested formula reflects a more accurate assessment based on risk the institution itself placed on the broader market. We would also like to point out that often these tools were used as potential "risk management" tools that have backfired and culminated in posing systemic risk instead.

Please do not hesitate to contact us if you would like further clarification or information.

Kindest regards,

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