TOGETHER, WE GROW COMMUNITIES
Community Bank
OF TRI-COUNTY

Michael Middleton
President,
Chairman of the Board

February 18, 2010

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street Building N.W.
Washington, D.C. 20429

Re: FDIC RIN #3064-AD56
Incorporating Employee Compensation Criteria into the Risk Assessment System

Dear Mr. Feldman:

Thank you for the opportunity to comment on the above referenced advance notice of proposed rulemaking. The background materials provided with the FDIC's recent proposed rulemaking on Employee Compensation practices combined with previous FDIC statements provide an ample basis to conclude that the FDIC's proposal is a problematic overreach by a regulatory agency.

While the FDIC professes that the proposed regulation would be separate and complementary to the current initiatives of prudential regulators, the inevitable negative outcomes caused by this proposal are easily foreseen.

The underlying premise of this proposal is that in a minority of institutional failures (37%), poorly designed compensation systems were a contributing factor and therefore must be addressed by manipulating FDIC assessments to force "voluntary" compliance with a "criteria" developed by the FDIC. In previous announcements during 2009, the FDIC stated that the majority of failures were caused by rapid growth funded by non-relationship brokered deposits. In this proposal, 63% of failures were caused by some factor other than poorly designed compensation plans. One could question why the FDIC deems it necessary and prudent to assume a greater responsibility for oversight of compensation plans than the current prudential regulators such as the Federal Reserve.

Further, previous statements by the FDIC prior to the current economic crisis, clearly implied that community banks are reaching the tipping point where the burden of regulation impedes the success of that business model. This proposed regulation will overwhelmingly and unfairly impact community banks, including both privately held and publicly traded institutions.

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Another concern is the claim that the FDIC and the stockholders are similarly situated as stakeholders in the Bank. The stockholders have the ultimate risk of losing their entire investment. That risk is controlled by attracting and retaining competent management to conduct operations and independent directors to conduct prudent oversight.

In its Request for Comments section, the FDIC asks for comments on many aspects of the proposal. Rather than specifically arguing for or against each element, my focus is on the effect on the survival of the banking system as a whole, particularly community banking. Especially impacted by this proposed regulation are CAMELS, an acronym for the safety and soundness rating system used by the prudential regulators for rating specific components of an institution (Capital, Assets, Management and Earnings). To attract sufficient capital, the "C" in the rating, an institution must provide returns to the shareholder equal to or better than another economically similar opportunity. To produce earnings, the E in the rating, at levels sufficient to attract and retain capital, competent management must be attracted and retained; the "M" in the rating. Lastly, earning assets, the "A" in the rating, must be sufficient to produce stable revenue streams.

The proposed regulation affects each of the regulatory components and interferes with the relationship between management and stockholders. It usurps the fiduciary obligation of corporate governance and imposes a benchmark criteria developed by a federal agency that is not the institution's primary regulator. In many cases, well run institutions have little day-to-day contact with the FDIC if the FDIC is not the institution's primary regulator. It is also the imposition of a "top down" regulatory approach rather than market driven criteria. This will lead to a "race to the bottom" for the efficacy of management in affected institutions and will destabilize the risk/reward calculus of private sector capital markets that attract and retain adequate capital.

My overriding concern about the effect of the proposed regulation is that while the FDIC may gain some comfort in its effort to eliminate rather than manage risk, we must consider how the non-regulated "shadow banking" institutions and lightly regulated, tax payer subsidized credit unions will be better able to attract and retain the Capital, Earnings, Assets and Management than community banks. The proposed regulation is without parallel in our banking system and is especially damaging to community banks.

Specifically, the provisions in the compensation scheme, where restricted stock is the incentive vehicle of choice, force a one way bet by the recipient. After punitive taxes are paid in advance by the employee and the award is subjected to arbitrary claw back criteria, the restricted stock compensation is not really an effective incentive. Is there any empirical support for the premise that restricted stock is the most effective incentive compensation tool for thinly traded or privately held entities? What are the recipient's reasonable expectations of an ultimate conversion into cash? How will payment in this debased currency affect our ability to attract and retain effective management?

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The proposed regulation should be withdrawn in its entirety and adoption of the Federal Reserve or other prudential regulator's guidance should be the standard in this matter.

Thank you for the opportunity to comment on this critical matter. If you have questions or choose to discuss any of these comments in greater detail, please do not hesitate to contact me at 240.427.1030 or mikemid@cbtc.com.

Sincerely,

Michael L. Middleton

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