Anchor State Bank

JAMES R. ECKERT
PRESIDENT AND TRUST OFFICER

September 6, 2006

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

Attention: Comments

Re: Deposit Insurance Assessments and Federal Home Loan Bank Advances
RIN 3064-ADO9

Dear Mr. Feldman:

Anchor State Bank would like to comment in response to the Federal Deposit Insurance Corporation notice of proposed rulemaking and request for comment on deposit insurance assessments. Specifically, we write to address the Corporation's request for comment on whether Federal Home Loan Bank (FHLB) advances should be included in the definition of volatile liabilities and whether higher assessment rates should be charged to institutions that have significant amounts of secured liabilities.

We are a \$12MM to \$13MM bank situated in rural McLean County, Illinois. Although McLean County is considered a MSA, we are located about 30 miles from Bloomington/Normal, the population "capital" of the MSA.

We believe that FHLB advances should not be characterized as "volatile liabilities" for FHLB members. FHLB advances are secured extensions of credit to members with pre-defined, understood, and predictable terms. Unlike deposits, advance liabilities do not increase or decrease due to circumstances outside of the control of an FHLB member. Experience has shown that deposits may be lost due to disintermediation arising from a variety of factors: special, short-term promotions by larger institutions in our market area or the existence of higher returns to depositors on alternative investments.

While most larger institutions can look to the Wall Street capital markets for replacement liabilities, the capital markets are not typically long-term, stable providers of wholesale funds to the community banks that comprise the bulk of the membership of the Federal Home Loan Bank System. Specifically, major deposit brokers are not interested in funding deposits of less than \$1,000,000 or, if they do, assess additional fees or demand a higher rate than for \$1,000,000 blocks. A \$12MM-\$13MM institution, such as ours, seldom has need for that much liquidity at any one time, and certainly not in one particular maturity.

As established by Congress, the primary purpose of the FHLB System is to provide a source of liquidity for FHLB members. Throughout their history, the FHLB's have performed this mission successfully. The FHLB's are a stable, reliable source of funds for member institutions, and the availability of such credit has a predictable, beneficial effect on members' business plans. Given the value of such a stable source of finding, it is not surprising that more than 8,100 financial

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institutions are members of the FHLB System. It would be illogical to include FHLB advances in the definition of volatile liabilities given the stability of the FHLB's, the reliable availability of advances as a source of wholesale funding, and the beneficial and predictable effect of such finding on members' business plans.

Deposit insurance premiums should be based on an institution's actual risk profile, taking into account an institution's supervisory rating and capital ratios. Banks that are engaged in excessively risky activities should pay a higher premium, regardless of whether those activities are financed by insured deposits, FHLB advances, or alternative wholesale funding sources.

The continued availability of FHLB advances reduces the risk of failure of FDIC-insured institutions. Charging a higher deposit insurance premium to financial institutions that use advances could discourage borrowing from the FHLB's and lead to the unintended effect of increasing risks to FHLB members. Financial institutions frequently use FHLB advances for liquidity purposes and to manage interest-rate risk, as well as to fund loan growth. In many markets, the supply of deposit funds is inadequate to meet loan demand and prudent financial management needs. Curtailing the use of FHLB advances would force institutions to look to alternative, often more costly wholesale funding sources that are actually volatile, thereby reducing profitability and increasing liquidity risk.

While this bank does not necessarily agree with the "social engineering" inherent in the FHLB's Affordable Housing Program, the proposal would hurt consumers by increasing the cost of funding mortgage portfolios. Making FHLB advances more costly would likely result in a reduction of borrowing and thus income to the FHLB's. This, in turn, would reduce the funding available to the FHLBs' Affordable Housing Program and other community investment programs. In 2005, the FHLB's provided $280 million in grants for affordable housing across the nation.

Penalizing the use of advances through the imposition of insurance premiums also would conflict with the intent of Congress in establishing the FHLB's, in opening membership in FHLB's to commercial banks in FIRREA, and, more recently, in adopting the Gramm-Leach-Bliley Act, which expanded small banks' access to advances. The FHLBs' mission is to provide financial institutions with access to low-cost funding so they may adequately meet communities' credit needs to support homeownership and community development. Charging higher assessments to those banks utilizing advances would, in effect, use the regulatory process to restrict the FHLBs' mission as established and repeatedly reaffirmed by the Congress.

During the consideration of FDIC reform legislation in the past several years, Congressional Committees and principal sponsors of such legislation expressed specific concerns that the FDIC, in developing a risk-based insurance assessment proposal, not adversely affect advances. The Congressional intent has been expressed in both the House and Senate on a bi-partisan basis. Both the House Budget Committee report on reconciliation (November 7, 2005) and the House Financial Services Committee report on deposit insurance reform (April 29, 2005) contained such expressions of concern.

Finally, a regulatory and legal structure is already in place to ensure collaboration between the FDIC and the FHLB's. If an FDIC-insured institution is experiencing financial difficulties, the FDIC and the relevant FHLB are required by regulation to engage in a dialogue to ensure the institution has adequate liquidity while minimizing other risks, including losses to the FDIC.

The cooperative relationship between the FHLB's and member financial institutions has worked well for 74 years. FHLB advances serve as a critical source of credit for housing and community development purposes, support sound financial management practices, and allow member banks throughout the nation to remain competitive. FHLB membership has long been viewed as protection for deposit insurance funds because FHLB members have reliable access to liquidity. Penalizing financial institutions for their cooperative relationship with the FHLB's would unjustifiably limit their ability to offer competitive pricing, limit credit availability in the communities they serve, and limit the members' use of a valuable liquidity source.

We urge the FDIC not to include Federal Home Loan Bank advances in the definition of volatile liabilities or to impose a deposit insurance premium assessment on "secured liabilities."

Sincerely,

James R. Eckert
President and Trust Officer