Minutes

of

The Meeting of the Advisory Committee on Community Banking

of the

Federal Deposit Insurance Corporation

Held in the Board Room

Federal Deposit Insurance Corporation Building

Washington, D.C.

Open to Public Observation

January 28, 2010 - 8:30 A.M.

The meeting of the FDIC Advisory Committee on Community Banking ("Committee") was called to order by FDIC Chairman, Sheila C. Bair.

The members of the Committee present at the meeting were: R. Daniel Blanton, President and CEO, Southeastern Bank Financial Corporation and Georgia Bank & Trust Company of Augusta, Augusta, Georgia; Dorothy J. Bridges, President & CEO, City First Bank of D.C., Washington, D.C.; Charles G. Brown, III, Chairman and CEO, Insignia Bank, Sarasota, Florida; Deborah A. Cole, President and CEO, Citizens Savings Bank and Trust Company, Nashville, Tennessee; Craig M. Goodlock, Chairman and CEO, Farmers State Bank of Munith, Munith, Michigan; James H. Gray, Chairman, Beach Business Bank, Manhattan Beach, California; Jack E. Hopkins, President and CEO, CorTrust Bank, National Association, Sioux Falls, South Dakota; Timothy W. Koch, Professor and Chair, Finance Department, Moore School of Business, University of South Carolina, Columbia, South Carolina; John P. Lewis, President and CEO, Southern Arizona Community Bank, Tucson, Arizona; Jan A. Miller, President and CEO, Wainwright Bank & Trust Company, Boston, Massachusetts; Bruce A. Schriefer, President, Bankers' Bank of Kansas, National Association, Wichita, Kansas; Laurie Stewart, President and CEO, Sound Community Bank, Seattle, Washington; Ignacio Urrabazo, Jr., President, Commerce Bank, Laredo, Texas; and Matthew Williams, Chairman and

President, Gothenburg State Bank & Trust Company, Gothenburg, Nebraska. Committee Member Rebecca Romero Rainey, Chair and CEO, Centinel Bank, Taos, New Mexico, was absent from the meeting.

Members of the Federal Deposit Insurance Corporation ("Corporation" or "FDIC") Board of Directors present at the meeting were Sheila C. Bair, Chairman, Martin J. Gruenberg, Vice Chairman, and Thomas J. Curry, Director (Appointive).

Corporation staff who attended the meeting included Valerie J. Best, Richard A. Brown, Jason C. Cave, Kymberly K. Copa, Christine M. Davis, Patricia B. Devoti, Diane L. Ellis, Robert E. Feldman, George E. French, Steven D. Fritts, Tiffany K. Froman, Mitchell L. Glassman, Alice C. Goodman, Leneta G. Gregorie, Tray Halverson, William F. Harral, Michele A. Heller, Christopher L. Hencke, Greg Hernandez, Ellen W. Lazar, Alan W. Levy, Skip Miller, Tariq A. Mirza, Roberta K. McInerney, Kathy L. Moe, Arthur J. Murton, Christopher J. Newbury, Richard J. Osterman, Jr., Sally A. Rinaldi, Claude A. Rollin, Lisa K. Roy, Barbara A. Ryan, Jon T. Rymer, Christopher J. Spoth, John V. Thomas, Sandra L. Thompson, Jesse O. Villareal, Kelly N. Walsh, Cottrell L. Webster, James R. Wigand, and Katherine Wyatt.

William A. Rowe, III, Deputy Chief of Staff, Office of the Comptroller of the Currency; and Charlotte M. Bahin, Senior Counsel for Special Projects, Office of Thrift Supervision, were also present at the meeting.

Chairman Bair opened and presided at the meeting. After welcoming Committee members, she acknowledged the issues confronting community banks and underscored the Corporation's commitment to a thriving community banking sector and its support of important community banking functions, particularly in the area of small business lending. She then provided a brief overview of the meeting agenda and introduced Roberta K. McInerney, Deputy General Counsel, Consumer and Legislation Branch, FDIC Legal Division, as the overall meeting moderator, and Sandra L. Thompson, Director, FDIC Division of Supervision and Consumer Protection ("DSC"), and Steven D. Fritts, Associate Director, Risk Management Policy Branch, Policy, DSC, as moderators of the first panel discussion on "Community Banks as Growth Engines: Raising Capital and Increasing Lending in the Current Environment."

At Ms. McInerney's request, Committee members introduced themselves and briefly discussed the history and characteristics of their respective institutions and, in some cases, the communities in which they operate.

Initiating the panel discussion, Ms. Thompson noted that regulators had recently been encouraging banks to raise their capital levels and expressed an interest in hearing Committee members' comments on any challenges they face in that regard. First, however, she requested that Mr. Fritts offer his general observations on the issue from a regulatory point of view.

Mr. Fritts noted that, at the Committee's meeting on October 15, 2009, there had been a great deal of discussion on bank capital levels and supervisory examinations; that the discussion had been helpful in development of the *Policy Statement on Prudent Commercial Real Estate Loan Workouts* issued by the banking agencies on October 30, 2009; and that, subsequent to issuance of the policy statement, Corporation staff had hosted separate conference calls with bankers and examiners to explain and answer questions on the guidance. He then acknowledged the somewhat circular dynamics underlying the need for banks to work through existing credit problems, extend new credit, raise profitability, and increase capital, but noted that Chairman Bair and FDIC staff have engaged in discussions with officials of the U.S. Department of the Treasury regarding the impact of such issues on community banks and, more specifically, regarding the importance of having easily understandable and attainable qualifications and requirements for any Troubled Asset Relief Program ("TARP") assistance to help community banks lend to small businesses.

Then, in response to a question by Ms. Thompson as to how the program to help community banks lend to small businesses could best be designed to encourage participation, Committee Members Cole, Blanton, Urrabazo, and Grey suggested renaming the program to avoid the negative public perception associated with TARP; Committee Members Miller and Urrabazo suggested attractive pricing, with Mr. Urrabazo elaborating on the possibilities of a tiered pricing structure or pricing discounts based on the percentage of increase in loans to small businesses; and Committee Member Bridges suggested more flexible qualifications criteria to expand program access to community development financial institutions and community bank involvement in the establishment of program parameters. In addition, Committee Members Blanton, Goodlock, and Miller suggested not tying the program to loan growth or volume because they believe that doing so would incent the wrong behavior in the current economy, with Mr. Miller noting that there is a natural decline in loan demand during a recession; Mr. Grey suggested allowing TARP I participants to convert to the new program; and Committee Member Schriefer suggested that the program not be limited to CAMELS "1"- and "2"-rated banks, but include lower-rated institutions that simply need a credit cushion to survive until the economy recovers. Committee Member Brown noted that it was the larger banks and not community banks that had cut back on lending and that, in recognition of that fact, any program tied to an increase in lending should not just look at any increase going forward, but should also look back one year. Finally, Ms. Cole introduced her idea for a simple capital investment program that would include availability of funds for a set period of time, perhaps five years, with an option for renewal; and a tiered interest rate structure, with the rate for individual banks dependent upon their examination ratings and their ability to raise additional funds.

Chairman Bair, noting that there had been some industry objection to a recent proposal for reallocation of a portion of unused TARP funds to create a small business loan fund with a loss-sharing feature, then asked whether the effort to provide support for new lending should take the form of a capital investment program. Mr. Brown responded that an injection of funds directly into a bank's loan loss reserves would be much more attractive than a loan guarantee because the former approach would have a positive effect on earnings, whereas in the latter approach, there exists the possibility that the guarantee may not be honored if certain conditions are determined not to have been met. Agreeing that an infusion of capital into loan loss reserves is a good concept, Mr. Blanton nevertheless observed that the attractiveness of the idea would depend on how the program is structured. Mr. Goodlock also agreed, noting that an injection of capital into loan loss reserves was consistent with the need to shore up balance sheets. Although acknowledging a need for growth in small business lending, Ms. Bridges indicated that such growth should be the secondary goal for reallocation of unused TARP funds and that bringing bank balance sheets back to a healthy condition should be the primary goal. Mr. Brown suggested that any program aimed at community banks should provide the option to shore up capital or increase loans to small businesses, depending upon the needs of the individual bank.

Indicating that TARP was originally designed to generate real economic activity through extension of credit, Chairman

Bair expressed support for tapping unused TARP funds to spur new lending.

There followed a brief discussion of the December 6, 2006, interagency *Guidance on Concentrations in Commercial Real Estate Lending* ("CRE Guidance") and the manner in which it was being applied during supervisory examinations. Mr. Brown indicated that there seemed to be confusion among examiners as to whether the concentration criteria set forth in the CRE Guidance should be viewed as guidelines or applied as a fixed ceiling. He noted, in particular, the anomaly that occurs when banks attempt to diversify out of CRE concentrations by getting rid of their "2"- and "3"-rated loans, leaving them with a higher ratio of lower-rated credits yet able to pass the CRE concentration test. In response, Ms. Thompson advised that although common characteristics among banks that failed in 2009 included rapid growth, a high concentration of CRE loans, and volatile funding structures, examiners are nevertheless encouraged to adopt a balanced approach and use sound judgment when evaluating banks' lending portfolios, with the aim of facilitating good lending rather than restricting it. Mr. Fritts reiterated that examiners review the underlying credit characteristics of a bank's loan portfolio, focusing more on credit quality rather than credit concentration

Returning to Ms. Thompson's original question on challenges faced by community banks in raising capital, Committee members offered a number of observations. Mr. Brown observed that not only are banks experiencing problems with raising capital, but also with the erosion of capital resulting from troubled debt restructuring. Messrs. Urrabazo and Miller observed that regulatory compliance costs represent a huge drain on capital and earnings, with Mr. Urrabazo noting that the current lack of loan demand compounds the problem. Mr. Miller further pointed out that the increase in deposit insurance assessments was also taking capital out of the banking system. Committee Member Hopkins made two observations: first, that banks are being forced to shrink their balance sheets which, in some cases, can only be accomplished by getting rid of performing loans, a process that lowers the capital of banks acquiring the loans; and second, that existing shareholders are reluctant to invest more capital for fear that their investments will only lessen the loss to the Bank Insurance Fund in the event of the bank's failure. Offering additional thoughts, Ms. Cole suggested that, although private investment funds are available, there may be reluctance on the part of some to accept funds that will result in a dilution of ownership and control; Mr. Brown suggested that, while there may be investment funds available, it may not be on favorable economic terms; and Mr. Goodlock suggested that bank regulators give some thought to revisiting the makeup of Tier 1 and Tier 2 capital.

The discussion then turned to the public relations impact of bank failures, with Ms. Cole and Committee Member Williams suggesting that many bankers believe the intent of the FDIC is to decrease the number of banks. Chairman Bair refuted those statements, indicating that she was at a loss regarding the source of the belief and noting that, to the contrary, the Corporation has been a strong advocate for the role of community banks in the U.S. banking system. Further emphasizing her support of the community banking sector, she expressed concern that bailout polices will have the effect of increasing consolidation because, thus far, the policies had been skewed in favor of larger institutions. Vice Chairman Gruenberg echoed Chairman Bair's comments, stating that in his opinion there have been no more vigorous advocates for community banks than the FDIC or Chairman Bair. He noted, however, that it would be in no one's best interest for the Corporation not to carry out its statutory responsibilities with regard to the resolution of failed banks.

In closing, Chairman Bair advised that guidance on small business lending would soon be issued and, it is hoped, would include a prescription for banks, particularly larger institutions, to abandon mathematical formulas and historical loss rates in favor of returning to standard banking practices of getting to know their customers and employing basic loan underwriting criteria.

Mr. Urrabazo then briefly commented on pending legislation regarding overdraft fees and the negative repercussions it could have on profitability. Chairman Bair suggested that the topic be revisited during the open discussion later in the day.

Ms. McInerney then called then for a short recess. Accordingly, at 10:02 a.m., the meeting stood in recess.

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The meeting reconvened at 10:20 a.m. that same day, whereupon Christopher J. Spoth, Senior Deputy Director, Supervisory Examinations, DSC, and Kathy L. Moe, Field Office Supervisor, San Francisco Region, DSC, opened the second panel discussion on "hot button" examination issues including interest rate risk, brokered deposits, and CRE Guidance. Mr. Spoth, in his introductory remarks, noted that supervisory interests closely align with the interests of bankers with respect to encouraging safe and sound banking practices and avoiding the market disruptions that result from unduly risky behavior. He reported on several of the strategies employed by DSC to keep the lines of communication open between DSC management and examiners in the field, including National Field Supervisors' Conferences, the next one of which would occur in February 2010, to present the opportunity for dialogue between DSC management, field supervisors, bankers, and trade association representatives, and periodic meetings between the Field Supervisors' Council and DSC management for purposes of keeping abreast of issues arising in the field. Then, in her introductory remarks, Ms. Moe noted that she and her field staff have been dealing with many of the issues raised by Committee members at the December 15, 2009, meeting, including the challenges of raising capital; the classification of assets, particularly those related to real estate; and the appropriateness of allowance for loan and lease losses ("ALLL") methodologies and documentation.

Mr. Brown then indicated that, based on his own experiences and those shared by other bankers in his area, an issue had arisen regarding the reasonableness test for validating ALLL methodology. He reported that he and other bankers had been required by examiners to increase their reserves and expressed concern that, without bank access to the models being used by examiners, the same problem would arise in future supervisory examinations. In response, Ms. Moe advised that rather than using a standard model or a bright line test, examiners rely on the model used by the bank, the model's underlying assumptions, the extent to which the bank has validated the reasonableness of its ALLL methodology, and, in some cases, their own judgment. In addition, both Ms. Moe and Mr. Fritts stated that, although it is not directly related to the reasonableness test, examiners are asked to look more closely at situations in which an institution's reserves are not keeping pace with its level of non-performing loans, particularly when the institution is close to capital thresholds. Mr. Brown suggested nevertheless that it would be helpful if the Corporation would issue a white paper, with examples, for bankers to use as a guide, and Mr. Hopkins, seemingly in agreement, observed that bankers were becoming fearful of making loans because of a lack of understanding of the factors on which examiners base their judgments. Mr. Blanton, however, disagreed on the need for a white paper, expressing a preference for examiner latitude to make judgments on the effectiveness of a bank's methodology. Mr. Fritts stated that he would take the suggestion for a white paper under advisement.

Mr. Brown then turned the discussion to Financial Accounting Standards Board ("FASB") Statement No. 114, *Accounting by Creditors for Impairment of a Loan*, reporting some confusion among bankers as to when an impaired loan is subject to specific reserve and when it is subject to write-down. He then suggested that it would be helpful if the Corporation could offer more guidance in that regard. Mr. Blanton then inquired about the FDIC's position on excess reserves, in response to which Chairman Bair advised that examiners are required to follow FASB's generally accepted accounting principles in that regard, but noted that all of the bank regulators have urged FASB to provide more flexibility for banks because of the pro-cyclical impact of existing rules.

The discussion then turned to funding sources, possible extension of the Transaction Account Guarantee ("TAG") Program, interest rate risk, reclassification of troubled debt restructuring ("TDR"), and business plans. With respect to funding sources, Ms. Bridges and Mr. Blanton observed that reciprocal Certificate of Deposit Account Registry Service ("CDARS") deposits in many instances are core deposits and, therefore, should be distinguished from traditional brokered deposits. In response, Ms. Moe and Mr. Spoth indicated that examiners are under instructions to look at the underlying relationships and franchise value of reciprocal CDARS deposits to determine whether they are, in fact, core deposits. However, Mr. Brown suggested that, because some reciprocal CDARS are not core deposits, it might be appropriate for the bank regulators to consider amending the Consolidated Report of Condition and Income Report definition of brokered deposits to reflect the distinction. Chairman Bair and several Committee Members then discussed the effect of brokered deposits on deposit insurance premiums and liquidity, with both Mr. Blanton and Mr. Goodlock making the point that, for purposes of calculating dependency ratios, raising the reporting threshold for brokered deposits and Federal Home Loan Bank advances to the current deposit insurance limit of $250,000 would significantly reduce the ratio, particularly if the calculation also recognizes the extent to which the deposits are core deposits. Finally, Mr. Schriefer observed that, currently, thrifts can use Federal Home Loan Banks to issue letters of credit to secure deposits whereas banks cannot and inquired whether any consideration was being given to changing the rule to provide additional funding opportunities for banks. Mr. Spoth answered that the issue had been raised at the staff level but has yet to be developed into a proposal for consideration by the Board of Directors.

With respect to TAG Program, Committee members were in general agreement that the program has had a positive impact on the stability of deposit accounts and suggested that the Corporation give consideration to extending the program beyond the June 30, 2010, termination date. Chairman Bair replied that staff was continuing to analyze market conditions and the volatility of deposits and expressed an interest in hearing the perspectives of Committee members, perhaps at the next Committee meeting, on the potential ramifications of allowing the program to terminate as scheduled.

On the issue of interest rate risk, Mr. Miller observed that while brokered deposits and Federal Home Loan Bank advances can be effectively used to minimize interest rate risk, they result in a deposit insurance assessment penalty and are subject to being viewed by examiners as an inappropriate funding source. In addition, Professor Koch, while complimentary of the January 6, 2010, *Advisory On Interest Rate Risk Managemen*t jointly issued by the FDIC and other financial institution regulators, expressed concern that, although many of the models used by community bankers can effectively capture interest rate, they do not adequately capture the credit risk that accompanies a rising rate environment. He also asked, after noting the expectation of rising interest rates and the difficulty of changing balance sheets to adjust for interest rate risk in the short term, for staff's reaction to interest rate swaps and the purchase of interest rate caps. In response, Chairman Bair and Mr. Spoth expressed general support of community banks taking advantage of hedging opportunities; however, Ms. Moe advised that the level of internal bank expertise required to take advantage of hedging opportunities should be commensurate with the size of the institution and the complexity of its balance sheet and hedging products, even when outsourced. She further advised that use of hedging strategies should be supported by appropriate policies, controls, validation and back-testing. Committee Members Stewart and Hopkins then requested that staff address the issues facing less than well capitalized institutions that are constrained in establishing interest rates by the need to consider rates in the competitive environment, including the rates of institutions considered "too big to fail." Specifically, they indicated that the rates offered by branches of larger institutions, which can be quite numerous in some markets, must be factored in separately rather than counting as one institution, which Mr. Blanton noted arbitrarily drives down the interest rate. George E. French, Deputy Director, Policy, DSC, acknowledged the need to factor all branches in the competitive market into the equation, but indicated that the impact is only about 10 basis points.

Moving to the topic of reclassification of troubled debt restructurings, Mr. Goodlock requested clarification on the appropriate timing for troubled debts restructurings that returns to performing status. Ms. Moe, in answer, noted that the general rule of thumb is that reclassification is appropriate when there are six months of performance and financial analysis projects continued performance beyond the six month period. Mr. Miller pointed out that he believes the CRE Guidance is unclear because it states the TDR needs to be shown on four consecutive call reports and suggested that further clarification may be needed. Chairman Bair, agreeing that the question is raised frequently, stated that the issue should in fact be clarified.

Regarding business plans, Mr. Brown noted that there is developing folklore that the business plans of many *de novo* institutions are being disapproved because of high levels of CRE concentration. He underscored the difficulty of making reliable projections in the current environment and expressed concern that institutions would be penalized for failing to meet projected targets and that business plans may be used as leverage to revisit an institution's capital ratios and portfolio diversification. Mr. Spoth explained that there are a number of reasons a business plan may require changes, including growth in the balance sheet beyond expectations or within certain categories of loans and failure to meet projections; that the FDIC expects that there will be some variability between projections and actual performance, particularly with respect to projections beyond one year; and that business plan changes basically amount to a resetting of projections to reflect the economics of the area, with the FDIC ultimately wanting to determine whether an institution is taking more risk and whether that risk make sense. Ms. Moe added that the business plan needs to make sense and the bank must be performing in accordance with the plan.

Next, Ms. McInerney introduced Alice C. Goodman, Deputy Director, FDIC Office of Legislative Affairs, who provided the Committee with an update on legislative activity related to financial regulatory reform legislation, including the bill recently passed by the U.S. House of Representatives, H.R. 4173, *Wall Street Reform and Consumer Protection Act of 2009* ("House Bill"). Summarizing some of the highlights of the House Bill, she reported that, in many ways, it acknowledges the value of community banks; that it makes an effort at putting an end to the concept of "too big to fail" by establishing a resolution process for large, failing institutions that present a systemic risk; that it establishes a new, independent Consumer Financial Protection Agency ("CFPA"), with provisions for a community bank advocate within the agency; that the focus of the CFPA would be supervision and enforcement activities for non-bank financial service providers not currently subject to oversight, with primary federal regulators retaining supervision and enforcement authority for insured financial institutions with under $10 billion in assets; and that it would require the FDIC to base deposit insurance assessments on assets. In comparison, she reported that, currently, the Senate is divided on establishment of an independent consumer protection agency, with some Senators favoring a bureau under the proposed new regulator for federally-chartered institutions, some Senators favoring an autonomous agency with its own budget and rulemaking authority, and still other Senators favoring creation of a consumer protection bureau within the Department of Treasury or the Board of Governors of the Federal Reserve System. She then advised that the FDIC has continued to work with Congress on development of financial regulatory reform legislation and that its priorities in that regard are ensuring that the Financial Services Oversight Council that will identify and regulate large firms that represent a system risk to the financial system have sufficient independence and that the FDIC, as deposit insurer, plays a major role on the council, and that the systemic resolution authority is credible, timely, and be funded in advance.

In the discussion that followed, Committee members and staff touched on the merits of various aspects of financial regulatory reform legislation, including its impact on the issue of preemption, preferences and concerns regarding a new consumer protection agency, the use of assets as the base for calculating deposit insurance assessments, and funding for the systemic resolution authority. In response to a question from Committee Member Gray as to whether preemption had been addressed in the House Bill, Ms. McInerney advised that it would allow the regulator for federally-chartered institutions to preempt state law only on a case-by-case basis and only if it makes a determination that the law would prevent, significantly interfere with, or materially impair the ability of a national bank to engage in the business of banking, which she noted sets a higher bar than the current standard that allows preemption by regulation if state law would obstruct, impair, or condition the ability of a national bank to engage in an activity. She advised, moreover, that the House Bill would change the standard for court review of preemption actions, no longer giving deference to the regulator and requiring courts to more carefully assess the validity and thoroughness of such actions.

On the issue of the new consumer protection agency, Chairman Bair expressed concern with having the consumer protection agency placed within an entity that regulates only national banks and lacks a broader perspective. Mr. Williams, on the other hand, expressed concerns that the establishment of a consumer protection agency, regardless of where it is placed, would be detrimental to community banks because it would result in increased regulatory compliance costs. Mr. Hopkins's concerns were related to exclusions in the House Bill for the farm credit system and automobile dealers and the possibility that even more financial service providers would be excluded, leading to banks continuing to bear the onus of consumer protection regulations and uneven enforcement. Chairman Bair acknowledged the danger of political pushback during the legislative process by entities not currently subject to regulation and further erosion of coverage.

With respect to an asset-based approach to deposit insurance assessments, Mr. Williams opined that it would potentially shift the deposit insurance premium burden to community banks because larger banks have more flexibility to restructure their balance sheets. Chairman Bair, indicating that the FDIC was neutral on the issue, stated nonetheless that analysis conducted by the Corporation suggests that using assets as the basis for deposit insurance assessments would significantly reduce the premiums for smaller banks.

Finally, regarding funding for the systemic resolution authority, Chairman Bair emphasized that while the House Bill included a working capital fund that would be pre-funded through a tax on large bank, it was uncertain whether any bill ultimately approved by the Senate would provide for a pre-funding mechanism. She further emphasized that the working capital fund in the House Bill would not be used to guarantee any liabilities; it would merely provide the funds to establish a short-term bridge entity to facilitate the wind-down of large financial intermediaries and would not be comingled with the Deposit Insurance Fund.

Chairman Bair then called for a recess. Accordingly, at 12:00 p.m., the meeting stood in recess.

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The meeting reconvened at 1:30 p.m. that same day, whereupon Chairman Bair introduced Mitchell L. Glassman, Director, FDIC Division of Resolutions and Receiverships ("DRR"), and James R. Wigand, Deputy Director, Franchise and Asset Marketing Branch, DRR, who led the final discussion panel of the day on Clarifying the Bank Resolution Process. In his introductory remarks, Mr. Glassman noted that the FDIC has more than 75 years of experience in its dual roles as deposit insurer and receiver of failed institutions, but indicated that its receivership process has changed due changing statutory requirements and market conditions. He added that, from a global perspective, the FDIC is unique in controlling not only the assets, but also the liabilities of an institution at the time of failure, and emphasized that the FDIC does its best, through marketing and customer service, to ensure a successful reopening for each failed bank.

Mr. Wigand then outlined the typical resolution process, which he stated begins with revocation of the charter by the chartering authority, followed by the appointment of the FDIC as receiver and simultaneous coverage of insured deposits, either through conveyance of insured or all deposits, if its determined to be the least costly transaction, to an acquiring institution or through the process of a payout. He then advised that the FDIC, as receiver, will sell the whole bank, sell deposits and branches, liquidate assets, or sell asset pools.

Mr. Wigand next discussed in detail the various transaction structures utilized by the FDIC, identifying those structures as purchase and assumption transactions, which he advised could take the form of a clean bank transaction, a transaction involving put or call options, a transaction involving optional loan pools, a whole bank transaction or modified whole bank transaction, or a loss-share transaction or modified whole bank transaction with loss-share; insured deposit transfers; straight deposit payoffs; bridge banks; and open bank assistance transactions. He explained the basic features of each type of transaction, the circumstances in which they are likely to be utilized, and, in some instances, their respective pros and cons

Reporting on 2009 bank resolutions, Mr. Wigand advised that 86 percent of bank resolutions in 2009 were all deposit whole bank transactions with a loss-share agreement, six percent were all deposit clean purchase and assumption-type transactions, four percent were some form of payout, and one percent were all deposit whole bank transactions. He further advised that the weighted average cost to the FDIC for the 2009 transactions was 21 percent of failed bank assets, as compared to a weighted average cost for the last cycle (1980-1994) of 21.4 percent. Mr. Wigand noted that media reports that recent costs compare unfavorably with bank resolution costs during the last cycle do not take into account that the FDIC is now resolving thrifts, not just banks, and thrift resolution is more expensive.

Mr. Wigand then discussed what he termed "works in progress," noting that, in 2010, the FDIC is working with regulators to cluster failing banks so that they resolve concurrently, giving bidders the option to bid on any combination of the failing banks, with the hope of bringing more bidders into the process; working with chartering authorities to allow more time to market failing institutions from 45 days to 60 days, with the aim of providing more time—*e.g.*, a minimum of 10 days—for potential acquirers to perform due diligence; and working to incorporate equity appreciation instruments and loss-share options into the resolution process. He explained that equity appreciation instruments, commonly referred to as warrants by the media, would allow the Corporation capture for publicly traded institutions some of the short-term gain in value associated with a transaction that is not quantifiable in advance or reflected in the bid because of uncertainty as to how the market will view the transaction. He further explained that loss-share options would provide the flexibility for bidders to elect loss-share protection on some loan pools and to decline it for others as well as identify different loss-share ratios for different pools.

Concluding his presentation, Mr. Wigand provided an overview on the creation of a limited liability company ("LLC"), explaining that the FDIC creates an LLC to which assets are transferred from the receivership; the receivership then has the equity and an IOU note, guaranteed by the FDIC in its corporate capacity; the equity is sold through competitive auction, resulting in the receivership having the note, cash, and equity certificate for LLC; and the guaranteed note is sold in private market, subsequent to which the receivership estate can distribute cash to creditors.

In the discussion that followed, Committee members asked a number of questions. Mr. Lewis inquired as to the amount of time allowed a publicly traded holding company under an order to raise additional capital, in response to which Ms. Thompson indicated that, by law, institutions subject to a prompt corrective action directive have 90 days to address their capital issues and Mr. Wigand responded that it really is dependent upon the circumstances of each case and that, in the absence of any statutory mandate, more leeway may be accorded to an institution that has good management, adequate operating income, and no significant operating losses.

Ms. Bridges questioned the treatment of securities owned by a failing institution and Mr. Wigand responded that, if the security is liquid, then it usually passes to the assuming institution, but that distressed assets are generally aggregated sold in a structured transaction.

Mr. Brown questioned the connection between the filing of professional liability lawsuits and the existence of directors and officers' liability insurance. Richard J. Osterman, Jr., Deputy General Counsel, Litigation and Resolutions Branch, FDIC Legal Division, provided an overview of claims against directors and officers and stated that amount sought is determined by damages theory in litigation. Mr. Osterman noted that Board approval is required and the business judgment rule is considered in the determination. Mr. Grey noted that it is increasingly difficult to get insurance because several insurance companies are leaving the market, and there is also fear that personal estates will get attacked. Mr. Glassman suggested a speaker series in Florida and Georgia to deal with certain misconceptions.

Mr. McInerney then opened the roundtable discussion. In response to a number of questions from Committee members, staff discussed, among other things, the DIF balance and the availability on the FDIC web site of FDIC Chief Financial Officer Reports for those wanting more in-depth information, the problem bank list, the appropriate accounting treatment for prepaid deposit insurance assessments, and the advance notice of proposed rulemaking ("ANPR") on *Incorporating Employee Compensation Criteria Into the Risk Assessment System*, issued by the FDIC on January 19, 2010. Mr. Williams expressed concern about a recent IRS ruling disallowing the deductibility of the 2010 prepayment of deposit insurance assessment, noting that it would be detrimental to some institutions. He also questioned whether there is pressure on field examiners to downgrade banks in an effort to increase the level of funds to the DIF. Chairman Bair responded that examiners follow a standardized exam process, guided by statutory requirements, and suggested it might be beneficial for the FDIC Office of Public Affairs an education campaign for members of the media to explain the supervisory process.

Mr. Lewis inquired whether the committee is serving the purpose that Chairman Bair envisioned. Chairman Bair affirmed that she feels the committee is serving its intended purpose and identified the TAG program and overdraft protection issues as possible topics for Committee's next meeting. Mr. Urrabazo and Mr. Miller also suggested consumer compliance issues and regulations as a possible topic for the next meeting.

Chairman Bair thanked the bankers for attending and suggested April 21, 2010, as a possible date for the next meeting.

There being no further business, the meeting was adjourned.

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
And Committee Management Officer
FDIC Advisory Committee on Community
Banking

Minutes

of

The Meeting of the FDIC Advisory Committee on Community Banking

of the

Federal Deposit Insurance Corporation

Held in the Board Room

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Washington, D.C.

Open to Public Observation

January 28, 2010 - 8:30 A.M.

I hereby certify that, to the best of my knowledge, the attached minutes are accurate and complete.

Sheila C Bair

Sheila C. Bair
Chairman
Board of Directors
Federal Deposit Insurance Corporation

and

Presiding Officer
January 28, 2010, Meeting of the
FDIC Advisory Committee on Community Banking

Dated: April 23, 2010