REGULATORY SOUP - Q & A

by Steve Brown

Today is Halloween, so we switched things up by dropping in a modified picture of a person in a soup costume. We know you were all getting sick our soup analogies, so we end the week by agreeing never to use the word "soup" again for the rest of the year in this publication. As the applause dies down, we move to answer the deluge of questions that have been sent to us over the past few weeks. You should also note that our meetings with regulators are continual, so if you have more questions in coming days, don't be shy about sending them in and we will try to get them answered as well.

Q) We received quite a few questions seeking clarification on the Transaction Account Guarantee where we commented that the program covered traditional demand deposit checking or savings accounts. A) What we failed to include is that those accounts must be non-interest bearing to be covered.

Q) Other readers asked where they could get more information on all of these programs in an effort to stay on top of things closer to real time. We suggest any regulatory agency, the Treasury ("UST"), ABA, ICBA and us of course. A) Many send out daily email updates, so information flows are nearly continual.

Q) What is the deal with the 3Y call structure on the capital? A) Preferred stock may be called prior to 3Ys by the bank if it is replaced with common or perpetual preferred capital. After 3Ys, you may pay it off with other capital issuance or out of earnings.

Q) Can de novo banks participate? A) We have seen nothing on this, but would expect the UST might consider it. We think this is a long-shot, but it will likely be based on credit, capital and earnings performance. Make your case to the primary regulator because their opinion counts the most. We would not expect the UST to invest in banks in formation, however.

Q) Is it likely that non-SEC reporting holding companies will likely be required to become reporting companies if they play? A) No, we have heard UST is working on this and a solution for both private and Sub S banks could come next week that will clarify.

Q) Are retail sweep programs (where monies are moved under a deposit reclass from non-interest bearing accounts to other non-interest bearing accounts) covered under the FDIC TLGP non-interest guarantee program? A) Yes, there was an exception included in the proposed interim rule that indicates noninterest bearing accounts that are swept would be covered. Note that some additional customer disclosures are now required.

Q) Are NOW and MMDA accounts covered under TLPG? A) Not right now, however bankers are encouraged to make comments to the FDIC so accounts held by sole proprietorships, non-profits, charitable organizations and deposits of public funds could be covered as long as the interest paid is small.

Q) How will Fed funds lines be affected if banks opt out? A) This is one of the thorniest issues still making the rounds. Banks are rightfully concerned that if they opt out they might see their FF lines get cut, while those who opt in are paying a very high fee at 75bp. We urge banks to comment on this to the FDIC, at the very least indicating the 75bp level is too high and a flat rate for all banks to pay as and when they borrow Fed funds is much more equitable.

Q) What CDs are guaranteed under TLGP? A) The only ones are interbank; meaning the lender and the issuer are both banks. Negotiable CDs are excluded, since even though they are issued by a bank, they can be purchased by any entity (not necessarily another bank).

Q) Has the UST put any restrictions on the use of TARP capital? A) There are none at this time that we know of (except not to take unnecessary risks as determined by the primary regulator).

Other quick thoughts: You must "opt-out" of TLGP, but must "opt-in" to TARP; at present once you opt out of TLGP you cannot come bank in later (but we understand this is being reviewed); you cannot opt out after the 30 day period; banks will be billed 75bp for any amount issued under the guarantee as they issue and will be charged via ACH at that time by the FDIC; the 5% dividend on the preferred shares is not tax deductible, so the effective cost is more like 8.50% (still inexpensive for a community bank); we expect large national banks will opt-out unless the 75bp drops down to something more like 25bp.

BANK NEWS

Writedowns

The FDIC issued a reminder that because of the EESA, banks can treat losses associated with the impairment of their auction rate, FN & FH preferreds for 3Q as an "ordinary" loss (instead of capital loss) in 3Q. In addition to the change to ordinary, the Act implied that banks should recognize the loss in 4Q, or after the Act went into effect. Recent clarifications allow banks to recognize both GAAP and tax losses in 3Q for regulatory purposes.

SBA Loan Volume

After a record 2007, SBA loan approvals dropped 30% by number and dollar totals dropped 13% this year. Average loan sized increased from $142k to $183k.