A FIREHOUSE OF REGULATORY UPDATES

by Steve Brown

A fire hose is so powerful, it can shoot water up to 100 feet straight up into the air. That is a good analogy to banking right now, given the sheer pressurized and consistent flow of regulatory rulings and guidance shooting out of the agencies these days. Since many community bankers have much to do, we provide below a synopsis of a few critical regulatory updates to be sure all community bankers remain informed.

Call Report Changes: There are multiple new reporting line items required for the 2Q Call Report. Items that most likely will impact community banks include: real estate construction and development loans with capitalized interest (banks with construction and development loan concentrations); holdings of commercial mortgage-backed securities and structured financial products; fair value measurements for assets and liabilities (banks $500mm or more in total assets); pledged loans; remaining maturities of unsecured other borrowings and subordinated notes and debentures; investments in real estate ventures; whether the bank is a trustee or custodian for certain types of accounts. Bankers can see drafts of the report forms and draft instructions for the new and revised Call Report items on the FFIEC Web site (www.ffiec.gov/ffiec_report_forms.htm).

Volatile Funding: The FDIC released this ruling in an effort to maintain bank franchise value and decrease the cost of resolution in the event of a failure. To do so, the FDIC is moving to slow down "aggressive" asset growth (not defined in the ruling) mostly for banks rated 3, 4 or 5 ("weakened banks") by limiting the use of "volatile" or "special funding sources" (although the ruling indicates even 1 & 2 rated banks with aggressive growth strategies or reliance on non-core funding could also see higher premiums). The ruling reminds directors and officers that they are responsible for operating in a safe and sound manner and that weakened banks should be taking immediate action to limit growth and improve their risk profile. Funding sources specifically mentioned in the ruling include volatile liabilities, funding guaranteed by the FDIC under a temporary program, high-cost brokered deposits, internet deposits, secured borrowing (FHLB) and other wholesale funding sources. The FDIC indicates weakened banks must also have a plan to stabilize or reduce their risk exposure and limit growth.

Modification of TLGP: This interim rule allows banks under TLGP to issue mandatory convertible debt (debt that automatically converts into stock at some date in the future) with prior FDIC approval. The purpose behind the change is to give banks flexibility to obtain funding from investors with longer-term investment horizons, while also reducing concentration of FDIC-guaranteed debt maturing in mid-2012. The debt must be senior unsecured, be newly issued on or after 2/27/09 and convert into common stock no later than 6/30/2012.

Interest Rate Restrictions: This proposed rule modifies brokered deposit interest rates by redefining the "national rate" as a simple average of deposit rates paid by US depository institutions. This eliminates the use of Treasury yields (well below deposit rates) in the definition. Under the proposal, banks would not be allowed (if less than well-capitalized) to pay a rate of interest significantly exceeding the prevailing rate in the institution's market area (or the area where the deposit is accepted). For brokered deposits, this would be calculated as 120% of the "national rate." The purpose behind unlinking the definition of "national rate" from Treasury yields allows the rate cap to be calculated to prevent payment of rates that significantly exceed prevailing market rates, but would allow depository institutions to pay prevailing "national rates."

The year is still young, but we'll keep watching for future regulatory updates so community bankers can stay up-to-date without having to learn how hang onto the fire hose.

BANK NEWS

FDIC

Has asked the Treasury to increase its line from $30B to $100B in order to reduce current assessments to banks.

Half The Slice

The FDIC plans to reduce the 20bp assessment on 2Q domestic deposits to 10bps, assuming Congress approves an increase in their borrowing line.

Merril Lynch

The beleaguered firm announced "trading irregularities" uncovered after the merger with BofA. The size is estimated to be above $120mm.

Credit Union Cap

A Bill was introduced yesterday that would lift the 12.5% cap on commercial loans for credit unions.

Hotel Lending Softness

A hotel research company projects full service hotels that won't have the cashflow needed to service their debt will jump 25% this year and property values will drop 20%. The company tracks more than 6k hotel financial statements and said about 16% of hotels could not generate enough cashflow from operations to service debt in 2008. They also projected the average hotel will see a 9.8% drop in revenue per available room.