

## Bank & Thrift - Industry News

### Extending banks' adolescence

*September 03, 2009 4:11 PM ET*

By Christina M. Mitchell

An FDIC policy change effectively extends adolescence for young banks, lengthening the period of increased regulatory supervision required for de novo institutions in a move that industry observers say will heighten the already considerable barriers to opening new banks.

The change, handed down in an FDIC letter dated Aug. 28, extends the de novo period to seven years, from three, meaning newly established banks now must comply with more frequent regulatory examinations and higher capital requirements through their seventh year of operation. Banks in this period also must seek FDIC approval before making any "material changes" to their business plans.

"You know, I think the big thing right now is, what is a material deviation from a business plan?" asked Donald Musso, president and CEO of FinPro Inc., a New Jersey-based financial institutions consulting firm. He described de novo clients' reactions to the change as a mix of frustration, confusion and apprehension, responses Musso told SNL would likely continue until the FDIC releases more detailed definitions and guidance related to the policy change.

The change means new regulatory requirements for two distinct types of existing institutions: New banks that have yet to complete their third year of operations, and those that are in their fourth through seventh operating years. Both groups will be subject to a 12-month examination schedule, as opposed to the less frequent schedule permissible for older institutions. In addition, banks that have yet to complete their third year of operations, and therefore are operating in accordance with their original business plans, must update their plans to cover operations through year seven.

"Those banks that are within zero to three years old, they suffer the brunt of this," said Dennis Wendte, one of the partners in charge of the financial institutions group at Chicago-based law firm Barack Ferrazzano Kirschbaum & Nagelberg LLP. "It's definitely changing the rules in the middle of the game."

The FDIC's letter does offer an explanation for the policy change, pointing to the many young institutions that have failed during 2008 and 2009. An SNL analysis found that of the institutions established since 2002, or those about seven years old and younger, 21 had failed as of the last closures Aug. 28, and 17 of those failures occurred in 2009. With 84 bank failures thus far this year, that means banks established since 2002 have accounted for roughly 1 in 5 of the failures in 2009. SNL's analysis excluded de novos

established under a pre-existing holding company, and the FDIC's new policy also generally excludes those established as subsidiaries of certain "existing 'eligible' holding companies."

<b>De novo bank failures</b>											
<b>Institutions established 2002 - present</b>											
<b>Company</b>	<b>Location</b>	<b>Date established</b>	<b>Age at failure (years)</b>	<b>Total assets (\$M)</b>	<b>Total deposits (\$M)</b>	<b>Total equity capital (\$000)</b>	<b>Risk-based capital ratio (%)</b>	<b>Tier 1 risk-based ratio (%)</b>	<b>Leverage ratio (%)</b>	<b>Adj NPA + adj loans 90PD/tang equity + LLR*</b>	<b>(%)</b>
Waterford Village Bank	Williamsville, NY	02/26/07	2.4	55.7	56.1	-685	-1.75	-1.75	-1.23		NM
Alpha Bank & Trust	Alpharetta, GA	05/08/06	2.5	354.1	344.2	5,286	2.92	1.59	1.38		382.04
MagnetBank	Salt Lake City, UT	09/29/05	3.3	300.7	282.6	15,895	6.76	5.50	4.84		385.21
American Southern Bank	Kennesaw, GA	08/30/05	3.7	106.0	105.9	-307	-0.47	-0.47	-0.37		1,115.19
Freedom Bank	Bradenton, FL	05/17/05	3.5	270.8	256.8	10,069	3.45	2.20	2.00		166.17
MetroPacific Bank	Irvine, CA	02/07/05	4.4	75.3	70.1	2,718	5.36	4.08	3.51		237.37
Citizens Community Bank	Ridgewood, NJ	10/28/04	4.5	40.7	40.7	-237	-2.09	-2.09	-1.43		1,367.13
First Coweta Bank	Newnan, GA	07/12/04	5.1	163.8	154.9	3,307	3.77	2.50	2.00		459.76
Integrity Bank	Jupiter, FL	07/12/04	5.1	105.3	98.5	-1,153	-1.79	-1.79	-1.26		28,090.67
Main Street Bank	Northville, MI	03/01/04	4.6	112.4	98.9	2,797	4.20	2.94	2.28		236.29
Freedom Bank of Georgia	Commerce, GA	02/17/04	5.1	172.5	159.0	4,620	4.72	3.44	2.73		233.53
First Priority Bank	Bradenton, FL	12/08/03	4.7	258.6	226.7	1,511	1.72	0.86	0.70		378.65
Community Bank of Arizona	Phoenix, AZ	11/25/03	5.7	158.5	143.8	13,572	15.77	14.49	8.62		185.72
Security Bank of North Fulton <sup>^</sup>	Alpharetta, GA	09/19/03	5.8	190.6	179.5	1,515	2.04	1.02	0.63		503.11
Millennium State Bank of Texas	Dallas, TX	08/20/03	5.9	118.6	115.5	742	1.81	0.90	0.61		187.98
Community Bk of West Georgia	Villa Rica, GA	03/25/03	6.3	201.2	189.4	7,303	5.89	4.61	3.58		429.82
Security Bk of Gwinnett County <sup>^</sup>	Suwanee, GA	02/24/03	6.4	259.2	256.6	-20,882	-10.68	-10.68	-7.19		NM
Pinnacle Bank of Oregon	Beaverton, OR	09/18/02	6.4	71.9	64.2	5,964	9.96	8.70	7.97		159.25
Mirae Bank	Los Angeles, CA	07/01/02	7.0	480.6	410.0	15,578	5.55	4.23	3.12		145.90
Security Bank of North Metro <sup>^</sup>	Woodstock, GA	05/20/02	7.2	184.2	182.4	-5,375	-3.60	-3.60	-2.75		845.15
FirstBank Financial Services	McDonough, GA	01/28/02	7.0	317.2	279.3	8,169	4.46	3.13	2.31		390.07

As of Sept. 2.  
List includes failed de novo institutions established after Jan. 1, 2002. Institutions established under a pre-existing holding company are excluded.  
Financial data reflects the values reported for the quarter prior to failure.  
<sup>^</sup>Purchased by Security Bank Corp. prior to failure. All six of Security Bank Corp.'s subsidiaries were closed by the FDIC on June 30.  
\*Nonperforming assets plus loans 90 days or more past due net of delinquent government guaranteed loans divided by tangible equity and reserves. Ratios less than zero are considered not meaningful.  
Source: SNL Financial

"Recent experience demonstrates that newly insured institutions pose an elevated risk to the Deposit Insurance Fund, particularly during an economic downturn," read the letter announcing the FDIC's extension of the de novo supervisory period.

Some de novo consultants, however, argued that the economic downturn played a larger role in the de novo failures than anything that the banks' management could control.

Many of the de novos that later suffered had filed business plans that focused on real estate lending from the beginning, and thus they were particularly vulnerable when the housing market suddenly deteriorated, said Byron Richardson, president of Atlanta-based Bank Resources Inc., a consulting firm. "I think the risk is the overall economic risk," Richardson told SNL. "What hurt these banks was that the real estate markets stopped, and thus the credit markets stopped ... we had an overheated real estate market, and no one recognized it."

Nine of the failed de novos were in Georgia, a center of the real estate bust.

Those banks that launched just as the real estate market was beginning to cool "couldn't have started at a worse time," Wendte told SNL. "The loans that were available to be made were real estate loans, and you were making them just like everybody else," he

said. "Unfortunately, you didn't have the same kind of cushion to withstand the blows when those real estate loans went bad that other, more established banks did."

Ultimately, the existing banks impacted by the FDIC's new supervisory policy will learn how to adapt, de novo consultants said, but the change also may help to dissuade any groups considering launching a new bank. De novo activity already is on track for the most sluggish year of openings since the early 1990s, with just 18 new banks opening their doors since Jan. 1, compared to 73 in the full year of 2008 and 146 in 2007, according to SNL data.

"It [the new supervisory policy] will certainly give more guidance to de novos that are starting out, but I think the hurdle has just been raised," said Wendell Brock, a principal at Texas-based consulting firm De Novo Strategy. He added that he expects no more than a dozen or so organizing groups per quarter to win new charter approvals for the foreseeable future.

Many would-be de novo organizers have turned away from the chartering process to seek out acquisitions, the consultants said, citing a lengthy charter processing period and more stringent regulatory requirements and added expense among the main causes.

"I think every day that goes by, it's getting harder and harder for de novos to form here in the U.S.," Musso told SNL. "There's no moratorium per se, but it certainly appears that through policy they're making it awfully difficult for de novos to form."