VEDDER PRICE®

A Complimentary Half-Day Conference Presented by the

Financial Institutions Group of Vedder Price

Friday, May 13, 2011

The Chicago Club
81 East Van Buren Street
Chicago, Illinois 60605

7:45 a.m. Registration and Continental Breakfast

8:30 a.m. – 11:45 a.m. Program

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Managing Your Bank in the New Normal

A Complimentary Half-Day Conference Presented by the

Financial Institutions Group of Vedder Price

Agenda		Tab
8:00 – 8:30 a.m.	Registration and Continental Breakfast	
8:30 – 8:35 a.m.	Introduction	
	✦ Robert J. Stucker, Chairman, Vedder Price P.C.	
8:35 a.m.	Mergers and Acquisitions/Capital Markets Update	
	✦ Daniel C. McKay, II, (Moderator) Financial Institutions Group, Vedder Price P.C.	
	✦ Jeffrey Brand, Managing Director, Keefe, Bruyette & Woods, Inc.	A
	✦ James Hemmer, Managing Director, Sandler O'Neill & Partners L.P.	B
	✦ Charles K. Smith, Principal, Sandler O'Neill & Partners L.P.	C
	✦ Daniel O'Rourke, Financial Institutions Group, Vedder Price P.C.	D
9:45 a.m.	Keynote Speaker: Ellen M. Costello, President and Chief Executive Officer, Harris Financial Corp.	
10:30 a.m.	Break	
10:45 a.m.	Dodd-Frank Update, Fair Lending/CRA, and Executive Compensation	
	✦ James M. Kane, Chair, Financial Institutions Group, Vedder Price P.C.	E
	✦ Jerry L. Miller, President, Regulatory Compliance Associates, Inc.	F
	✦ James W. Morrissey, Shareholder, Vedder Price P.C.	G
	✦ Philip L. Mowery, Executive Compensation, Vedder Price P.C.	H
11:45 a.m.	Adjourn	
	Speaker Profiles	I
	About Vedder Price	J

Discussion Materials for:

VEDDER PRICE®

May 13, 2011

Jeffrey A. Brand *Managing Director*

KBW KEEFE, BRUYETTE & WOODS

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Current Market Environment

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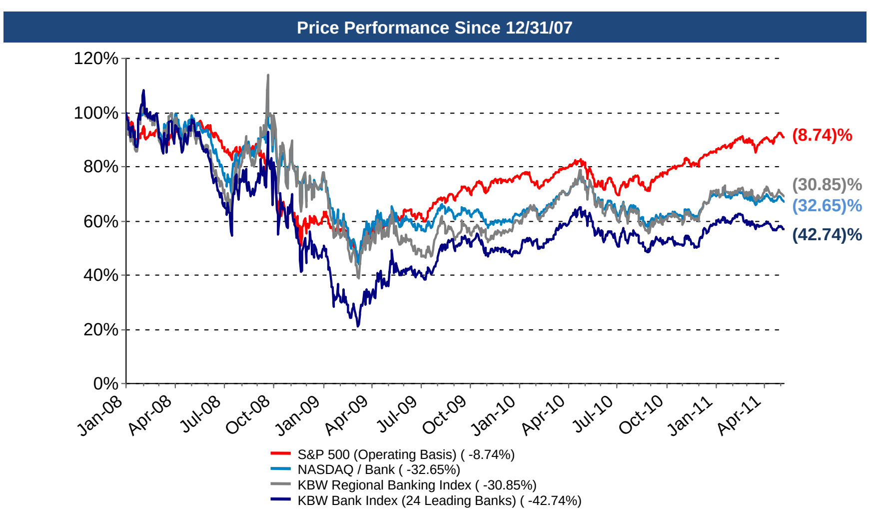
State of the Banking Industry

- The banking industry has experienced unprecedented changes
- The economic downturn has strained bank results
  - Elevated level of bank failures since 2007
- Banks are beginning to show signs of improvement
- Regulatory environment has permanently changed
  - Compliance costs are increasing
  - Revenue streams are being altered
  - Required capital levels are elevating
- The U.S. economy may have changed for the foreseeable future
  - Consumer deleveraging may mean more moderate growth

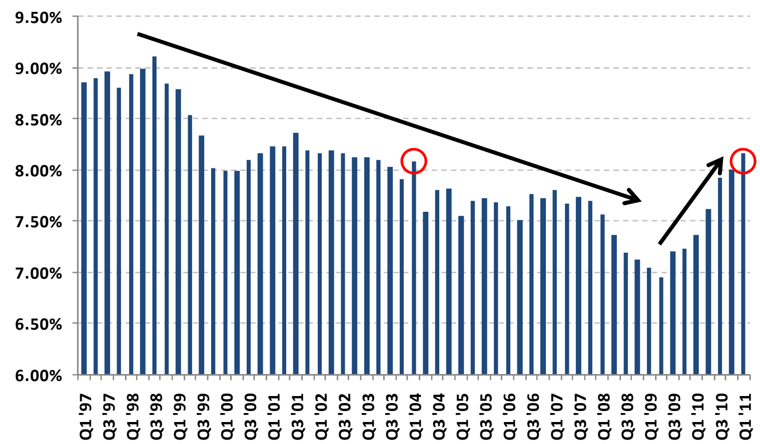
Bank Stocks: A Recovery of Sorts



Source: FactSet. Data as of 5/6/11
The KBW Bank Index is a composition of 24 money center banking institutions in the U.S. and is calculated using a market cap-weighted method
The KBW Regional Bank Index is a composition of 50 regionally diversified mid & small-cap banking institutions in the U.S. and is calculated using an equal-weighted method

Capital Levels Have Increased Significantly

Historical Median TCE/ TA Ratio for Major Exchange Traded Banks and Thrifts (%)



Source: SNL Financial
Includes all major exchange traded banks and thrifts as of 2011Q1 with reported financials as of 4/29/11

Why do Community Banks Need Capital?

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Overview of Capital Needs for Community Banks

- Increased regulatory requirements
- Problem assets remain elevated
- Repayment of TARP
- Offensive capital
- Asset sales

Basel III Capital Requirements

	Tier 1 Common %	Tier 1 Capital %	Total Capital %
Minimum	4.5%	6.0%	8.0%
Minimum Plus Conservation Buffer	7.0%	8.5%	10.5%
Minimum Plus Max. Countercyclical Buffer	9.5%	11.0%	13.0%

"We think 7% is plenty … My attitude would be we'd run the business at 7% or 8% Basel III"

(Jaime Dimon, 2011Q1 Earnings Call 4/13/11)

- **Capital conservation buffer (2.5%)**
  - Additional capital minimum; if breached, a bank would need to husband capital through restrictions on dividends, share repurchases and compensation
- **Countercyclical buffer (0% - 2.5%)**
  - Additional capital required if lending in the local market exceeds local market economic growth
- **Systemic risk buffer**
  - Additional capital required of the largest, systemically important banks

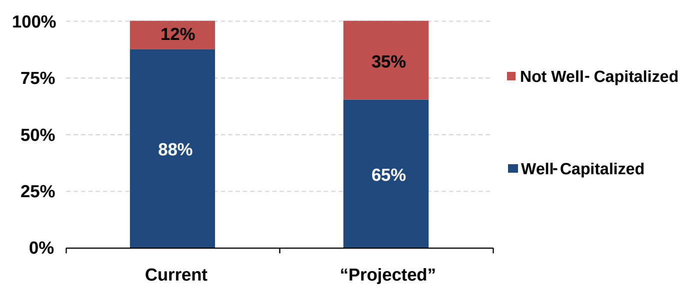
Note: It is currently unclear as to how U.S. regulators will later define "adequately capitalized" and "well capitalized"

Impact of Higher Regulatory Capital Requirements

Capital Requirements

	Current	"Projected"
Leverage Ratio	5%	8%
Tier 1 Ratio	6%	10%
Total Capital Ratio	10%	12%

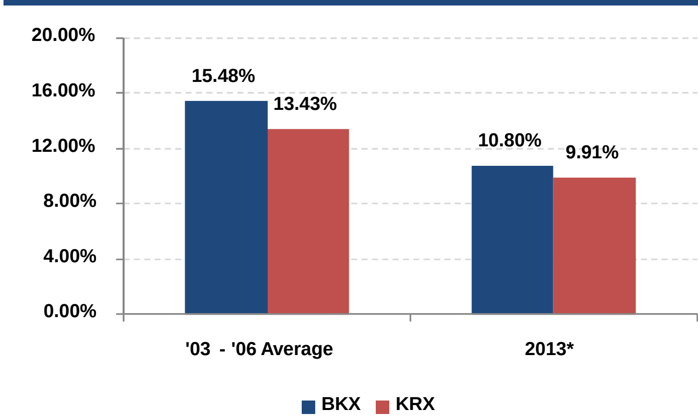
% of Bank Holding Companies "Well-Capitalized" (1)



Source: SNL Financial
Data as of most recent quarter available. Includes all BHCs greater than $100mm in assets
(1) Must meet or exceed all three capital ratio thresholds for inclusion in "well-capitalized" classification

Impact of Higher Regulatory Requirements

Median Industry ROAE



Source: SNL Financial
The BKX Index is a capitalization-weighted index composed of 24 geographically diverse stocks representing money center banks and leading regional institutions
The KRX Index is a composition of 50 regionally diversified mid & small-cap banking institutions in the U.S. and is calculated using an equal-weighted
* Median return on equity estimate of each index member as reported by FactSet using analyst estimates for the year 2013

Stressing the Nation's Banks

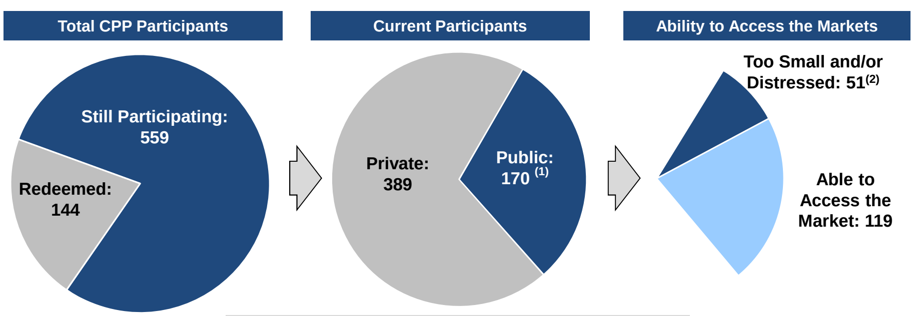
Loan Portfolio	12/31/07 Loans ($mm)	U.S. Treasury Base Case Loss Rate	Gov't. Base Case Loss ($mm)	U.S. Treas. Severe Case Loss Rate	Gov't. Severe Case Loss ($mm)
C&D	$473,865	8.00 %	($37,909)	18.00 %	($85,296)
CRE	889,232	5.00	(44,462)	12.00	(106,708)
Multifamily	133,387	3.50	(4,669)	11.00	(14,673)
Home Equity	700,020	6.00	(42,001)	11.00	(77,002)
First Mortgage	1,549,646	5.00	(77,482)	8.50	(131,720)
C&I	1,283,146	3.00	(38,494)	8.00	(102,652)
Leases	118,881	6.00	(7,133)	10.00	(11,888)
Credit Cards	383,024	12.00	(45,963)	20.00	(76,605)
Other Consumer	1,065,129	4.00	(42,605)	12.00	(127,815)
Other Loans	417,465	2.00	(8,349)	10.00	(41,747)
Total	**$7,008,907**	**4.98 %**	**($349,067)**	**11.07 %**	**($776,105)**
Cumulative Net Charge-offs (Since 12/31/07)			$472,739		$472,739
Total Remaining Cumulative Losses		**NM**	**NM**	**4.33 %**	**($303,366)**

- $303 billion of losses still imbedded in bank's loan portfolios
- Reserves of $265 billion represent 87% of remaining severe cases losses

Source: SNL Financial and U.S. Treasury
Data as of most recent quarter available
Includes all top-tier consolidated banks and thrifts

Industry Ability to Repay TARP

- The Treasury is very close to breaking even on the TARP CPP
  - Treasury invested $204.9 billion in 707 banking institutions and earned back $204.1 billion to date



The Treasury currently has outstanding CPP investments of approximately $23 billion

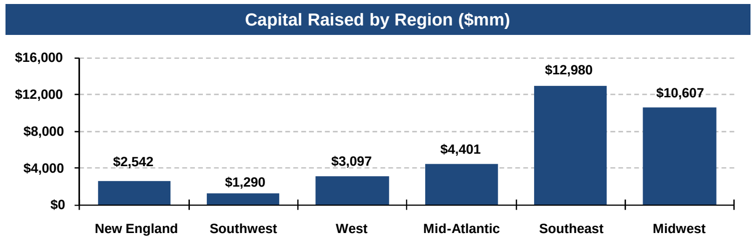
Top 3 Remaining Companies [3]

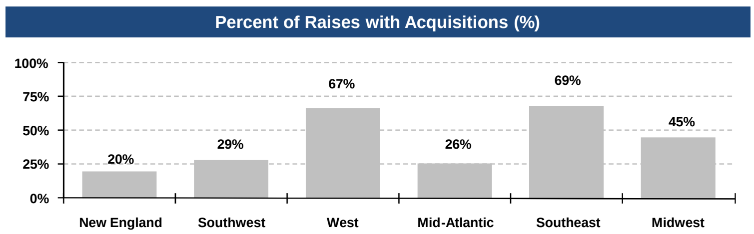
Regions Financial:	**$3,500mm**
Zions Bancorporation:	**$1,400mm**
Synovus Financial Corp:	**$968mm**

Source: CPP data per KBW Research (KBW TARP Tracker - 76th Edition published 4/4/2011) and SNL Financial
Note: Redeemed includes CDCI conversions; Treasury recognized losses on 4 institutions
(1) Includes major exchange traded banks
(2) Banks with less than $500 million in assets or Texas ratios greater than 100% are considered too small and/or distressed
(3) Excludes merger targets (Marshall & Ilsley Corp)

Capital is Needed by the "Consolidators"

- Nationwide, roughly 50% of all capital raises coincide with an acquisition
- 45% of Midwest institutions that have raised capital have completed an acquisition since 2008

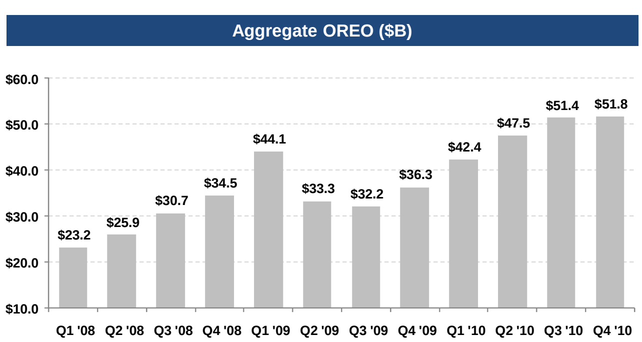




Source: SNL Financial
Capital raises include public follow-on offerings for banks and thrifts with a sub $20 billion pre-deal market cap from the US or Puerto Rico since 12/31/2008; excludes ATMs, PIPEs and 144A offerings
Acquisitions include whole bank and thrift and FDIC-Assisted transactions announced from 12/31/2008 to 4/27/11

Asset Sales

- The amount of assets in OREO continues to increase
- The market has placed an emphasis on cleaning up problem assets quickly, even in the face of weak real estate valuations in the near term
- More banks are considering asset sales despite significant losses
- Capital may need to be raised alongside asset sales



Source: SNL Financial
Data for all banks and thrifts headquartered in the United States

Case Study: UCBI Recapitalization and Asset Sale

Transaction Overview

- United Community Banks, Blairsville, GA; $8B in assets
- In March, UCBI completed a $380 million capital raise
- In April, UCBI sold $266 million in classified substandard and nonperforming loans
- Additionally, the company plans to sell $143 million of OREO
- UCBI recognized $227 million in pre-tax losses from the loan and property sales, a **52% loss**

Transaction Highlights

Investment ($000)	$380,000
Common Stock	32,943
Convertible Preferred	347,057
Investment Price per Share	$1.90
New Ownership	69.7 %
Price / Tang. Book (1)	39.9
Price / Adjusted Tang. Book (2)	61.3

Capital Impact

	12/31/10	Pro Forma NPA Sale	Pro Forma Capital Raise & NPA Sale (3)
Tang. Com. Equity / Assets	6.0 %	4.0 %	8.5 %
Leverage Ratio	6.7	3.8	8.6
Total Capital Ratio	12.1	8.3	15.8
Tangible Book Value	$4.76	$3.10	$2.27
NPAs / Assets	4.3%		1.1%

Source: SNL Financial and Company documents
Data as of or for the three months ending 12/31/10
(1) Based on UCBI's tangible book value per share of $4.76
(2) Based on UCBI's pro forma tangible book value per share of $3.10 resulting from the NPA sale
(3) Based on net proceeds from offering of $362.5 million, per UCBI

Access to Capital Markets and Capital Strategies

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Types of Capital: Benefits and Considerations

Senior Debt	▲	• Would provide liquidity without ownership dilution
	▲	• Straightforward execution, investment grade
	▼	• Would not count as Tier 1 capital at holding company
Straight Preferred	▲	• Simpler than a hybrid security
	▲	• No ownership dilution effect
	▼	• No tax deductibility of dividends
	▼	• Would not provide common equity credit although would provide Tier 1 credit
Hybrids / Converts	▲	• May provide a significant portion of common equity immediately compared to a straight preferred
	▼	• Significantly more complex structure
	▼	• May present execution challenges and smaller investor target group given the complexity & size
Common Equity	▲	• Execution in structuring, marketing and appealing to a wider investor base
	▲	• Offers greater clarity within the capital structure, especially in light of changing regulatory environment
	▲	• Would not be cash flow constrained like a fixed coupon on the hybrid / preferred dividend
	▼	• Ownership dilution

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Sources of Capital for Community Banks

	Benefits	Issues
Public Capital Raise	▲ Effective way to boost capital	▼ Success of capital raise subject to market conditions and investor sentiment
Private Equity Raise	▲ Private equity investors actively looking to deploy capital ▲ Often willing to absorb bad assets / recapitalize distressed banks	▼ Deep discounts ▼ Often have control / management issues ▼ Substantial dilution to current shareholders
Rights Offering	▲ Minimal ownership dilution to current shareholders	▼ Often steep discount ▼ Short term fix
SBLF	▲ Low-cost source of capital	▼ Government involvement ▼ Dividend will increase if small business lending does not increase

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Capital Issued

- Non-SCAP banks have raised $31.6B or 20% of common equity vs. $160.2B for the industry as a whole

Dollars in $mm	2007	2008	2009	2010	Total
Common Equity (SCAP Banks)	$0	$46,694	$77,747	$4,150	$128,591
Common Equity (Non-SCAP Banks)	276	6,313	14,913	10,151	$31,653
Preferred Raised (All Banks)	29,010	49,066	4,800	3,993	$86,869
Debt Raised (All Banks)	141,722	56,239	50,001	47,230	$295,192
Total	**$171,008**	**$158,312**	**$147,461**	**$65,524**	**$542,305**

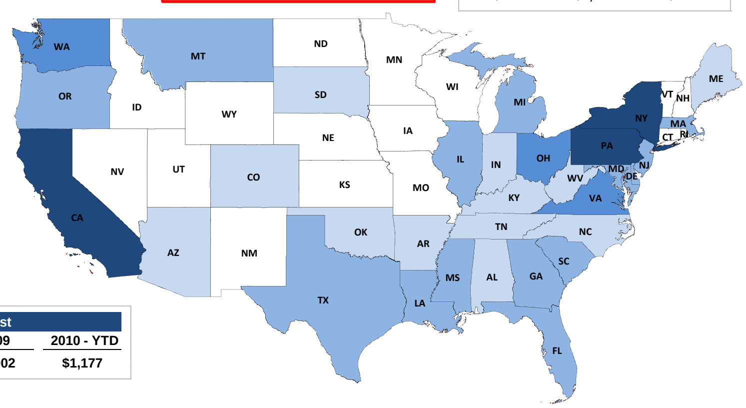
Source: Dealogic
Includes public equity follow-on, preferred equity, trust preferred, subordinated debt and senior debt raises by U.S. banks from 2006 – 2010

Community Bank Capital Raised

Midwest		
2008	2009	2010 - YTD
$155	$697	$388

Mid-Atlantic / New England		
2008	2009	2010 - YTD
$636	$1,541	$838

Capital Raises
- 0
- 1 - 2
- 3 - 5
- 6 - 10
- 10 - 20



West		
2008	2009	2010 - YTD
$119	$1,002	$1,177

Southwest		
2008	2009	2010 - YTD
$0	$275	$154

Southeast		
2008	2009	2010 - YTD
$117	$1,623	$1,063

Dollars in millions
Source: SNL Financial
Data as of 4/29/11
Includes all common stock offerings by bank and thrift institutions with assets less than $10.0 billion since 12/31/07; excludes PIPEs, rights offerings and capital raises under $1.0 million

Recent Bank Follow-On Trends and Results

- Offering discounts and valuations have generally improved in 2011 YTD

Pre-Deal Market Cap	2009 Median File / Offer Discount	2009 Median Price / PF TBV	2010 Median File / Offer Discount	2010 Median Price / PF TBV	2011 Median File / Offer Discount	2011 Median Price / PF TBV
Sub $200 million	(18.23)	0.97	(20.29)	0.79	(9.87)	0.83
$200 million - $1 billion	(10.15)	1.21	(6.59)	1.08	(4.03)	1.32
$1 billion - $5 billion	(6.87)	1.11	(5.90)	1.33	(2.96)	1.50
North of $5 billion	(8.50)	1.68	(2.90)	1.12	(4.18)	1.25

Source: KBW ECM. Includes public follow-on offerings since 12/31/08 for banks and thrifts from the US or Puerto Rico; excludes ATMs, PIPEs and 144A offerings

Issuer Characteristics By Market Cap

- Issuers in 2010-2011 had the following characteristics prior to launching a follow-on offering

Sub $200 million pre-deal market cap

Metric	Median Metric: Quarter Prior Offering	Median Metric: Quarter After Offering
Texas Ratio	31 %	24 %
TCE / TA	6.50	8.42
Total Capital Ratio	12.93	15.38

$200 million - $1 billion pre-deal market cap

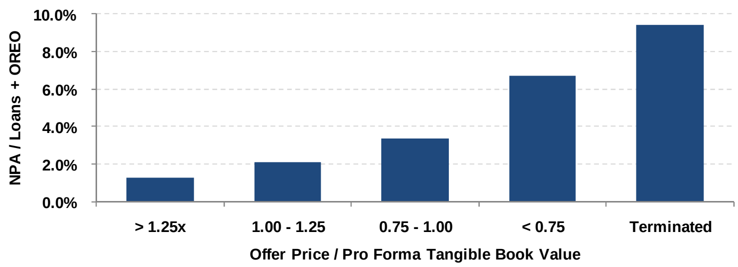
Metric	Median Metric: Quarter Prior Offering	Median Metric: Quarter After Offering
Texas Ratio	40 %	33 %
TCE / TA	6.71	8.38
Total Capital Ratio	14.36	16.48

Source: Source: KBW ECM and SNL Financial. Includes public follow-on offerings since 12/31/09 for banks and thrifts from the US or Puerto Rico; excludes ATMs, PIPEs and 144A offerings

Issuer Characteristics – Sub $200M Market Cap

- Asset quality issues drive costs of raising capital

Median NPA / Loan + OREO to Offer Price/ Pro Forma Tangible Book Value

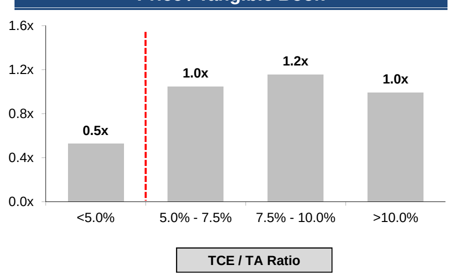


Offer Price / Pro Forma Tang. Book	NPAs / Loans + OREO	TCE / TA	MRQ ROAA	Shares Issued / Pre-Deal Shares Out	Discount to Filing Price
> 1.25x	1.30 %	6.0 %	0.72 %	34.7 %	(10.6) %
1.00 - 1.25	2.12	7.5	0.67	42.9	(9.4)
0.75 - 1.00	3.38	6.8	(0.16)	60.7	(22.7)
< 0.75	6.72	6.0	0.29	125.0	(36.8)
Terminated	9.39	5.4	(0.50)	--	--

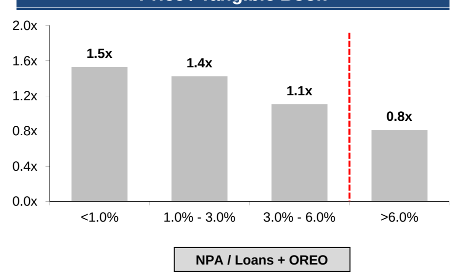
Source: SNL Financial
Offering data as of 4/29/11; financial data as of or for the most recent quarter prior to pricing
Includes public follow-on offerings since 12/31/08 for banks and thrifts with a sub $200 million pre-deal market cap. from the US or Puerto Rico; excludes ATMs, PIPEs and 144A offerings

Influence of Capital and Asset Quality on Valuation

Price / Tangible Book



Price / Tangible Book



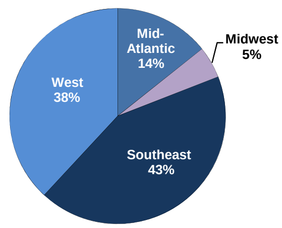
Source: SNL Financial and FactSet Research Systems
Note: Includes publically traded banks and thrifts on the NYSE, NASDAQ, NYSE Amex
Pricing as of 5/2/11

Private Equity Recapitalization Activity

Summary Statistics

	Median Metrics				
Companies (# of)	Legacy Ownership (%)	Total Assets ($M)	TCE / TA (%)	NPAs / Lns + REO (%)	Texas Ratio (%)
Distressed (16)	16	1,875	5.0	10.9	116
Less Distressed (5)	57	1,629	6.3	3.4	39

Percent of Total Deals by Region



Source: SNL Financial and Company documents
Data as of quarter prior to announcement. Includes announced private equity activity since 12/31/2008

Rights Offerings

Overview of Rights Offerings

- In a rights offering, the company's existing shareholders buy additional securities at a given price, usually at a discount
- Large shareholder, as well as the Board of Directors, often participate in order to fill a capital shortfall

Recent Community Bank Rights Offerings

- 79 community banks completed a subscription rights offering with a median raise of $17.25 million
- 24% of the community banks rights offerings were raised around an additional capital raise

Source: SNL Financial
Data as of 4/27/11
Includes all completed rights offerings for institutions with assets under $10.0 billion since 12/31/07

The Small Business Lending Fund

- On September 27, 2010, President Obama signed the Small Business Jobs and Credit Act, which established, among other things, a new $30 billion Small Business Lending Fund ("SBLF")

- Bank holding companies with assets under $10 billion are eligible for SBLF funding
  - Must have a CAMELS score of 1, 2, or 3

- Institutions can convert TARP funds into SBLF

- The Fund will provide community banks with incentives to increase small business lending
  - Dividend rate can be as low as 1% if small business lending increases by 10% or more

- More than 600 banks & thrifts have applied for over $6.5 billion in SBLF funding

Source: US Treasury

On the Horizon

- A shift from capital accumulation to capital deployment
  - Increased dividends
  - Share repurchases
  - Mergers and Acquisitions

- Focus on "normalized earnings"

- Balance sheet deleveraging

- Non-accruals continue to increase, although at a slower pace

- Failures expected to peak in the near future

- Opportunity to consolidate the "walking wounded"

KBW - The Historical / Current Bank Equity Capital Markets Leader

2004 – 2010 Bank Bookrunner League Table (All Deal Values)

Rank	Bookrunner	Deal Value ($mm)	No. Deals
1	**Keefe Bruyette & Woods**	**$6,422.1**	**63**
2	Sandler O'Neill & Partners	5,129.7	49
3	JPMorgan	37,872.7	30
4	Morgan Stanley	47,437.0	25
5	Goldman Sachs	48,799.2	22
6	Stifel Nicolaus Weisel	901.8	20
7	Bank of America Merrill Lynch	12,755.6	14
8	Barclays Capital	6,244.9	13
9	Raymond James	882.7	11
10	RBC Capital Markets	964.4	9

2010 Bank Bookrunner League Table (All Deal Values)

Rank	Bookrunner	Deal Value ($mm)	No. Deals
1	**Keefe Bruyette & Woods**	**$2,034.6**	**14**
2	JPMorgan	7,243.7	10
3	Sandler O'Neill & Partners	907.8	9
4	Morgan Stanley	18,048.4	8
5	Goldman Sachs	2,477.0	6
6	Stifel Nicolaus Weisel	248.5	5
7	RBC Capital Markets	621.5	4
8	Barclays Capital	612.6	4
9	Bank of America Merrill Lynch	787.2	4
10	Robert W Baird & Co	130.9	2

$21.2 Million Follow-On Offering Bookrunner March 2011	$73.5 Million Follow-On Offering Bookrunner March 2011	$46.0 Million Follow-On Offering Bookrunner March 2011	$51.2 Million Follow-On Offering Bookrunner December 2010	$57.6 Million Follow-On Offering Bookrunner December 2010	$23.3 Million Registered-Direct Placement Agent October 2010
$50.3 Million Follow-On Offering Bookrunner August 2010	$150.2 Million Follow-On Offering Bookrunner August 2010	$35.2 Million Follow-On Offering Bookrunner July 2010	$34.5 Million Follow-On Offering Bookrunner July 2010	$240.1 Million Follow-On Offering Bookrunner April 2010	$90.0 Million Follow-On Offering Bookrunner April 2010

Source: Dealogic
Notes: As of December 31, 2010. Search excludes best efforts offerings, PIPE offerings and ATMs. Includes SEC registered underwritten initial public offerings and follow-on offerings for bank issuers from the United States and Puerto Rico since 2004

VEDDER PRICE

Merger & Acquisition Market Update

Private and Confidential
May 2011

SANDLER O'NEILL + PARTNERS, L.P.
New York + Atlanta + Boston + Chicago + San Francisco
+ www.SandlerONeill.com

M&A Market Update

Key Themes

- The U.S. banking industry has finally stabilized . . .
  - Credit metrics seem to have peaked. A return to pre-crisis credit levels, however, could take many years
  - Approximately $176 billion in bank common equity capital has been raised publicly since early 2009
  - 320 banks have been closed during the same period – with more likely to come
- . . . but it remains fragile. Uncertainty prevails regarding:
  - Future capital requirements (e.g., the "new" Well Capitalized minimum level, Basel III)
  - Impact of proposed financial regulations
  - Return of loan demand and "core" profitability
- We expect the increased regulatory reform to significantly impact the industry
  - Rising compliance costs will disadvantage those without sufficient scale
  - 17 government agencies creating 500+ rules, 60 studies, and 93 Congressional reports
  - Increased capital requirements will reduce industry returns
- Weak organic growth and regulatory pressures should accelerate banking consolidation in the next 12-18 months

M&A Market Update

2011 & Beyond

- 2009 was the slowest year of M&A activity in more than 19 years; 2010 began at a similar pace
  - Traditional buyers remain internally focused on credit and cost structure and hesitate to increase credit risk through non-assisted transactions
  - Most acquisitions require incremental capital to consummate
  - There are far more sellers than buyers
- Beginning in mid-2010 there was an uptick in both the number of transactions and pricing
  - Certain buyers are feeling more and more comfortable with their own credit portfolio
  - FDIC transactions, particularly in the Mid-Atlantic and New England, have been limited
- Nevertheless, assisted deals should dominate through 2011
  - Many troubled institutions are trying to sell at fire-sale prices to avoid failing
  - Some buyers are only focused on assisted transactions at this time

Source: SNL Financial, FDIC

M&A Market Update

Closed Bank Transactions

- Bank failures have continued to accelerate; peak numbers to occur in 2010 or 2011
  - In 2008, 25 banks with $376.7 billion of total assets failed (WaMu and Indy Mac accounted for 91% of failed bank assets)
  - 140 failed banks in 2009 with assets of $173 billion
    - Highest number of failures since 1993 but far below the peak bank failure years of 1988 and 1989 when 464 and 533 banks and thrifts failed
  - 157 failed banks in 2010 with assets of $97 billion
  - 34 failed banks year to date in 2011 with assets of $14.9 billion

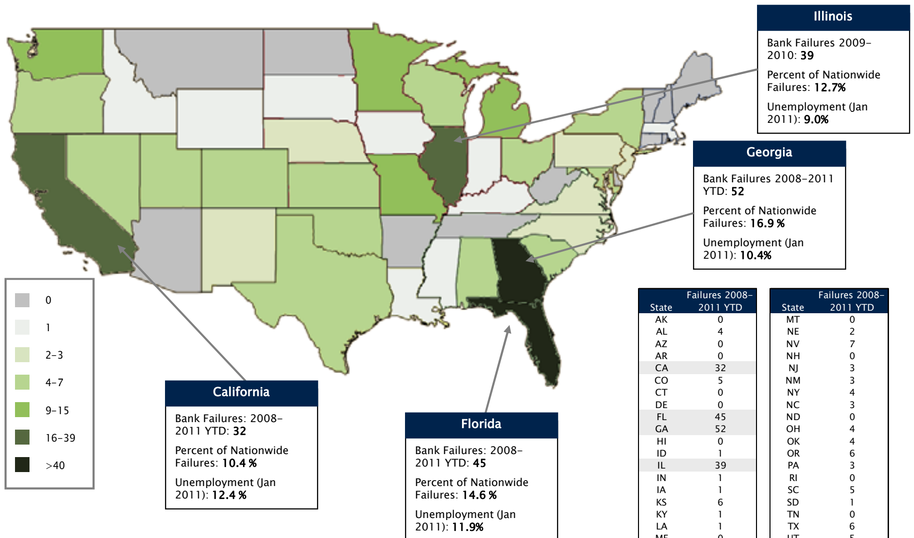
Banks on the FDIC's "Problem List"

	2008				2009				2010			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Number of Banks	90	117	171	252	305	416	552	702	775	829	860	886
Assets ($bn)	$26.3	$78.3	$115.6	$159.4	$220.0	$299.8	$345.9	$402.8	$431.0	$403.0	$379.0	$390.0
Number of Failed Banks	2	2	9	12	21	24	50	45	41	45	41	30

- Transactions have evolved from primarily deposit-only transactions with very low premiums in 2008 to whole bank transactions with loss sharing agreements with the FDIC
  - Loss share terms have been altered three times this year, most recently in September

M&A Market Update

Failed Banks Nationwide 2009-2011 YTD



State	Failures 2008-2011 YTD
AK	0
AL	4
AZ	0
AR	0
CA	32
CO	5
CT	0
DE	0
FL	45
GA	52
HI	0
ID	1
IL	39
IN	1
IA	1
KS	6
KY	1
LA	1
ME	0
MD	6
MA	1
MI	10
MN	14
MS	1
MO	9

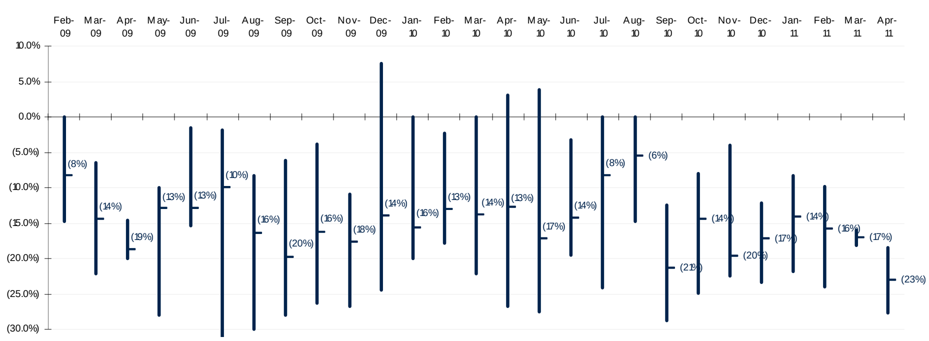
State	Failures 2008-2011 YTD
MT	0
NE	2
NV	7
NH	0
NJ	3
NM	3
NY	4
NC	3
ND	0
OH	4
OK	4
OR	6
PA	3
RI	0
SC	5
SD	1
TN	0
TX	6
UT	5
VT	0
VA	2
WA	14
WV	0
WI	6
WY	1

Source: FDIC

M&A Market Update

FDIC Assisted Transaction Pricing

U.S. Bank Failures: Bid Price/Loss Share Assets, by Month



- ❑ Asset discounts as a percentage of covered assets were declining before the FDIC's move to three tranche loss-sharing in September of 2010
- ❑ Some large transactions saw very aggressive bidding
  - ➢ TD Bank's three acquisitions in Florida each contained a 0% asset discount
  - ➢ Harris' acquisition of Amcore at a 3.7% asset discount
  - ➢ First Merit's acquisition of Midwest Bank & Trust was at a premium of 3.8%
  - ➢ Great Western's acquisition of Tier One had a 3.2% discount

M&A Market Update

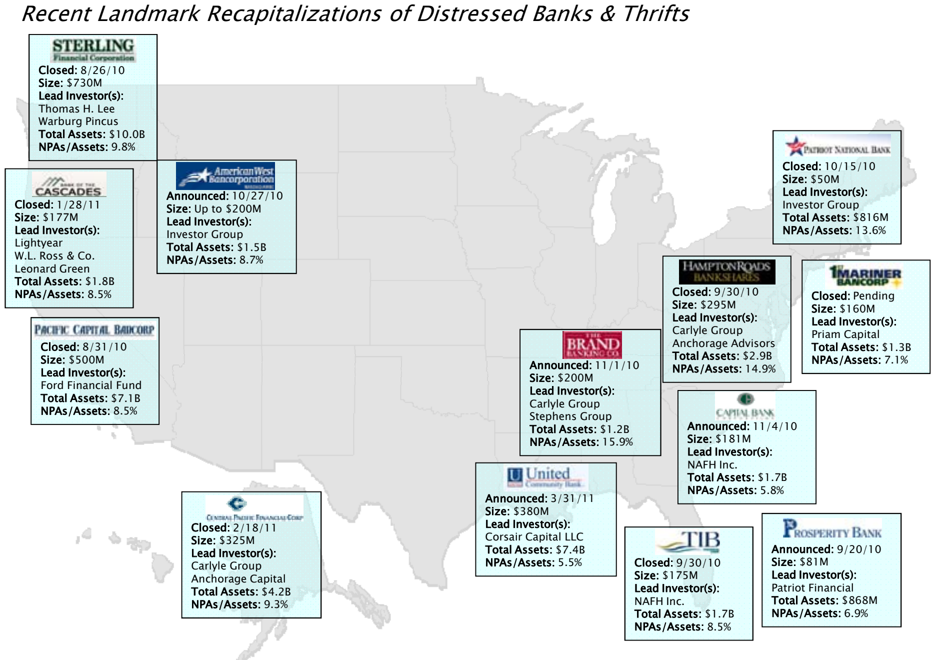
Benefits and Considerations of a Loss Share Transaction

Benefits	Considerations
❑ Loss share limits downside risk	❑ Limited on-site due diligence
❑ Deposits typically acquired for low premiums	❑ Quality varies on the data provided from target's books and records
❑ Most transactions involve an up-front cash payment from the FDIC	❑ Additional reporting burden for loss share assets
❑ Loss share deals typically result in the generation of negative goodwill which provides an eventual boost to capital	❑ Servicing costs increase due to high delinquency and foreclosure rate
❑ Assets covered by loss sharing agreement carry a 20% risk weighting	❑ Limited ability to sell or securitize assets without FDIC consent
❑ Acquiring entity has 90 days to decide whether they will purchase fixed assets	❑ Loss share arrangements vary – single family vs. commercial

SANDLER O'NEILL + PARTNERS, L.P.

M&A Market Update

Recent Landmark Recapitalizations of Distressed Banks & Thrifts



Source: SNL Financial; Company documents

M&A Market Update

Sterling Financial Corporation (NASDAQ: STSA)

Summary

- Sterling Financial Corporation, headquartered in Spokane, Washington, had $10.6 billion in assets, $7.6 billion in deposits and $245 million in equity at March 31, 2010
  - At the time, STSA had negative tangible common equity and over 10% of NPAs/assets
- On April 27, 2010, the Company announced that it entered into a binding letter of agreement for the private placement of $134.7 million of common stock (at up to $0.20 per share) and preferred stock (at up to $75 per share) with Thomas H. Lee Partners, L.P. ("THL")
- On May 24, 2010, the Company announced an adjustment to the agreement with THL to increase the investment to $139 million, as well as announced an agreement with Warburg Pincus Private Equity X, L.P. ("WP") to invest an equal amount
- On August 20, 2010, Sterling announced agreements to raise a total of $730 million in new capital from approximately 30 institutional, private equity and other accredited investors
- In addition as part of the recapitalization, the company also completed an exchange with the U.S. Treasury of the company's TARP preferred equity for common stock at a discounted conversion value equal to 25% of the liquidation amount of the preferred (plus accrued and unpaid dividends)
- The amount of capital raised exceeds the amount required under Sterling's agreements with its regulators and restores both Sterling's and Sterling Savings Bank's regulatory ratios to levels that exceed well-capitalized thresholds under applicable guidelines

August 20, 2010

Common & Preferred Stock

$730,000,000

STERLING Financial Corporation

Co-Lead Placement Agent

SANDLER O'NEILL + PARTNERS, L.P.

Source: SNL Financial; Company filings

M&A Market Update

Pacific Capital Bancorp (NASDAQ: PCBC)

Summary

- Pacific Capital Bancorp, headquartered in Santa Barbara, CA, had $7.4 billion in assets, $5.4 billion in deposits and $279 million in equity at March 31, 2010
  - At the time, PCBC had a TCE/TA ratio of 1.33% and NPAs/assets ratio of 6.22%
- On April 29, 2010, Pacific Capital announced a $500 million placement of common stock and preferred stock to SB Acquisition Company LLC, a wholly-owned subsidiary of Ford Financial Fund, L.P.
  - The investment closed on August 31, 2010 and resulted in a 91% ownership of the Company for Ford
- In addition to the Ford investment and as part of the recapitalization, the company also completed the following transactions:
  - An exchange with the U.S. Treasury of the company's TARP preferred equity for common stock at a discounted conversion value equal to 37% of the liquidation amount of the preferred (plus accrued and unpaid dividends)
  - Tender offers for a portion of the company's subdebt (an aggregate of $121 million)
  - The Company and the Bank did not receive valid tenders from holders of any other Trust Preferred Securities or Subordinated Debt Securities

August 31, 2010

Common & Preferred Stock

$500,000,000

PACIFIC CAPITAL BANCORP

Financial Advisor

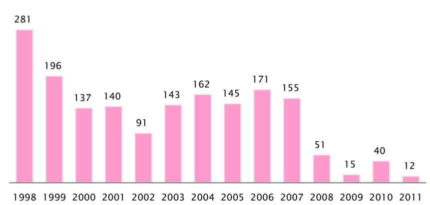
SANDLER O'NEILL + PARTNERS, L.P.

Source: SNL Financial; Company filings

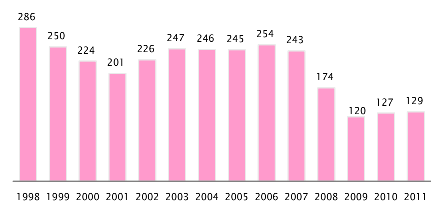
M&A Market Update

Bank & Thrift Deals Since 1998

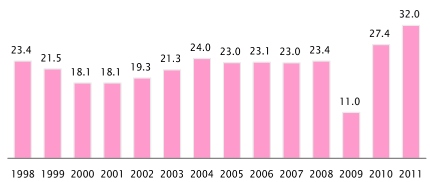
Number of Transactions



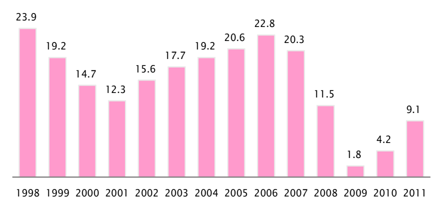
Price / Tangible Book (%)



Price / LTM EPS (x)



Core Deposit Premium (%)



Note: Includes all nationwide bank and thrift deals with announced deal value greater than $15mm; excludes FDIC deals
Source: SNL Financial

M&A Market Update

Emerging Trends

- Conventional M&A will continue to reemerge as buyers get more comfortable with their own credit profile and sellers weigh their options
  - Confident buyers are pursuing M&A discussions as a means to counter their own financial headwinds, accelerate their longer term objectives and deploy offensive capital
  - Compressing economics of assisted transactions encourage a more proactive stance on the part of capable buyers
  - Pricing structures that minimize risk to buyers and/or retention of problem assets by seller will be used
- More banks are being pressured by their regulators or their boards to raise capital, but not all have a compelling story or shareholder base that will allow them to successfully complete a recap or capital raise
  - As a result, more are weighing their options in the M&A market as a less punitive outcome for their shareholders
  - Meanwhile, others being forced to attempt selling at fire-sale prices to avoid failing

M&A Market Update

Emerging Trends – Continued

- Targets are also weighing their options due to:
  - Mounting board and management fatigue from the last three years
  - Depressed stock price with no obvious catalyst for improvement
  - Uncertainty around regulatory reform / greater regulatory burden
  - Rising but unknown regulatory capital targets
  - Meaningful dilution implied by raising needed capital
  - TARP CPP repayment options
  - Revenue growth challenged by limited attractive lending opportunities and legislative impacts on fee income
- These same forces should drive an increase in merger activity between similar sized institutions as means to build scale, diversify business mix and eliminate duplicative costs
- This cycle will continue to favor and reward institutions that are capital rich and acquisition ready while also possessing the due diligence skill set, integration expertise and cohesive, clear strategic vision required to execute

M&A Market Update

Deal Activity by Size

2010 – YTD 2011 Bank and Thrift Transactions

	Announced Transaction Value			
	< $25	$25 – $100	$100 – $500	$500 +
Announced Transactions	51 / 54.8%	25 / 26.9%	12 / 12.9%	5 / 5.4%
Transaction Multiples1				
Price / Book	115%	120%	134%	102%
Price / Tangible Book	112%	121%	162%	164%
Price / LTM Earnings	17.9x	25.9x	24.9x	24.6x
Price / LTM Core Earnings	NA	30.2x	26.8x	24.6x
Price / Est. EPS	NA	18.3x	25.4x	21.6x
Market Premium	69.4%	63.6%	33.6%	31.4%
Core Deposit Premium	1.3%	3.1%	11.8%	3.6%

(1) Does not include transactions for which the deal value was not disclosed
Note: Transaction multiples represent median values. Dollars in millions
Source: SNL Financial

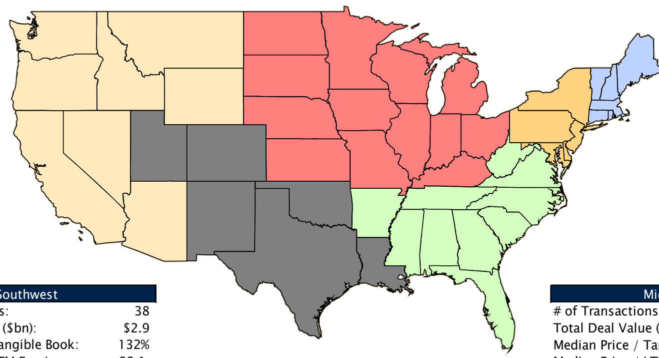
Merger & Acquisition Overview

2010 – YTD 2011 M&A Activity By Region

West	
# of Transactions:	26
Total Deal Value ($bn):	$0.5
Median Price / Tangible Book:	90%
Median Price / LTM Earnings:	45.0x
Core Deposit Premium:	5.4%

Midwest	
# of Transactions:	61
Total Deal Value ($bn):	$4.5
Median Price / Tangible Book:	112%
Median Price / LTM Earnings:	14.8x
Core Deposit Premium:	2.2%

New England	
# of Transactions:	11
Total Deal Value ($bn):	$2.6
Median Price / Tangible Book:	149%
Median Price / LTM Earnings:	24.6x
Core Deposit Premium:	8.8%



Southwest	
# of Transactions:	38
Total Deal Value ($bn):	$2.9
Median Price / Tangible Book:	132%
Median Price / LTM Earnings:	22.1x
Core Deposit Premium:	6.9%

Southeast	
# of Transactions:	37
Total Deal Value ($bn):	$0.7
Median Price / Tangible Book:	78%
Median Price / LTM Earnings:	27.9x
Core Deposit Premium:	(2.5%)

Mid Atlantic	
# of Transactions:	32
Total Deal Value ($bn):	$2.0
Median Price / Tangible Book:	119%
Median Price / LTM Earnings:	24.9x
Core Deposit Premium:	2.2%

Source: SNL Financial

M&A Market Update

Conclusion

- As the industry continues to work through its issues, opportunities for strong institutions will be numerous
- In the Midwest, FDIC assisted transactions should dominate 2011 but open bank M&A should increase
- Most institutions will look to clean up their balance sheets, raise capital and will seek out strategic acquisitions/merger partners

Sandler O'Neill + Partners, L.P.

Vedder Price's "Managing Your Bank in the New Normal"

Mergers and Acquisitions
Capital Markets Update
Whole Loan Climate

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May 13, 2011
The Chicago Club
Chicago, IL

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Table of Contents

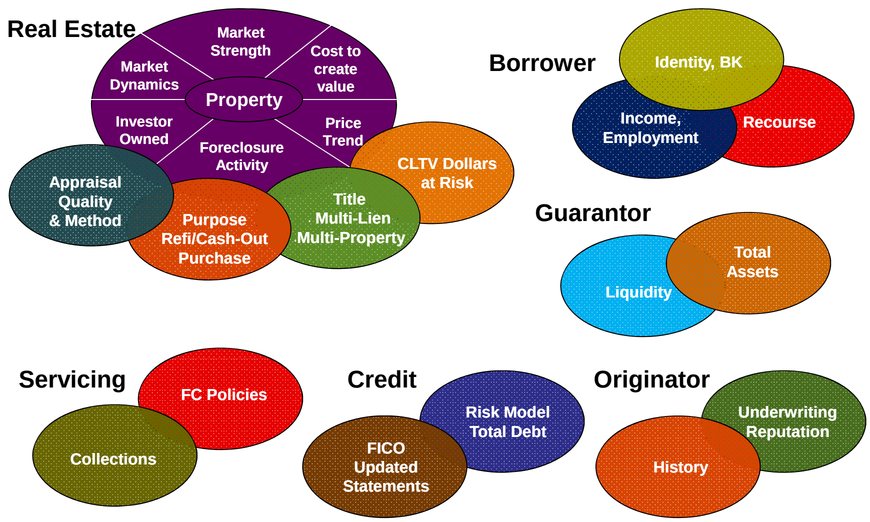
I. Sandler O'Neill Mortgage Finance L.P.

Sandler O’Neill Mortgage Finance L.P.

- 20 year history of serving clients / 15 seasoned professionals
- Since 1996, 600+ transactions for approximately $30B
- Advised / Valued portfolios for 13 FDIC Assisted Transactions
- Expertise across all asset classes and products
- Extensive network of purchasers
- Services: Strategic transaction support & design, portfolio valuation & sales
- Run a low profile end buyer process – no WSJ ads

II. What Buyers Consider

What Buyers Consider



III. Loan Portfolio Strategies

Strategies

- **Performing Loans**
  - Conforming Agency Securitization
  - Whole Loans Conforming and Jumbo

- **Non Performing Loans**
  - Whole Loan Sale Approaches
  - Cash Sale Overview
  - Structured Sale

Conforming Resi Agency Securitization

- **Best execution available, but…**
  - Agency pull-through rates are much lower than before
  - G – Fees: recent transactions have ranged between 30-100 BPS. and can have an "adverse market" fee added on

- **Positive / Negative effects**
  - The spread difference between agency securities and whole loans are at historical highs.
  - Securities are more liquid and offer better capital treatment
  - Income give up can be expensive

Performing Loan Sale – Approaches

- **Agency Cash – Conforming and Jumbo Conforming RESI & MF**
  - Often on a “best ex” basis
  - Less Market risk
  - Servicing retained or released
- **Secondary Market – Conforming and Jumbo RESI**
  - Money Center banks
  - Can be better execution
  - Servicing retained or released
- **Secondary Market – Non RESI**
  - Buyers returning (Conduit’s, PE’s, Banks, Insurance Co.’s), but…
  - Few trades to establish real price comp
  - Credit Quality requirements very high
  - Liquidity redeployment into new loans – limited opportunities

Non Performing Loan Sale - Approaches

- **“Friends and Family” – Bank Relationship**
  - One-by-one (one-off’s) – most frequent approach
  - Doesn’t move the needle very much – resource taxing
  - Buyer execution risk, but can have highest GROSS recovery
- **Retail / Auction**
  - Casts a wide net “shotgun approach” – local / national
  - Longer cycle time
  - Five O'clock news – wide advertisement is often necessary
- **Wholesale Institutional Buyer - Managed Transaction**
  - Advisor determined “go to” group of buyers
  - Can be with loan level or pool reserve prices
  - May be a lower average execution price, but with speed and certainty of closing
  - Under the radar process
  - Cleanses the portfolio

Non Performing Loan Sale – Types

- **Whole Loan Sale– 100% CASH at closing**
  - Sale treatment achieved – "clear the deck"
  - Typically the shortest execution time
  - Servicing released – Cut cost and return to offense
- **Bank Financed – Whole Loan Sale**
  - Can result in higher price but . . .
  - Some states may be subject to lending limits
  - Can have accounting/tax/regulatory hurdles
  - Some risk retention
  - Servicing retained or released

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Non Performing Loan Sale – Types

- **Shared Upside**
  - Some cash at closing - Risk Retention
  - Buyer gets a base return, bank has upside potential after buyer achieves IRR benchmark
  - Servicing retained or released
  - Can have higher accounting/tax/regulatory hurdles
  - Sale treatment typically achieved
- **Structured Product**
  - SPV / LLC
  - Risk Retention
  - Can have high accounting/tax/regulatory hurdles and maintenance
  - Credit Modeling
  - Funding Facility – ACD Loans
  - Servicing released
  - Sale and Capital treatment confirmation recommended

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IV. Appendix

Production/Issuance Statistics

Commercial/Multifamily Mortgage Debt Outstanding

Source: Mortgage Bankers Association/Federal Reserve
Dollars In Billions (4Q10)

Total	$2,400
Commercial	$1,602
Multifamily	$798

Source: Mortgage Bankers Association

Residential Loan Production By Year
(In Billions)

Year	Total	Prime	% Of Total	Alt A	% Of Total	I/O, SubPrime, FHA/VA, Etc.	% Of Total
2008	$1,614	$1,091	67.6%	$16	1.0%	$507	31.4%
2009	$1,919	$1,371	71.4%	$5	0.3%	$543	28.3%
2010 (Est)	$1,400	$900	64.3%	$1	0.1%	$499	35.6%

Source: MortgageStats.com

Commercial Loan Production By Year
(In Billions)

2008	$178.9
2009	$82.3
2010	$110.0

Source: Mortgage Bankers Association

CMBS Issuance By Year
(In Billions)

2008	$27.0
2009	$24.0
2010	$50.0

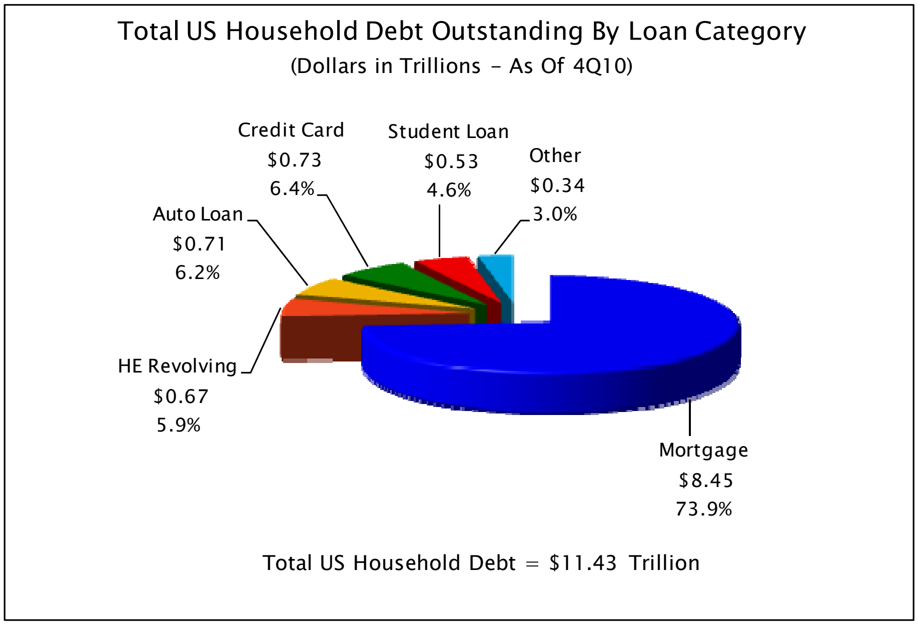
Source: Bloomberg

Agency RMBS Issuance By Year
(In Billions)

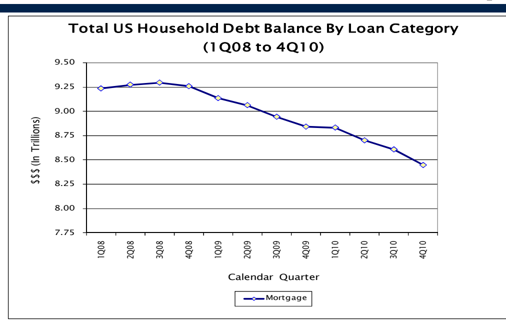
2008	$1,150
2009	$1,725
2010	$1,403

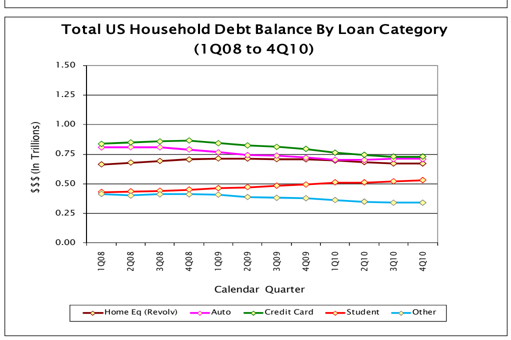
Source: Bloomberg

Total Household Loan Debt (US)



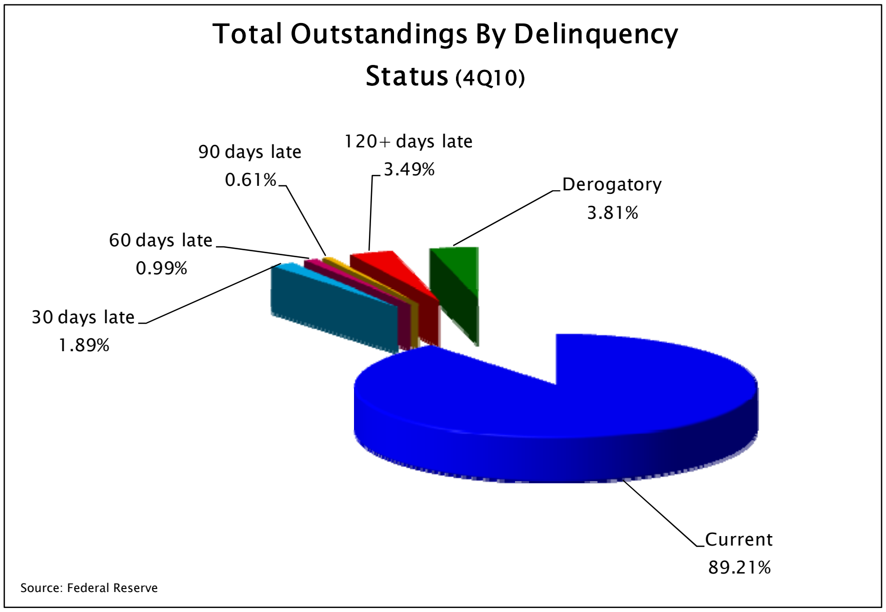
Total Household Loan Debt (US)



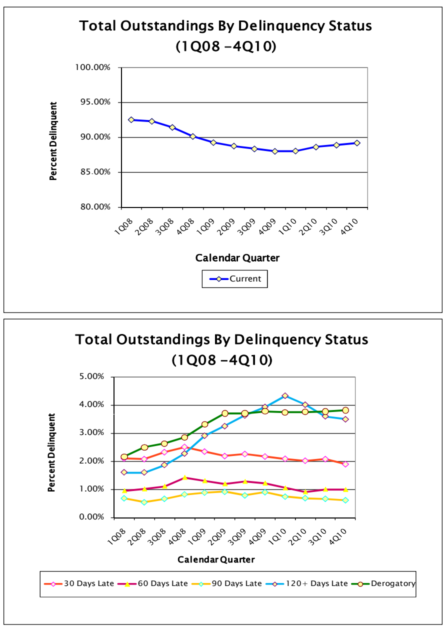


Source: Federal Reserve

Delinquency Experience (US)



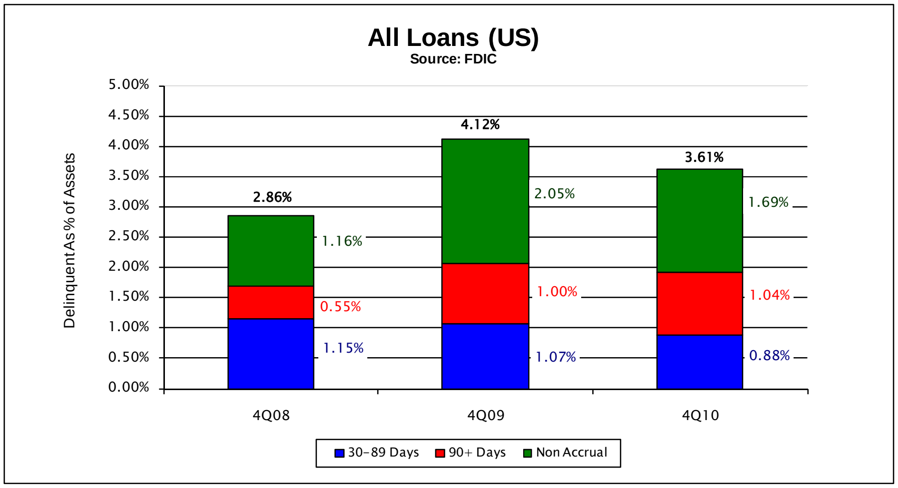
Delinquency Experience (US)



Source: Federal Reserve

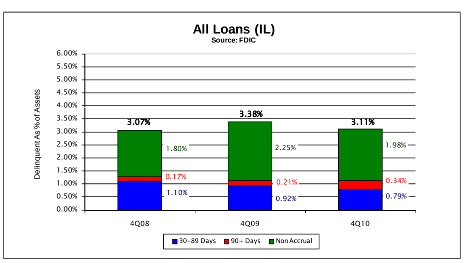
Delinquency Experience By Selected State

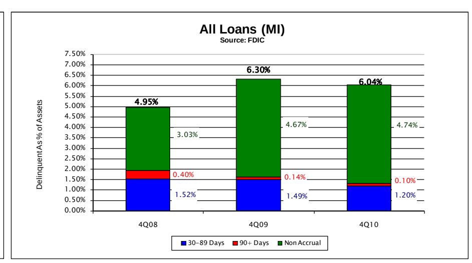
Stated As % Of Total Assets

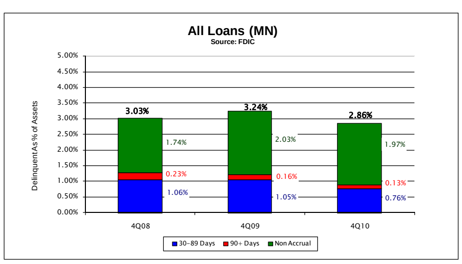


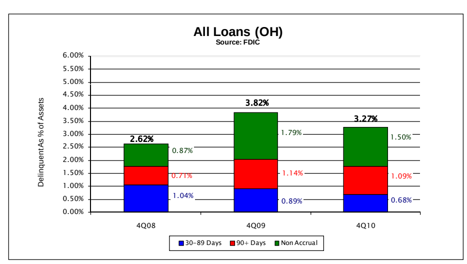
Delinquency Experience By Selected State

Stated As % Of Total Assets

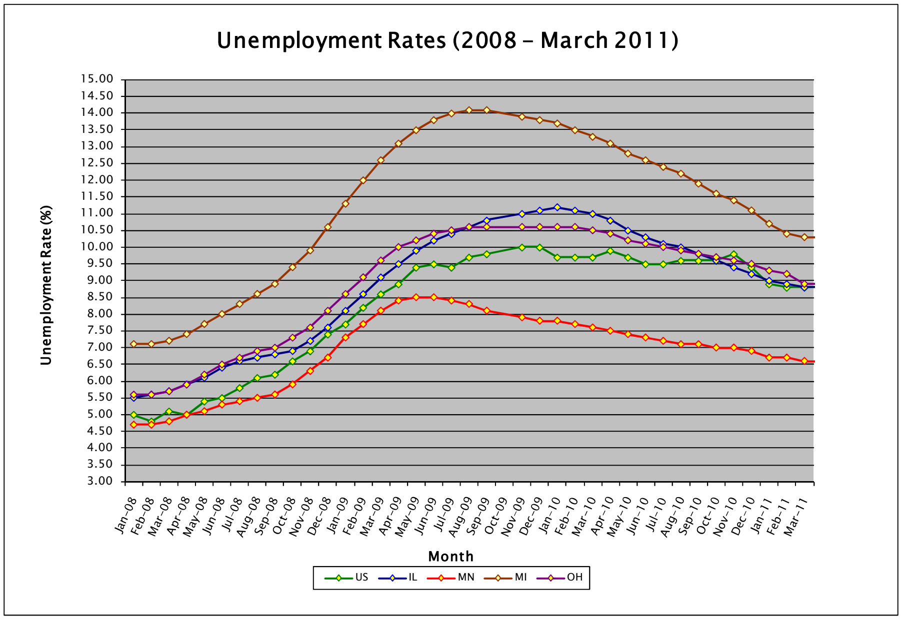








Unemployment Rates (US) vs. (Selected States)



FDIC Past Due & Non-Accrual (All Institutions)

4Q10 Data (% of Total Assets)

Source: FDIC

30 to 89 Days

Loan Category	US	IL	MI	MN	OH
Construction and land development	0.05%	0.08%	0.06%	0.08%	0.03%
Secured by farmland	0.00%	0.01%	0.01%	0.02%	0.00%
Secured by 1-4 family residential properties	0.44%	0.28%	0.61%	0.28%	0.41%
Secured by multifamily residential properties	0.01%	0.06%	0.03%	0.01%	0.02%
Secured by nonfarm nonresidential properties (CRE)	0.08%	0.18%	0.30%	0.19%	0.04%
Commercial and industrial loans	0.06%	0.10%	0.10%	0.12%	0.05%
Loans to individuals	0.20%	0.07%	0.08%	0.04%	0.11%
Credit cards	0.11%	0.01%	0.00%	0.00%	0.03%
Other loans	0.01%	0.01%	0.00%	0.01%	0.02%

90+ Days

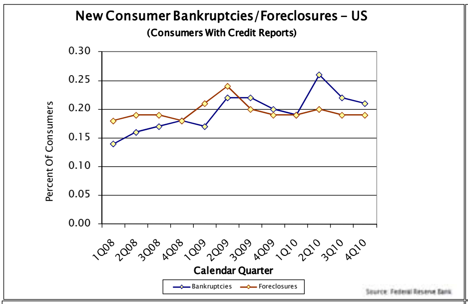
Loan Category	US	IL	MI	MN	OH
Construction and land development	0.05%	0.11%	0.01%	0.01%	0.02%
Secured by farmland	0.00%	0.00%	0.00%	0.01%	0.00%
Secured by 1-4 family residential properties	0.74%	0.07%	0.05%	0.03%	0.94%
Secured by multifamily residential properties	0.01%	0.03%	0.00%	0.00%	0.00%
Secured by nonfarm nonresidential properties (CRE)	0.03%	0.08%	0.02%	0.03%	0.02%
Commercial and industrial loans	0.02%	0.03%	0.01%	0.03%	0.02%
Loans to individuals	0.16%	0.02%	0.00%	0.01%	0.08%
Credit cards	0.11%	0.01%	0.00%	0.00%	0.03%
Other loans	0.00%	0.00%	0.00%	0.00%	0.01%

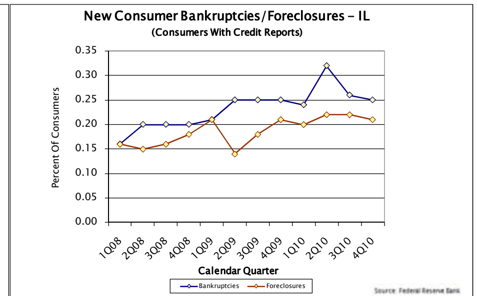
Non-Accrual

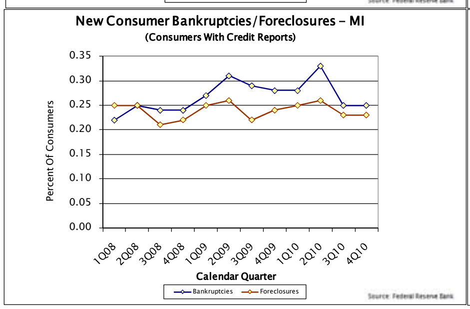
Loan Category	US	IL	MI	MN	OH
Construction and land development	0.34%	0.55%	0.47%	0.48%	0.13%
Secured by farmland	0.01%	0.03%	0.02%	0.06%	0.00%
Secured by 1-4 family residential properties	0.67%	0.43%	2.85%	0.36%	0.87%
Secured by multifamily residential properties	0.05%	0.14%	0.11%	0.04%	0.06%
Secured by nonfarm nonresidential properties (CRE)	0.31%	0.58%	1.04%	0.64%	0.15%
Commercial and industrial loans	0.21%	0.19%	0.21%	0.33%	0.20%
Loans to individuals	0.03%	0.02%	0.02%	0.02%	0.03%
Credit cards	0.01%	0.00%	0.00%	0.00%	0.01%
Other loans	0.04%	0.03%	0.00%	0.02%	0.04%

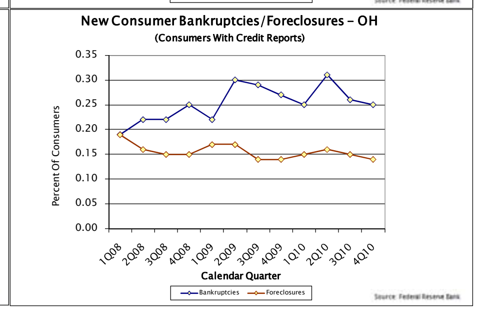
Foreclosure & Bankruptcy Experience

(All Districts) vs. (Selected Districts)



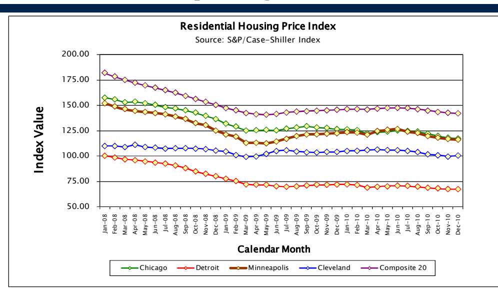


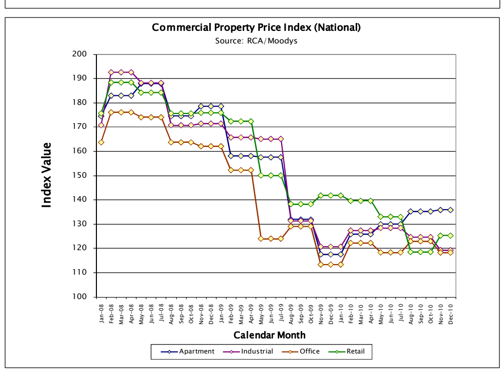




SANDLER O'NEILL + PARTNERS, L.P.

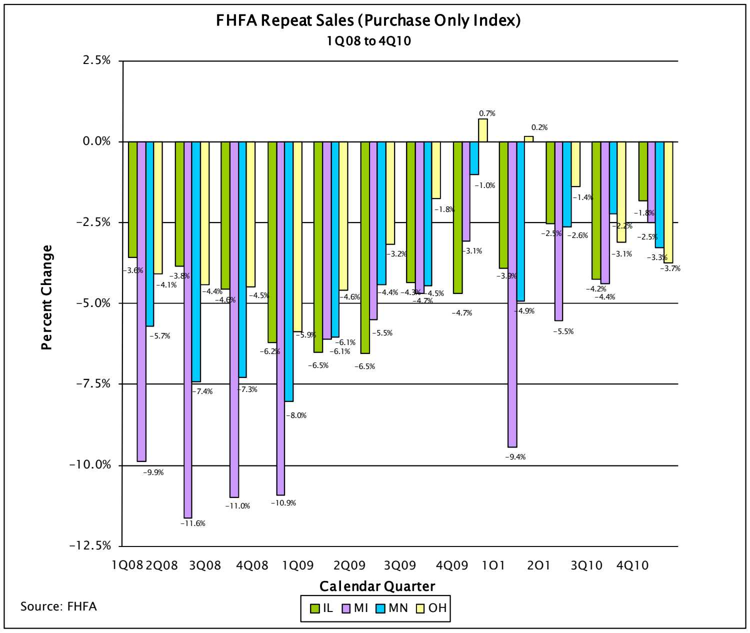
Property Values





SANDLER O'NEILL + PARTNERS, L.P.

Residential Repeat Sales Index



Residential Housing Statistics

Metro Area Residential Housing Statistics

Metro Area	Median Home Price	1 Yr Appreciation Rate	3 Yr Appreciation Rate	Unemployment Rate (1)
Illinois				
Chicago	183,400	-4.2%	-29.7%	8.6%
Springfield	117,100	4.7%	7.8%	7.1%
Peoria	126,100	12.7%	6.4%	8.8%
Minnesota				
Minneapolis	165,300	-1.3%	-23.9%	6.5%
Michigan				
Grand Rapids	92,600	3.0%	-25.5%	8.9%
Lansing	79,500	-5.4%	-27.5%	8.3%
Ohip				
Cincinnatti	127,200	1.8%	3.9%	9.0%
Toledo	74,500	-13.9%	-28.4%	10.4%
Cleveland	114,700	4.2%	-3.3%	8.5%
National	169,800	-0.60%	-18.20%	9.40%

Source: National Association of Realtors (4Q10 Data)

(1) December, 2010

Q & A

Key Legal Issues In Bank Consolidation and Capital Raising

Daniel O'Rourke
Shareholder
Financial Institutions Group
Vedder Price P.C.

Consolidation

- There have been relatively few negotiated mergers and acquisitions with financial institutions as buyers in the Midwest (see Harris Bank and M&I); however, the trend is positive
- There have also been few branch transactions (see Anchor Bank, Madison, Wisconsin) and one-off deals (see Citizens South Banking Corp.'s acquisition of Horizon Bank) done as P&A's, etc.
- There have been transactions with non-banks, e.g., Toronto-Dominion Bank's planned purchase of Chrysler Fin. Serv. Americas, LLC
- Private Equity firms have played a significant role in "forced recaps" of sick, but not dead, banks

continued

Consolidation

- In forced recaps, Treasury/TARP, TruPS holders, the “bank stock” correspondent lender and the public stockholders get crammed down to cents on the dollar. A rights offering for the public stockholders at the investor buy-in price is common
- Regulatory approval issues for Private Equity firms: avoiding Federal Reserve “BHC” control status and FDIC Private Equity Policy Statement. Renewed focus on “change of control” and BCOCA
- Blind Pools; Club Deals – more common; some without regulatory approval
- THE BIGGEST ISSUE OF ALL – how bad are the loans? How big is the hole? It won’t go away after 4 years. “Deep Dives”

Legal/Regulatory Issues

- Dealing with shareholder voting rights of seller
- Dealing with TruPS disclosure and consent issues:
  - Who votes and how – two-thirds supermajority?
  - CDO TruPS trustee may be unwilling to act without 100% consent for fear of liability to holders
  - Multiple tranches of investors
  - Indentures are vague and present tactical issues
- Disclosure issues: “going concern”; asset quality; ALLL, CRE
- See above for Private Equity
- New Delaware law on poison pills and director duties
- FDIC litigation against directors and officers

Legal/Regulatory Issues

- As "whole bank" mergers reemerge, issues will be
  - Asset quality representations
  - MAC clauses
  - Hold backs, earn-outs and contingent valuation rights

Bankruptcy: Not Just for Donald Trump

- Banks are not subject to the Bankruptcy Code, but bank holding companies ("BHCs") are, leading to BHC Bankruptcy § 363 sales and/or liquidations:
  - Why?
    - Too much BHC leverage
    - Recap investors often seek to dilute TruPS interests to enhance recap dollars
    - TruPS indentures may allow owners to block recap efforts
    - TruPS often pooled – investors impossible to locate, or won't agree
    - TruPS holders/trustee refuse to accept ("tyranny of the majority") a dilution of interest at the cost of a potential bank seizure
    - Section 363 may permit a sale despite these impediments

continued

Bankruptcy

- Who?
  - AmericanWest Bancorporation (BHC with a single bank subsidiary):
    - Severely underfunded – unsuccessful efforts to raise capital
    - TruPS were placed in complex CDOs – discouraged prospective investors
    - Section 363 allowed BHC to sell single bank sub to a P/E fund free and clear while averting impending FDIC bank seizure
    - TruPS holders objected but typically have little, if any, "standing" in § 363 sales
  - AmericanWest is the model other banks are seeking to replicate
  - Builders Financial Corp.:
    - Filed for Chapter 11
    - Requesting $40 million in TruPS holders to accept 10¢ on the dollar over the next 10 years
    - To Builders' surprise, trustee showed up and objected!
    - As of February 2011, Builders seeking to invalidate trustee's vote

continued

Bankruptcy

- Who?
  - Outsource Holdings, Inc.:
    - Seeking a § 363 sale
    - On May 5th, bankruptcy judge ordered a trustee to examine proposed sale of Jefferson Bank after a holder of $5.3 million of notes objected
    - Trustee will see if the stalking horse seller is underbidding

continued

Bankruptcy

- Drawbacks?
  - Lack of potential buyers
  - Regulatory approval
  - Timing constraints – FDIC receivership (bankruptcy not a "clock stopper")
  - Bankruptcy process also used after FDIC forces closing of bank subsidiary for an orderly liquidation and distribution of BHC assets, e.g., tax refunds, cash, real estate – see Corus

Capital Raising

- TARP is gone, now SBLF
- Privately held TARP recipients cannot pay back Treasury
- Some banks are seeking SBLF dollars to refinance preferred stock under TARP to eliminate "TARP stigma." But, this option is unavailable to FDIC problem banks
- Capital for healthy banks can be raised – at what price?
- Capital for sick banks is rare, unless they are both fixable and of a size at which further "roll-ups" are likely – searching for the "Unicorn"
- Open Bank Assistance is a myth
- Treasury will renegotiate TARP where situation warrants

Capital Raising

- FDIC Policy on P.E. – enforced on a deal-by-deal basis
- P.E. funds going after "failing" banks, but not "dead" banks
- TruPS: Tier 1 Capital status grandfathered under Dodd-Frank for banks with assets under $15 billion. Banks with assets under $500 million will still be able to issue TruPS. See Collins Amendment
- De Novos: a few in 2010 (e.g., California); need to focus on "traditional" bank lending, small business loans and core deposits; won't see any in near future in Atlanta, Chicago, Florida, Arizona, etc.
- Correspondent bank sources: still difficult to find, if they exist at all

Loss-Share

- Through September 2010 (the most recently available data), the FDIC has entered into 200 loss-sharing agreements, with $159.2 billion in assets under loss sharing

continued

Loss-Share

- The six most important features of the transaction documents are:
  - Loss Rate: Sharing losses on a 95/5 basis was eliminated for all loss-share agreements executed after March 26, 2010. Some deals as low as 50/50 (see, e.g., TD Bank NA acquiring 3 Florida banks)
  - Administration: Acquiring bank must track charge-offs, recoveries, reimbursable expenses, etc. over 8 or 10 years depending on whether the loan is a commercial or single-family loan (respectively)
  - Loan Changes: Acquiring banks have limitations on implementing amendments and restructuring of loans, i.e., acquiring banks cannot increase the principal of loss-share assets, except for certain permitted advances, or extend the term of loss-share assets beyond the term of the loss-share agreement without risking losing loss-share coverage

continued

Loss-Share

- The six most important features:
  - Estimated Loss: The FDIC estimates the total loss on loss-share agreements and will maintain the ability to "claw back" certain amounts if the ultimate losses on the loss-share agreement are lower than this estimated amount
  - First Loss Tranche: Bidding institutions must bid an amount of the first loss tranche, which cannot be less than zero. If the first loss tranche is a positive number, then loss-sharing will not commence until the losses on the loss-share assets exceed the first loss tranche
  - FDIC Audit: The acquiring bank is subject to an audit of loss-share loan administration by the FDIC's third-party auditor
  - Who can bid?
  - Accounting issues – too much negative goodwill

Loss-Share

- The six most important features:
  - FDIC may continue to tweak the formula
  - Some bidders have offered better terms, e.g., 50/50 loss share or no loss share at all

Keynote Speaker

Ellen M. Costello

President and Chief Executive Officer

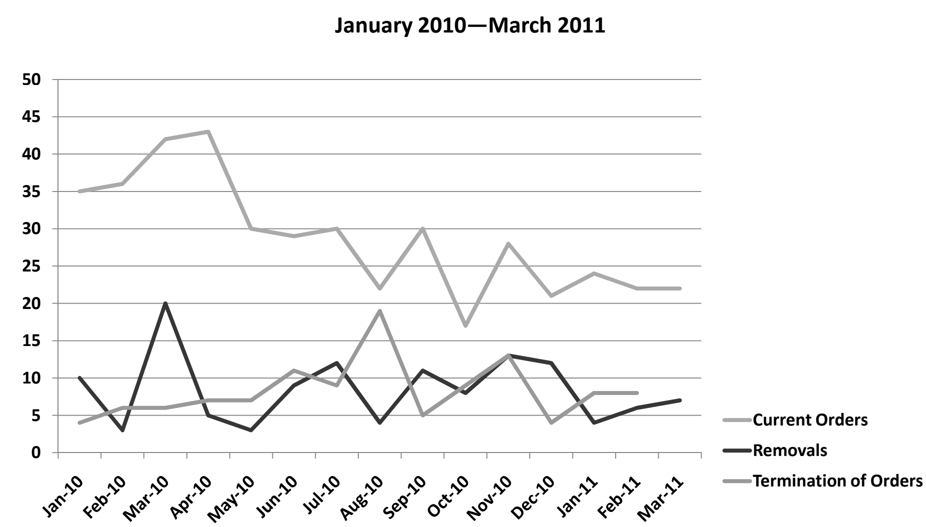
Harris Financial Corp.

VEDDER PRICE.

Enforcement Trends

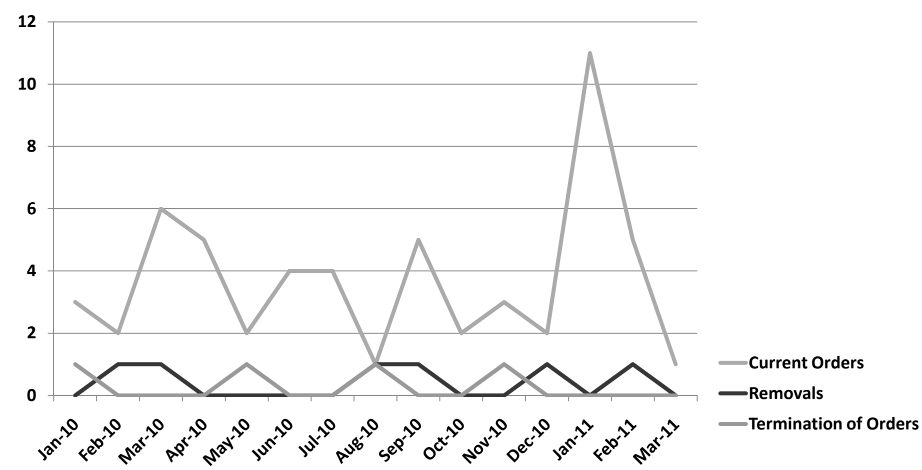
James M. Kane
Shareholder
Chair, Financial Institutions Group
Vedder Price P.C.

Selected FDIC Enforcement Actions Nationwide



Selected FDIC Enforcement Actions in Illinois

January 2010—March 2011



Selected FDIC Enforcement Actions in Illinois

January 2010—March 2011

	Current Orders	Removals	Termination of Orders
Jan-10	3	0	1
Feb-10	2	1	0
Mar-10	6	1	0
Apr-10	5	0	0
May-10	2	0	1
Jun-10	4	0	0
Jul-10	4	0	0
Aug-10	1	1	1
Sep-10	5	1	0
Oct-10	2	0	0
Nov-10	3	0	1
Dec-10	2	1	0
Jan-11	11	0	0
Feb-11	5	1	0
Mar-11	1	0	0

Changing Content of Enforcement Actions

- Capital
- Management studies

Capital

- Newest trend
  - 9% Tier 1
  - 13% TRBC

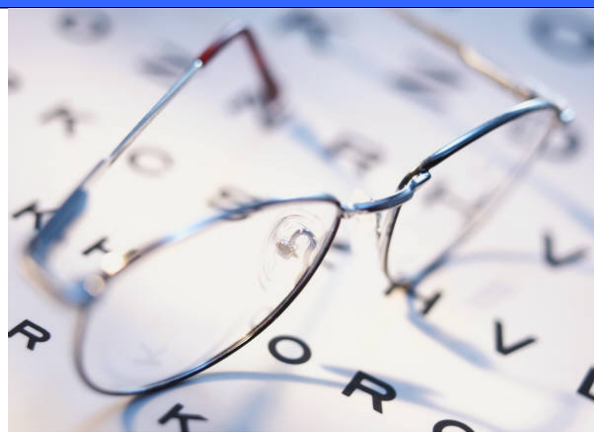
The Problems with Higher Capital Ratios

- Capital is hard to find
- Shrinking the bank
- Impact profitability (fewer loans)
- Increases FDIC assessment

Management Study

- Becoming automatic
- The perils of a management study

Focusing on CRA and Fair Lending Risk….



Discussion Comments by:

Jerry Miller, President
Regulatory Compliance Associates, Inc.
REGCOM

VEDDER PRICE

Events

Seminar: Managing Your Bank in the New Normal

05/13/2011

Discussion Insights

- Reflecting on the initial focus
  - Since initial passage of consumer regulations, there has been continual change
  - Regulations change, examination focuses change
- Looking at historical facts (examples)
  - Referrals by agencies to Department of Justice
  - CRA examination ratings
- Assessing the current issues and events landscape
  - New examination norm
  - Fair lending examination and CRA examination focuses
  - Range of examination findings plus
- Gazing a bit into the future
  - Regulatory changes
  - Industry changes
- Adjusting to evaluate risk change
  - Risk focus
  - Control points

Regulatory Insights (June 2010) — ABA Conference:

Ann Jaedicke, Deputy Comptroller for Compliance Policy, OCC
"*OCC examiners are much more sensitized to UDAP and as a result, it is more likely to lead to an enforcement action."*

Calvin Hagins, Director for Compliance Policy, OCC
"There are many fair lending issues that you may face, and that you need to demonstrate how you're identifying, measuring, and managing. You need to evaluate the direction of your risks whether they are increasing, decreasing, or remaining stable."

Luke Brown, Associate Director, Div. of Depositor and Consumer Protection, FDIC
"It is very important that you focus on your third-party relationships with regards to customer disclosures, etc."

REGCOM

CRA and Fair Lending Briefing

Risk Management Insights

The Negative Impact of Fair Lending Problems

May 2011

Prepared by:
Regulatory Compliance Associates, Inc.
REGCOM
www.regcominc.com

Focusing on CRA and Fair Lending Risk

Table of Contents

Regulatory Insights:

Ann Jaedicke, Deputy Comptroller for Compliance Policy, OCC

"*OCC examiners are much more sensitized to UDAP and as a result, it is more likely to lead to an enforcement action.*"

"There is a sense that zero tolerance is where regulation is headed."

Calvin Hagins, Director for Compliance Policy, OCC

"There are many fair-lending issues that you may face, and that you need to demonstrate how you're identifying, measuring, and managing. You need to evaluate the direction of your risks whether they are increasing, decreasing, or remaining stable."

Luke Brown, Associate Director, Div. of Depositor and Consumer Protection, FDIC

"It is very important that you focus on your third-party relationships with regards to customer disclosures, etc."

Focusing on CRA and Fair Lending Risk

Reflecting on the initial focus…….

- Fair lending = Fair Housing Act (FHA) and Equal Credit Opportunity Act (ECOA) plus Community Reinvestment Act (CRA) and Home Mortgage Disclosure Act (HMDA)

- Over the years, each of these regulations have been revised, expanded, and in some instances, new interpretations released

- Interagency Fair Lending Policy Statement on Discrimination in Lending, released April 1994, signed by 10 federal agencies, defines what discrimination

- In 1995, the industry moved from the 12 assessment factors to the stratified CRA exam with varying tests, based on asset size or categories:
    - Small Retail Institution
    - Large Institution
    - Limited Purpose
    - Wholesale
  - In 2005, a third category appeared: Intermediate Retail Institution

- In 2004, financial institutions subject to data collection and reporting provisions of the Home Mortgage Disclosure Act were required to substantially alter their data reporting systems to accommodate multiple changes. Changes included three provisions specifically designed to help identify potential predatory lending concerns:
  - Rate spread information for certain loans that trigger reporting requirements;
  - Home Owners Equity Protection Act (HOEPA) flags; and
  - Lien status for applications and loans originated (not required for purchased loans).

- In 2005, the federal banking regulatory agencies amended Regulation BB that implements the Community Reinvestment Act to specifically identify those regulations that if violated substantively, would trigger a finding of an illegal credit practice. The regulations identified include:
  - The Home Owners Equity Protection Act;
  - Section 8 of RESPA – HUD-1 and HUD-1A Settlement Statements; and
  - Section 5 of the Federal Trade Commission Act (FTC Act), which declares that unfair or deceptive trade practices are illegal.

NOTE: Several new Regulations added to the mix including UDAP, RESPA and HOEPA

Looking at historical facts …..

□ Consumer Complaints – FRB Analysis

Consumer Complaints Against State Member Banks				
Classification	**2006**	**2007**	**2008**	**2009**
Regulation AA (Unfair or Deceptive Acts or Practices	0	85	117	82
Regulation B (Equal Credit Opportunity)	53	62	30	49
Regulation C (Home Mortgage Disclosure Act)	0	1	8	4
Regulation BB (Community Reinvestment)	1	6	0	2
Fair Credit Reporting Act	117	138	72	83
Fair Housing Act	3	1	3	1
TOTAL	174	293	230	221

Source: Federal Reserve Board Annual Report Released in May each year.

□ Department of Justice (DOJ) Referrals by Regulatory Agencies

ALL REFERRALS	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	Total
FDIC	33	21	12	15	29	35	42	29	33	5	**254**
FRB	6	6	3	9	5	2	3	0	6	1	**41**
OTS	6	4	4	3	0	0	1	0	0	1	**19**
OCC	2	0	1	0	0	0	0	0	1	3	**7**
NCUA	0	0	0	0	0	0	—	—	—	—	**0**
HUD	2	0	0	0	0	1	1	0	2	—	**6**
Total	**49**	**31**	**20**	**27**	**34**	**38**	**47**	**29**	**42**	**10**	**327**

Race/Nat'l Origin Discrimination	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	Total
FDIC	14	5	2	1	3	1	0	2	1	2	**31**
FRB	4	3	0	4	2	0	0	0	1	1	**15**
OTS	4	3	3	2	0	0	0	0	0	1	**13**
OCC	2	0	0	0	0	0	0	0	0	0	**2**
NCUA	0	0	0	0	0	0	—	—	—	—	**0**
HUD	2	0	0	0	0	1	1	0	2	—	**6**
Total	**26**	**11**	**5**	**7**	**5**	**2**	**1**	**2**	**4**	**4**	**67**

"—"indicates there was no reference to the agency in that year's ECOA report.

NOTE:

As of December 31, 2010, DOJ had returned 28 of the 47 bank agency 2010 referrals for administrative resolution, or more than 59 percent.

CRA Examination Ratings

	Small Bank Test				Large Bank Test				Intermediate Small Bank Test			
RATING	**FRB**	**FDIC**	**OCC**	**OTS**	**FRB**	**FDIC**	**OCC**	**OTS**	**FRB**	**FDIC**	**OCC**	**OTS**
2010												
Outstanding	4%	2%	12%	31%	27%	13%	30%	33%	13%	6%	27%	31%
Satisfactory	96%	94%	87%	65%	73%	85%	70%	67%	87%	89%	71%	55%
Needs to Improve	0%	3%	1%	3%	0%	2%	0%	0%	0%	5%	2%	14%
Substantial Noncompliance	0%	1%	0%	1%	0%	0%	0%	0%	0%	0%	0%	0%
(Number of banks)	123	766	120	65	30	116	20	12	47	275	44	35
2009												
Outstanding	9%	2%	8%	30%	19%	19%	15%	30%	12%	7%	9%	20%
Satisfactory	89%	96%	91%	63%	74%	77%	24%	70%	87%	91%	88%	74%
Needs to Improve	1%	1%	1%	6%	7%	4%	0%	0%	1%	2%	3%	6%
Substantial Noncompliance	1%	1%	0%	1%	0%	0%	0%	0%	0%	0%	0%	0%
(Number of banks)	130	1093	191	106	43	97	39	23	74	216	67	61
2008												
Outstanding	5%	1%	15%	20%	21%	23%	26%	38%	15%	7%	17%	20%
Satisfactory	95%	97%	85%	75%	79%	74%	74%	54%	85%	91%	83%	80%
Needs to Improve	0%	2%	0%	4%	0%	2%	0%	8%	0%	2%	0%	0%
Substantial Noncompliance	0%	0%	0%	1%	0%	1%	0%	0%	0%	0%	0%	0%
(Number of banks)	104	979	157	138	42	115	19	26	60	219	48	45

Focusing on CRA and Fair Lending Risk

Assessing current issues and events…….

New Examination Norm:

- **Fair lending examination time (onsite/office) measured in weeks and even months**

- **Focus of a fair lending examination**
  - Underwriting and/or decision process(es)
  - Pricing, including fees
  - Servicing (including default management, loss mitigation practices, trouble debt homeowner counseling)
  - Product steering
  - Redlining
  - Marketing
  - Compliance and/or fair lending program, e.g., policy, procedures, training, self-monitoring, corrective actions

- **Data Accuracy**
  - HMDA data reporting
    - Quarter end
    - Year end
  - CRA data reporting
    - Small business data reporting
    - Community development loans
  - Support documentation critical for both of these reporting focuses
    - Consistent data capture
    - Organizational standard definitions

- **Data Analysis**
  - Evaluation of HMDA data for current year, and prior years, with analysis/comparisons to peer performance
  - CRA Data evaluation – analysis same as HMDA data
  - Assessment of consumer complaints and correlation to data analysis
  - Determination of assessment area adequacy

Focusing on CRA and Fair Lending Risk

Assessing current issues and events……. (cont.)

New Examination Norm: (cont.)

- **Findings**

  Fair Lending
  - Technical regulation violations – which often translate to expanded examiner fair lending reviews
  - Data inaccuracy – not only resulting in cited violations and potential Civil Monetary Penalties, but also follow-up examiner reviews
  - Lack of supporting documentation in loan files that justifies exceptions to loan policies or underwriting guidelines
  - Wide discretion in pricing of rates, fees, and minimums, with little guidance or no limits
  - Inadequate oversight of third-party arrangements and their performance, e.g., loan brokers, marketing representatives
  - Credit score granting system without adequate review of underlying criteria
  - Weak compliance management systems

  CRA
  - Errors in determination of assessment area (AA)
  - Insufficient lending within the AA
  - Minimal lending in low- and/or moderate income areas
  - Lack of investments in the designated AA
  - Poor community development lending, investment, and/or services initiatives
  - Inadequate community communications and/or marketing

AND

→ **More referrals to the Department of Justice**

→ **More negative CRA ratings**

→ **Problematic fair lending and CRA examinations which also have resulted in downgrades to compliance exam ratings and potentially, subsequent enforcement actions and/or CMPs**

Focusing on CRA and Fair Lending Risk

Gazing a bit into the future …..

2011 and Beyond

- ***Regulatory changes***
  - Consumer Financial Protection Bureau (CFPB) after July 21, 2011
    - For large banks, over $10 billion in total assets, it appears CFPB staff will review for ECOA and HMDA; meanwhile other regulators will review for CRA and FHA, as well as other fair lending related regs.
    - Possibly the CFPB will handle all fair lending and CRA exams
    - Responsibility for the actual regulations will rest with different agencies, e.g., FHA with HUD, CRA with respective agencies
    - For banks under $10 billion in total assets, anticipate change as new inter-related regulations continue to emerge, e.g., SAFE Act, and revisions to existing regulations, e.g., RESPA, Broker compensation
  - Further refinement of newly implemented Regulations, e.g., SAFE Act
  - Proposed new regulations including micro-requirements that creditors review consumers' ability to repay mortgage before lending
  - Examination approaches will change

- ***Loan modifications, mortgage foreclosures, and litigation***
  - Be careful in approach
  - Fallout on foreclosures is significant, and will continue
  - Private litigation today and in the future should be carefully monitored
    - Disparate impact

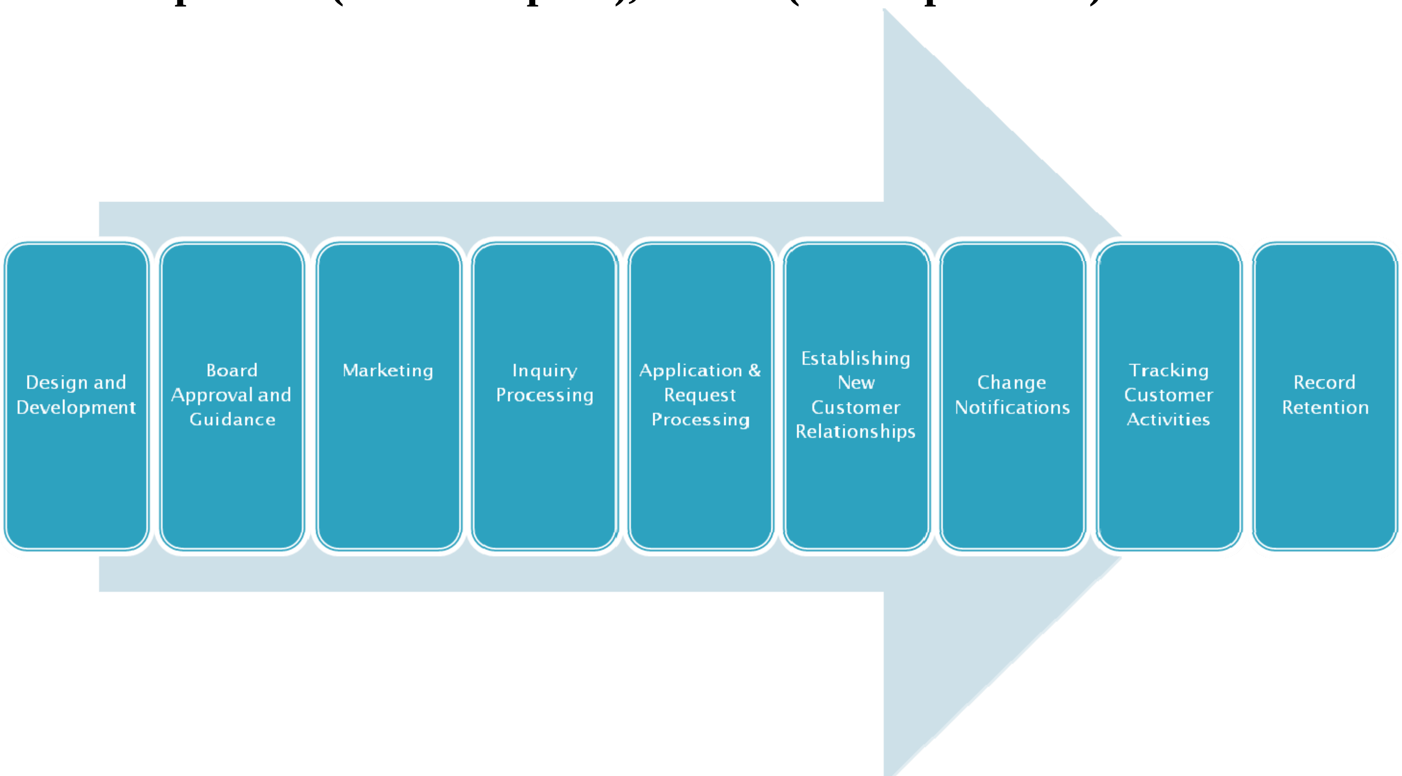
- ***Independent studies and reports***
  - Ex: REDLINED – A Fair Lending Analysis of the St. Louis Metro Area

- ***Specific organizational approach (asset size appropriate)***
  - Structure and approach to ensure fair lending and CRA compliance
  - Emphasis on data integrity
  - Analysis of lending performance bandwidth and reporting the findings
  - Evaluation and assessment of consumer complaints/comments
  - Utilization of analytical/statistical tools
  - Evidence of an independent fair lending self-assessment
  - Proactive response to cited areas of concern

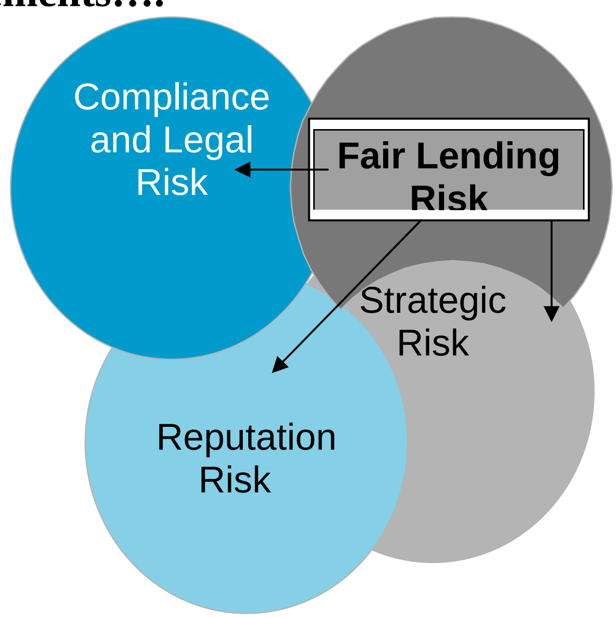
Focusing on CRA and Fair Lending Risk

Adjusting to evaluate risk……

Each product (loan or deposit), service (safe deposit box) or event:



Recognizing risk elements….



Appendix Items

Appendix A **Profile of CRA Examination Ratings by Agency**

Appendix B **November 16, 2010 FDIC Teleconference on Fair Lending Issues Questions and Answers (Posted January 2011)**

Appendix C **Referrals to DOJ**

Appendix D **Quantity and Quality of Fair Lending Risk Indicators—MACRO OVERVIEW**

Appendix E **Fair Lending Risk Indications Checklist**

Appendix A

Profile of Examination Ratings by Agency

CRA Ratings by Agency and Bank Size

Note: Preliminary list based on available information as of

	Small Bank Test				Large Bank Test				Intermediate Small Bank Test			
RATING	**FRB**	**FDIC**	**OCC**	**OTS**	**FRB**	**FDIC**	**OCC**	**OTS**	**FRB**	**FDIC**	**OCC**	**OTS**
2010												
Outstanding	4%	2%	12%	31%	27%	13%	30%	33%	13%	6%	27%	31%
Satisfactory	96%	94%	87%	65%	73%	85%	70%	67%	87%	89%	71%	55%
Needs to Improve	0%	3%	1%	3%	0%	2%	0%	0%	0%	5%	2%	14%
Substantial Noncompliance	0%	1%	0%	1%	0%	0%	0%	0%	0%	0%	0%	0%
(Number of banks)	123	766	120	65	30	116	20	12	47	275	44	35
2009												
Outstanding	9%	2%	8%	30%	19%	19%	15%	30%	12%	7%	9%	20%
Satisfactory	89%	96%	91%	63%	74%	77%	24%	70%	87%	91%	88%	74%
Needs to Improve	1%	1%	1%	6%	7%	4%	0%	0%	1%	2%	3%	6%
Substantial Noncompliance	1%	1%	0%	1%	0%	0%	0%	0%	0%	0%	0%	0%
(Number of banks)	130	1093	191	106	43	97	39	23	74	216	67	61
2008												
Outstanding	5%	1%	15%	20%	21%	23%	26%	38%	15%	7%	17%	20%
Satisfactory	95%	97%	85%	75%	79%	74%	74%	54%	85%	91%	83%	80%
Needs to Improve	0%	2%	0%	4%	0%	2%	0%	8%	0%	2%	0%	0%
Substantial Noncompliance	0%	0%	0%	1%	0%	1%	0%	0%	0%	0%	0%	0%
(Number of banks)	104	979	157	138	42	115	19	26	60	219	48	45
2007												
Outstanding	9%	3%	9%	20%	31%	22%	41%	63%	13%	8%	26%	46%
Satisfactory	90%	94%	91%	77%	69%	76%	59%	37%	87%	90%	74%	54%
Needs to Improve	1%	2%	0%	2%	0%	2%	0%	0%	0%	2%	0%	0%
Substantial Noncompliance	0%	1%	0%	1%	0%	0%	0%	0%	0%	0%	0%	0%
(Number of banks)	147	659	196	143	35	104	27	16	41	189	50	24
2006												
Outstanding	7%	6%	12%	19%	18%	17%	39%	50%	10%	14%	16%	0%
Satisfactory	92%	91%	87%	77%	82%	80%	61%	50%	90%	84%	84%	0%
Needs to Improve	0%	2%	1%	4%	0%	3%	0%	0%	0%	2%	0%	0%
Substantial Noncompliance	1%	1%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
(Number of banks)	151	422	127	114	45	109	36	20	42	169	50	0
2005												
Outstanding	5%	13%	13%	31%	18%	16%	22%	52%	0%	0%	25%	0%
Satisfactory	94%	85%	86%	66%	82%	83%	78%	48%	100%	100%	75%	0%
Needs to Improve	0%	1%	1%	3%	0%	1%	0%	0%	0%	0%	0%	0%
Substantial Noncompliance	1%	1%	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%
(Number of banks)	124	594	135	92	73	323	49	25	12	2	8	0

RATING	Small Bank Test				Large Bank Test				Intermediate Bank Test
	FRB	FDIC	OCC	OTS	FRB	FDIC	OCC	OTS	Not implemented
2004									
Outstanding	22%	7%	11%	27%	28%	12%	21%	16%	
Satisfactory	77%	91%	88%	70%	72%	87%	79%	84%	
Needs to Improve	0%	1%	1%	3%	0%	1%	0%	0%	
Substantial Noncompliance	1%	1%	0%	0%	0%	0%	0%	0%	
(Number of banks)	107	1356	331	197	82	288	96	148	
2003									
Outstanding	10%	4%	11%	17%	17%	12%	25%	29%	
Satisfactory	90%	95%	88%	81%	83%	87%	75%	71%	
Needs to Improve	0%	1%	1%	1%	0%	1%	0%	0%	
Substantial Noncompliance	0%	0%	0%	0%	0%	0%	0%	0%	
(Number of banks)	188	1363	326	138	64	273	91	48	
2002									
Outstanding	13%	1%	11%	15%	26%	11%	18%	18%	
Satisfactory	86%	98%	89%	84%	74%	88%	82%	79%	
Needs to Improve	0%	1%	1%	1%	0%	2%	0%	3%	
Substantial Noncompliance	0%	1%	0%	0%	0%	0%	0%	0%	
(Number of banks)	223	780	297	160	95	238	101	97	
2001									
Outstanding	6%	3%	9%	4%	20%	13%	32%	22%	
Satisfactory	93%	94%	91%	84%	79%	86%	68%	72%	
Needs to Improve	1%	3%	0%	8%	0%	2%	0%	6%	
Substantial Noncompliance	1%	1%	0%	4%	1%	0%	0%	0%	
(Number of banks)	177	352	172	51	100	181	71	107	

Source: FFIEC website

Appendix B

November 16, 2010 FDIC Teleconference on Fair Lending Issues
Questions and Answers (Posted January 2011)

1. Are we required to gross up non-taxable income. For example, a person on social security who only gets $12,000 a year, would we need to gross this income up by 1.20% to ensure fair lending?

Answer: While it is not required that an institution gross up non-taxable income, Fannie, Freddie and FHA all allow a gross up factor of 25% on this type of income. (Or alternatively you may use the current federal and State income tax withholding tables.) The decision to use this factor is discretionary. However, it is important that if you decide to gross up income, in order to avoid any appearance of a fair lending violation, ALL similar types of non-taxable income should be grossed up and in a similar manner.

2. I have three questions:
A) How are examiners treating banks / financial institutions that have decreased their loan production?
B) Are there additional tools / resources other than the FFIEC Interagency Guidance?
C) Are you aware of specific training targeting "Fair Lending?"

Answer: A) Examiners recognize that the economic climate has caused many institutions to decrease their lending or number of loan products. This is not a fair lending concern on its face, provided that the loans the institution does make are made in a manner that does not treat members of protected classes differently or made under policies that have a disparate impact on protected classes.
B & C – The FDIC does not endorse any particular tool, product or training that is available; however, trade associations are a good resource to find out what trainings are available. Also, in addition to the FFIEC Interagency Fair Lending Procedures, make sure you are aware of any guidance issued by your regulator.

3. I noticed the "Hot Topics" section of the presentation did not include any specific loan servicing or default area. Are there specific areas (Collections, Loss Mitigation, and Customer Service) that we should be concerned with or be proactively monitoring?

Answer: All of these areas should always be monitored to ensure fair and equitable treatment. Please refer to the FFIEC Fair Lending Examination Procedures for more detail.

4. Our bank is entering into a relationship with a mortgage broker whereby the broker will be processing the majority of our approved requests and the bank will be responsible for declining requests that do not meet the broker's criteria. The result will be that the vast majority of our LAR will be non-originations. Is there advice you can offer as to how to present this to our examiners?

Answer: It is important to first identify who is the creditor (under HMDA) in this new business arrangement. You can use the "HMDA Reporting - Getting It Right!" Guide to make sure you are reporting these applications properly on the LAR. Once you verify that the LARs are correct, there should not be a problem explaining the business arrangement to the examiners.

5. Only one product is originated in both our Secondary Market Channel and In-House Channels. If the customer expresses an interest in a 15 or 30 year fixed rate product they would have to go to the Secondary Market channel. However, our In-house Channel offers a similar product with a 5 year balloon. Does the bank need to underwrite the In-House product as an option for the customer, although the customer did not express an interest in the 5-year balloon?

Answer: It would not be necessary to underwrite the balloon loan for the customer unless the customer expresses an interest in such product. However, to ensure all applicants have equal access to credit, it would be advisable to make sure the customer is aware of the balloon option and then document the fact that the customer chose the secondary market product over the balloon loan.

6. What is the Ethnicity and Race for Iranian borrowers?

Answer: According to the US Census Bureau, there is no wrong or right answer to identifying a person's race and ethnicity. You can research this on the US Census website. Census data relies strictly on self identification, according to the race or races with which they most closely identify. Persons who report themselves as Hispanic can be of any race. Self-identification of a person's race and ethnicity does not need to conform to any biological, anthropological, or genetic criteria. For HMDA purposes, you should report the ethnicity and race as each applicant identifies themselves in the Government Monitoring Information on the application. If you need to use visual observation to report race and ethnicity for Regulations B & C, then, the identification of the applicant's race and ethnicity would be left to the interviewer's observation of the borrower.

7. We use the Appraisal Date as the Application Date -- Can we be off by a day or two in reporting Application Dates? Is it OK to use the Date of the Note as the Action Date or do we have to use the funding date?

Answer: We recommend that you get a copy of "A Guide to HMDA Reporting – Getting It Right!" for 2010 HMDA reporting. You can download this guide from the FFIEC website. As long as you follow the guidance in HMDA Getting It Right!, you should not have any problems explaining to examiners how or why you reported HMDA data as you did.

Specifically, the Guide states in appendix A (I.A.2.a) the application date should be reported as the date the loan application was received by your institution or the date shown on the application. Therefore, if you received the completed application on the date of the appraisal, then you could use the appraisal date as the application date.

Appendix D reads as follows regarding the action taken date:

For loan originations, an institution generally reports the settlement or closing date. For loan originations that an institution acquires through a broker, the institution reports either the settlement or closing date, or the date the institution acquired the loan from the broker. ***If the disbursement of funds takes place on a date later than the settlement or closing date, the institution may use the date of disbursement.*** For a construction/ permanent loan, the institution reports either the settlement or closing date, or the date the loan converts to the permanent financing. Although an institution need not choose the same approach for its entire HMDA submission, it should be generally consistent (such as by routinely using one approach within a particular division of the institution or for a category of loans). Notwithstanding this flexibility regarding the use of the closing date in connection with reporting the date action was taken, the year in which an origination goes to closing is the year in which the institution must report the origination.

8. In the past, banks have allowed discretionary pricing on consumer loans, including mortgages, based on relationship or to match a competitor's rate or fees. Should this practice be discontinued? What advice can you give to help us stay in compliance from a fair lending perspective, but still be able to take care of customers who have been loyal to us?

Answer: Allowing discretion in pricing is not a prohibited practice, but it does expose an institution to increased fair lending risk. The general principle is that more discretion equals greater risk. If an institution allows discretionary pricing, it raises a "red flag" for examiners, and it will always be closely reviewed during examinations.
An institution that allows discretionary pricing should establish monitoring mechanisms to ensure that pricing is not unfairly impacting any particular prohibited basis group. For example, this monitoring could occur by conducting comparative file reviews or by closely tracking pricing deviations through an exception report. Furthermore, maintaining documentation of the reason for the pricing deviation is pertinent in the event that questions are raised. Additionally, an institution should have regular training for its employees so everyone has a clear understanding of not only the institution's policies and procedures, but also the fair lending laws and regulations.

9. I saw in the recent FIL 47-2010 regarding overdraft legislation that "inconsistent application of waivers of overdraft fees will be evaluated in light of fair lending statutes and legislations." Our understanding in the past was that overdraft was not a Fair Lending concern as these programs qualified under the "incidental credit" exclusion (Reg. B). Does this mean that regulators are going to have a broader interpretation of Fair Lending than they have had in the past? If so, what other areas would you expect that Fair Lending will be expanded to include?

Answer: The FDIC's position that overdraft programs are subject to ECOA is neither a broader interpretation of fair lending nor is it new. FIL-47-2010 merely reiterated the same position that had been previously stated in prior supervisory issuance by the Federal Reserve, the FDIC, and other federal regulatory agencies.

FIL-47-2010 provides in relevant part: The FDIC will take supervisory action where overdraft payment programs pose unacceptable safety and soundness or compliance management system risks **or result in violations of laws** or regulations, **including** unfair or deceptive acts or practices and **fair lending laws**. (Emphasis added).

The statement merely reiterates previous statements of the same principle made in multiple regulatory issuances including but not limited to:

1. FRRS Joint Guidance on Overdraft Protection Program, FRRS 3-1579.43, 2006 3928977 effective Jan 1. 2010.
2. Joint Guidance on Overdraft Protection Programs issued by OCC, FED, FDIC, and NCUA, 70 FR 9127, 2005 WL 420970, Feb. 24, 2005.

With that said, not all overdraft protection plans qualify as "incidental credit." For example, plans where bank customers opt into the plan in writing do not constitute "incidental credit." *See* 12 C.F.R. §226.4(c).

10. I am an independent compliance consultant that works with various banks helping them with Fair Lending reviews and risk assessments. Do you see any problem with me using information from borrowers' drivers licenses that are stored in the bank's Customer Information System to obtain demographic information for fair lending analysis such as age, sex, and possibly race? As you know, the government monitoring information is only available for HMDA-covered loans. If I am trying to conduct fair lending analyses on other types of loans, such as consumer loans or vehicle-secured loans, there isn't much to go on other than making assumptions about race via surnames and gender via first names. If I could use information from the drivers license that is imaged and in the bank's system, I could get demographic information without having to make assumptions.

Do you see any problem with doing that? I am independent from the bank and this is done after the loan decision has been made (these are existing loans). To go one step further, would this be OK for a bank's compliance officer to do too, if that person is independent from the lending function and it's done after the loan decision has been made?

Answer: Regulation B does not prohibit the practice of photo copying or digitally storing photo identification, but it does prohibit the collection of certain demographic information. Given that photo identification usually contains this prohibited information, it is a best practice not to retain a copy of the photo identification. However, if a bank chooses to retain a copy of photo identification, it is best if it is segregated from loan files. Furthermore, the photo identification should only be requested to comply with the USA Patriot Act and not be used as part of the underwriting process.

Keeping the above in mind, photo identification that is available in a customer information system could be used to obtain demographic information to assist in a fair lending analysis. As stated in the question, it would be a more accurate way to conduct the analysis than making assumptions based on factors such as surnames.

11. We are a small community bank and we contract with a third party for independent review of our Fair Lending and have recently had a Fair Lending Risk Assessment completed. To my knowledge, our bank has not been cited for Fair Lending infractions.
My questions:
1. Are small banks required to have an internal audit program for Fair Lending?
2. If so, where can we find information to design an internal audit program for Fair Lending?

Answer: Each FDIC-supervised bank is expected to have a compliance management system (CMS) that appropriately manages all compliance risks, including fair lending risks. There is not a "one-size fits all" approach for a CMS to be effective because every institution is unique in size, demographics, product offerings, etc. Two components of an effective CMS are monitoring and audits of all business areas of a bank to ensure compliance with all laws and regulations, including fair lending.
In the question it states that the subject bank is a small institution that has contracted with a third party for an independent fair lending review. It also states that a fair lending risk assessment has been

performed. If the scope of the third-party fair lending review and risk assessment are comprehensive and no major exceptions were identified as a result, an additional internal fair lending audit is likely not warranted. Otherwise if risk factors or exceptions are identified, examiners would likely expect the bank to perform some type of internal review to investigate any concerns and take appropriate action. The best course of action will be dependent on the results of a third-party review and risk assessment. For the second question, the Interagency Fair Lending Procedures outline the process examiners use when reviewing an institution's fair lending program. Becoming familiar with these procedures would serve as a good starting point for designing an internal fair lending audit program which should be tailored to the business activities and risks of the institution.

12. Where would we find the information to determine if we have minority census tracts in our market area?

Answer: Demographic information is available on the Federal Financial Institutions Examination Council (FFIEC) website located at www.ffiec.gov. On the main page of the website, click on the link for "Census Reports" under the Consumer Compliance heading. Through this link you can produce reports for specific states either at the MSA or county level. The reports provide demographic information on the minority population for each census tract in the chosen area as well as for other factors such as median family income.

13. From a statistical point of view, isn't it the case that the more finely a set is divided, the more likely that one subset will represent a deviation from the norm? In other words, if the average (or median) for 100 items is, say, 75 then the odds of one of two subsets composed of, say, 40 and 60 items' deviating from the average or median by 25% (pick your percentage) is much lower than the odds of one of 25 subsets so deviating? Applied to Fair Lending, the odds of deviating from the norm are greater the more protected classes there are. Do the regulators take this into account, or doesn't it matter in their analysis?

Answer: This question assumes we are talking about something that naturally has variation, such as the height of the population. If we were to draw a random sample of 1/10 of the population versus a random sample of 1/100 of the population, there is indeed a greater likelihood that the smaller sample will deviate from the averages of the full population.

For fair lending and pricing in particular, we are comparing the adjusted mean interest rate (adjusted for all the pricing control factors) for the control group to the adjusted mean interest rate of the target group. After all the adjustments, which should reflect all the pricing factors used by the bank, we expect that the adjusted mean interest rates should be the same for both control and target group (i.e. there is no statistically significant difference). It does not matter how many target groups there are because there should be no statistically significant differences between the means of ANY target group and the control group once all the pricing factors have been controlled for.

14. On average, once the data gathering phase is completed, and all data required is provided to the FDIC, how long does it take the FDIC to issue the 15-day letter?

Answer: Once the FDIC has all of the data it needs to complete its review, it typically takes 60-90 days to issue a 15-day letter, if one is required.

15. Please provide information on how many outliers are reviewed each year v. the number of HMDA reporting institutions v. the number that are referred to DOJ for discrimination?

Answer: The FDIC has identified approximately 200 outlier institutions since pricing data was first reported in 2004 and in the past five years, has made 110 referrals to the Department of Justice based on findings of discrimination (29 in 2006, 15 in 2007, 12 in 2008, 21 in 2009 and 33 in 2010). For information about the number of HMDA reporting institutions, please visit the FFIEC's website.

16. Do the other regulatory authorities use the same practices in identifying outliers and conducting outlier reviews?

Answer: Each agency has its own screening process and outlier review process.

17. Is there a matrix of some kind that can be used to list all loans with the required items that need monitoring?

Answer: There is no such matrix but please refer to the FFIEC Interagency Fair Lending Procedures for guidance regarding what areas of risk examiners will review during a fair lending review.

18. We want to break down our HMDA information so that we can report it to the Board of Directors. Is there a program or software that can help us with this?

Answer: There are various programs that are available that assist banks in analyzing their HMDA data. The FDIC does not endorse any particular program but does encourage its banks to monitor its HMDA data.

19. The institution I work for is located in a low/mod income community. Many of the mortgage requests are for loans under $50,000. Can we set a minimum loan amount on the mortgages we offer without violating fair lending laws?

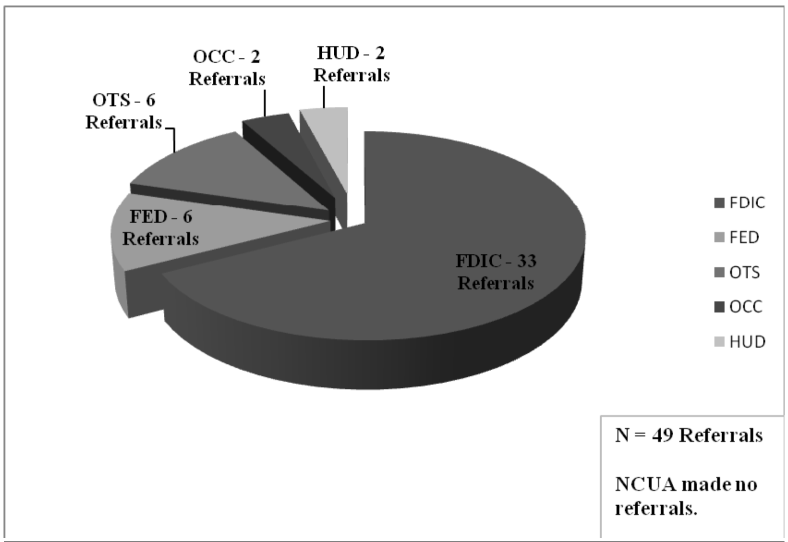
Answer: Setting any sort of limits on lending should always be reviewed for possible fair lending concerns. In the situation you describe above, we would advise the institution to determine whether such a practice has a disparate impact on a protected class and if so, whether there is a legitimate business reason for such practice. This will be the same sort of analysis that our examiners will conduct during an examination and thus the institution would be wise to conduct this analysis beforehand to ensure there are no concerns.

Appendix C

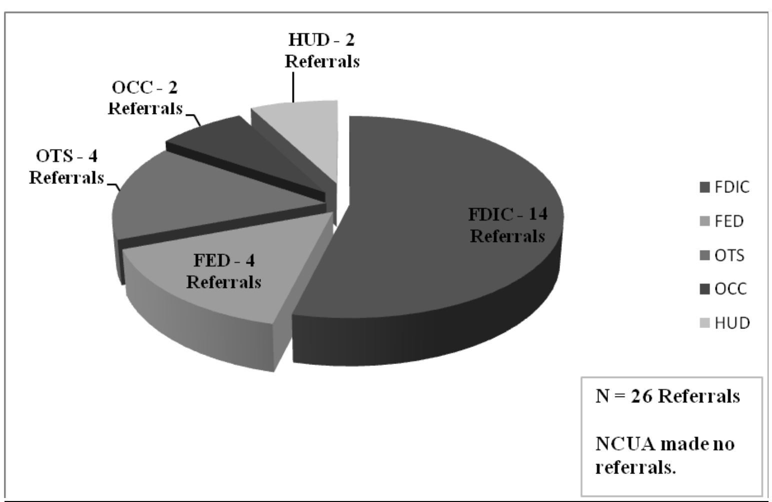
Referrals to DOJ

In 2010, DOJ received 49 fair lending referrals involving potential ECOA claims from the bank regulatory agencies and HUD, the largest number in more than a decade. The referrals included:

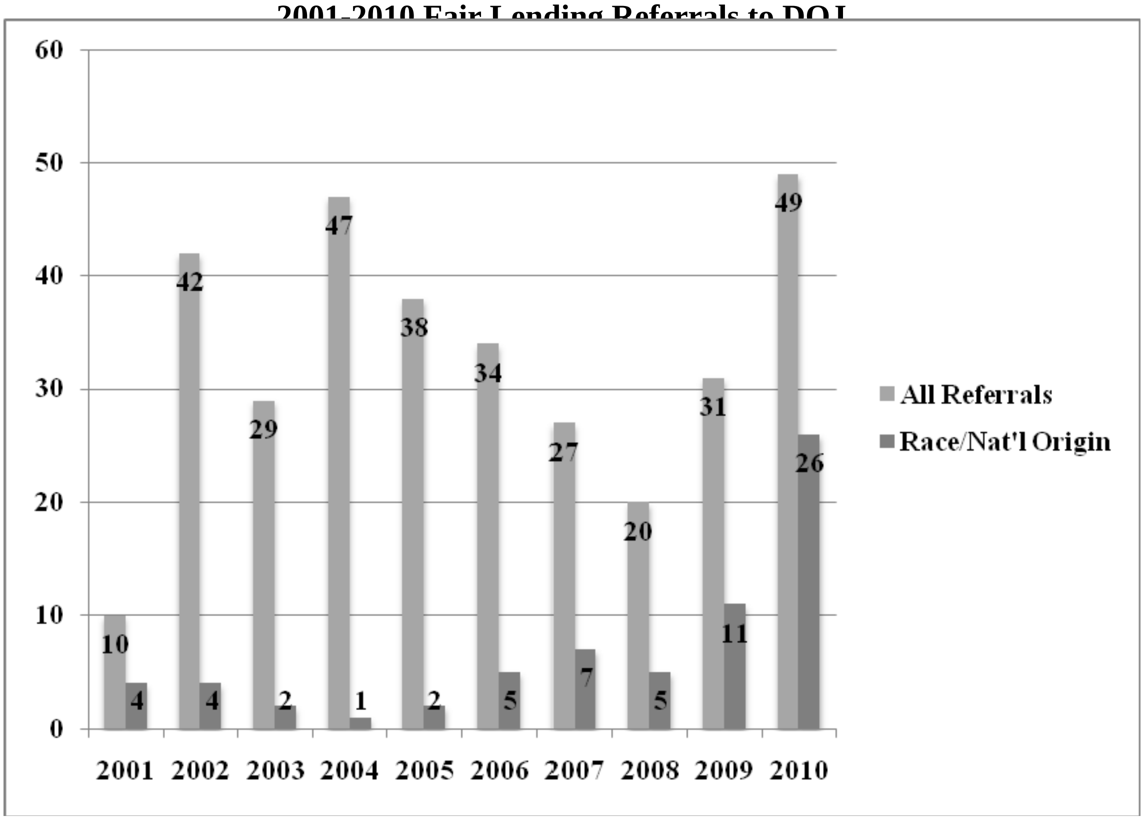
- 33 referrals from the Federal Deposit Insurance Corporation (FDIC);
- 6 referrals from the Federal Reserve Board (FRB);
- 6 referrals from the Office of Thrift Supervision (OTS);
- 2 referrals from the Office of the Comptroller of the Currency (OCC);
- None from the National Credit Union Administration (NCUA); and
- 2 referrals from HUD.



2010 Fair Lending Referrals to DOJ Involving Race & National Origin Discrimination



2001-2010 Fair Lending Referrals to DOJ[11]



[11] The data on this chart is presented in spreadsheet form at page 16 of this report.

Analysis of Referrals to DOJ for the Past 10 Years

ALL REFERRALS	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	Total
FDIC	33	21	12	15	29	35	42	29	33	5	**254**
FRB	6	6	3	9	5	2	3	0	6	1	**41**
OTS	6	4	4	3	0	0	1	0	0	1	**19**
OCC	2	0	1	0	0	0	0	0	1	3	**7**
NCUA	0	0	0	0	0	0	—	—	—	—	**0**
HUD	2	0	0	0	0	1	1	0	2	—	**6**
Total	**49**	**31**	**20**	**27**	**34**	**38**	**47**	**29**	**42**	**10**	**327**

Race/Nat'l Origin Discrimination	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001	Total
FDIC	14	5	2	1	3	1	0	2	1	2	**31**
FRB	4	3	0	4	2	0	0	0	1	1	**15**
OTS	4	3	3	2	0	0	0	0	0	1	**13**
OCC	2	0	0	0	0	0	0	0	0	0	**2**
NCUA	0	0	0	0	0	0	—	—	—	—	**0**
HUD	2	0	0	0	0	1	1	0	2	—	**6**
Total	**26**	**11**	**5**	**7**	**5**	**2**	**1**	**2**	**4**	**4**	**67**

"—" indicates there was no reference to the agency in that year's ECOA report.

NOTE:

As of December 31, 2010, DOJ had returned 28 of the 47 bank agency 2010 referrals for administrative resolution, or more than 59 percent.

Other DOJ Referral Considerations

In 1996, upon the recommendation of the General Accounting Office, DOJ provided guidance to the federal bank regulatory agencies on pattern or practice referrals. That guidance described the factors that DOJ would consider in determining which matters it would return to the agency for administrative resolution and which it would pursue for potential litigation. While numerous factors are considered, referrals that are most likely to be returned generally have the following characteristics:

- The practice has ceased and there is little chance that it will be repeated;
- The violation may have been accidental or arose from ignorance of the law's more technical requirements, such as spousal signature violations and minor price breaks for certain age groups not entitled to preferential treatment; and
- There either were few potential victims or *de minimis* harm to any potential victims.

Referrals that would likely be considered for litigation by the Department are referrals that do not meet the criteria set forth above, and have one or more of the following characteristics:

The practice is serious in terms of its potential for either financial or emotional harm to members of protected classes (for example, discrimination in underwriting, pricing, or provision of lender services):

- The practice is not likely to cease without court action;
- The protected class members harmed by the practice cannot be fully compensated without court action;
- Damages for victims, beyond out-of-pocket losses, are necessary to deter the lender (or others like it) from treating the cost of detection as a cost of doing business; or
- The agency believes the practice to be sufficiently common in the lending industry, or raises an important issue, so as to require action to deter lenders.

Focusing on CRA and Fair Lending Risk

CRA Assessment

Performing a CRA self assessment helps gauge a financial institution's lending performance and how well the institution is serving its community. This vital information can help the Board and management avoid surprises and possible poor ratings during the next exam. A CRA self assessment can show whether an institution's performance or processes could appear weak to examiners. It is a key to ensuring the institution's CRA rating is satisfactory or better!

Dig in with a CRA self assessment and get answers to these tough questions:

- How do we know our institution's lending performance is adequate?
- What amount of lending is inside versus outside of our assessment area?
- Are we using the right benchmarks to compare our institution's performance?
- Does our institution have products that meet the needs of our community?
- How does the institution market our products?
- How will fair lending impact our exam?
- Are our assessment area(s) delineated properly?
- How solid is our institution's HMDA/CRA data collection and testing process?
- Is our HMDA/CRA data accurate? Are we within tolerance?

A self assessment will uncover the answers to these questions by reviewing the following:

- Lending distribution
- Peer analysis
- Performance context data**
- Qualifying community development loans
- Highlighting services
- Qualifying investments

Gathering and evaluating this information is a solid way to gauge future performance and see how the story unfolds. Knowing this information will better position the institution for the next exam.

**To provide a complete picture of an institution's CRA performance, quite often CRA staff decide to prepare a performance context narrative.

Focusing on CRA and Fair Lending Risk

Fair Lending Assessment

Performing a fair lending self-assessment helps gauge a financial institution's fair lending performance. This type of assessment assists the Board and management to ascertain the bank's fair lending posture, and to avoid surprises during the next exam. The fair lending self-assessment can show whether an institution's performance or processes could appear weak to examiners.

In concluding a fair lending self-assessment, management receives specific focused feedback on:

- Marketing and advertising materials
- Loan policies and underwriting standards
- Application process, including forms
- Loan decision process
- Denial reviews
- Complaint correlation versus denials

A self assessment will uncover the answers to these questions by reviewing the following:

- Request compliance staff and/or internal audit staff to perform technical compliance reviews for each of the following regulations:
    - ECOA (Equal Credit Opportunity Act)
    - HMDA (Home Mortgage Disclosure Act)
    - FHA (Fair Housing Act)
    - CRA (Community Reinvestment Act)
    - UDAP (Unfair or Deceptive Acts or Practices

  Also, consider the Servicemembers Civil Relief Act, Fair Credit Reporting Act, and Appraisal points.

- Conduct self-testing of fair lending practices to determine where weaknesses exist and to address those weaknesses through improved policies, procedures, and training. The bank may also establish a formalized self-test program per Regulation B. Under this program, information regarding an applicant's personal characteristics may be gathered and analyzed for the purposes of monitoring and improving compliance with the Act. This information cannot be used for any other purpose (e.g., the credit decision or marketing efforts) and must be analyzed on a timely basis. Any likely violations uncovered by the self-test should be remedied.

- Engaging an independent third-party to perform a fair lending assessment.

Appendix D

Quantity of Fair Lending Risk Indicators—MACRO OVERVIEW

Reviewers should use the following indicators, as appropriate, when assessing the quantity of fair lending risk.

Low Risk =Rate 1 or 2	Moderate Risk = Rate 3 or 4	High Rate = Rate 5 to 6	Rating
Significant and explainable volume of consumer lending.	Lower volume of consumer lending, but explainable.	Low and unexplainable volume of consumer lending. (Bank could be discouraging applicants.)	
Generic, non-complex products offered.	Limited number of complex products offered. Mix of products change occasionally.	Several complex products offered (e.g., sub-prime high cost mortgages, etc.). Prime and subprime products offered appear similar.	
Low number of policy exceptions/overrides.	Modest number of policy exceptions/overrides. May exceed guidelines.	High number of policy exceptions/overrides.	
Lending policies allow little or no subjective factors (loan officer judgment, discretionary pricing, fees, etc.).	Lending policies allow some subjective factors.	Lending policy allows a high level of subjective decision-making factors.	
Little or no disparities among approval/denial rates by prohibited basis groups.	Some disparities among approval/ denial rates by prohibited basis groups.	Substantive disparities among approval/denial rates by prohibited basis groups.	
Low proportion of withdrawn/incomplete applications for prohibited basis groups.	Moderate proportion of withdrawn/incomplete applications for prohibited basis groups.	Higher portion of withdrawn/incomplete applications for prohibited basis groups.	
No conspicuous gaps in lending patterns identified.	Conspicuous gaps in lending patterns identified are explainable.	Conspicuous gaps in lending patterns identified are not explainable.	
Bank originates its own consumer loans. Bank has no broker relationships (centralized underwriting).	Low volume of consumer loan is originated by local brokers.	High volume of consumer loans is originated by multiple statewide or nationwide brokers (decentralized underwriting).	
No marketing practices or products that are targeted to any specific group or location.	Limited marketing practices or products that are targeted to specific groups. Activity is commensurate with strategic focus.	Marketing practices or products are targeted to specific groups or locations, e.g., advertising subprime or higher cost consumer loans in a language other than English.	
No special purpose credit programs, i.e., a program primarily for an economically disadvantaged group.	One special purpose credit program.	Several special purpose credit programs.	
No fair lending complaints or complaints to DOJ or HUD regarding discrimination or discouraged applications.	Limited number of fair lending related complaints.	Numerous fair lending related complaints.	
No fair lending lawsuits or claims regarding discrimination or discouraged applicants.	Community groups have raised fair lending issues. Some potential lawsuits, e.g., allegations of predatory lending.	Actual fair lending lawsuits or claims. Any investigations of fair lending complaints by DOJ or HUD.	
		Average Total Risk	

(***Insights***: If average total risk is 2.5 or higher, then risk level is moderate.)

Quality of Fair Lending Risk Management—MACRO OVERVIEW

Reviewers should use the following indicators, as appropriate, when assessing the quality of fair lending risk management.

Low Risk =Rate 1 or 2	Moderate Risk = Rate 3 or 4	High Rate = Rate 5 to 6	Rating
Bank conducts an effective fair lending risk analysis. Results are discussed with the BOD. (Determined via discussion with management. It is not necessary for bank to share results).	Bank conducts a fair lending risk assessment but system is flawed. (Determined via discussion with management. It is not necessary for bank to share results.)	Little or no monitoring of fair lending compliance.	
Centralized decision making with ongoing monitoring for consistency. Bank adheres to well-defined underwriting standards and override procedures.	Bank generally adheres to underwriting standards and override procedures.	Decentralized decision making without monitoring of: • Discretionary pricing • Overrides • Policy exceptions	
Bank has an effective second review process in place.	Bank has implemented an informal second review process (e.g., inconsistent consideration of denied applications, exceptions, and/or overrides.	No second review process.	
Fair lending considerations are incorporated into all areas of the bank, i.e., roll out of new products, advertising, changes in forms, disclosures, etc.	Fair lending considerations sometimes overlooked and not incorporated into all areas of the bank. Management effects corrective action when identified.	Fair lending considerations are not incorporated in numerous areas of the bank. Management does not effect corrective action.	
Policies and procedures are adequate.	Policies and procedures are generally adequate but certain weaknesses were noted.	Policies and procedures are significantly flawed and do not provide sufficient guidance as to why business reasons or other factors are not discriminatory.	
When deficiencies are identified, management promptly implements meaningful corrective action.	Management is responsive when deficiencies are identified in the normal course of business or second review.	Errors and deficiencies are not self-identified. Management may only respond when violations are cited.	
Training to ensure consistent treatment is appropriate and effective. Necessary resources have been provided to ensure compliance. Experienced, well-trained and knowledgeable staff.	Training is conducted, but is conducted infrequently or is not timely. Management might not provide adequate resources and employee turnover may be high.	Training is sporadic and ineffective, e.g., as evidenced by inconsistent application of underwriting standards, high volume of withdrawn/incomplete applications may indicate bank is discouraging applicants.	
Bank is responsive and resolves complaints promptly when received.	In general, complaints are promptly and adequately addressed.	Management does not monitor or adequately and promptly address complaints.	
Appropriate fair lending compliance controls and systems (e.g., quality control functions, compliance audits, and self-assessments) are implemented to identify compliance problems and assess performance.	No shortcomings of significance are evident in fair lending compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). The probability of serious future violation or noncompliance is within acceptable tolerance.	Shortcomings of significance are evident in fair lending compliance controls or systems (e.g., quality control functions, compliance reviews, compliance audits, and self-assessments). The probability of serious future violation or noncompliance is NOT within acceptable tolerance.	
		Average Total Risk	

Appendix E

Fair Lending Risk Indications Checklist

The following checklist is based on the interagency fair lending examination procedures, which identify indicators of risk factors for potential discriminatory patterns and practices. Each "no" answer should serve as a red flag for an institution's compliance management because it suggests that a possible discrimination issue exists within the institution's lending program.

Indicators of Overt Discrimination	**Yes**	**No**	**N/A**
1. Does the institution refrain from including explicit prohibited-basis identifiers in underwriting criteria or pricing standards?	_____	_____	_____
2. Does the institution collect only the information allowed under the provisions of Regulation B (i.e., race and gender for purchase money mortgages) and Regulation C, HMDA-reportable applications?	_____	_____	_____
3. Does the institution's credit scoring system exclude the variables that represent a prohibited basis or factor under Regulation B or, for residential loan scoring systems, the Fair Housing Act?	_____	_____	_____
4. Do the institution's officers, employees, or agents refrain from making statements that constitute an express or implicit indication that one or more such persons have engaged or do engage in discrimination on a prohibited basis in any aspect of a credit transaction?	_____	_____	_____
5. Does the institution refrain from making statements and/or disallow employees to make statements that suggest the existence of attitudes based on prejudices or stereotypes of protected-class members?	_____	_____	_____
Indicators of Potential Disparate Treatment in Underwriting			
1. For an institution that reports HMDA data, do the institution's data reveal *no* substantial disparities among the approval/denial rates for protected-class applicants compared to those for nonprotected-class applicants?	_____	_____	_____
2. For an institution that reports HMDA data, do the institution's data reveal *no* substantial disparities among the application processing times for protected-class applicants compared to those for nonprotected-class applicants?	_____	_____	_____
3. For an institution that reports HMDA data, do the institution's data reveal a substantially *similar* proportion of withdrawn/incomplete applications from protected-class applicants compared to those from nonprotected-class applicants?	_____	_____	_____

Fair Lending Risk Indications Checklist (cont.)

	Yes	No	N/A
4. Are the institution's underwriting criteria clear and clearly communicated to all relevant personnel?	_____	_____	_____
5. Does the institution offer its employees clear guidance on making exceptions to its underwriting criteria, including credit scoring overrides?	_____	_____	_____
6. Does the institution require the reasons for exceptions to normal underwriting standard, including credit scoring overrides, to be documented consistently in all affected loan files?	_____	_____	_____
7. Do the institution's lending decisions generally support the validity of the underwriting criteria (i.e., are there relatively low percentages of either exceptions to underwriting criteria or overrides of credit score cutoffs)?	_____	_____	_____
8. Does the institution refrain from compensating loan officers or brokers based on loan volume, particularly loans approved per period of time?	_____	_____	_____
9. Does the institution promptly investigate and respond to any consumer complaints alleging discrimination in loan processing or in approving/ denying loans?	_____	_____	_____
Indicators of Potential Disparate Treatment in Pricing (interest rates, fees, or points)			
1. Does the institution refrain from establishing a relationship between loan pricing and the compensation of officers or brokers (e.g., overages)?	_____	_____	_____
2. Does the institution maintain and enforce consistent parameters to guide lender discretion in pricing or other transaction costs and/or does the institution limit the discretion of lenders in pricing or other transaction costs?	_____	_____	_____
3. If the institution uses a system of risk-based pricing, is the system verifiably empirically based and statistically sound?	_____	_____	_____
4. If the institution is a HMDA reporter, do the institution's data reveal that there are no substantial disparities among prices being quoted or charged to protected-class applicants compared to nonprotected-class applicants?	_____	_____	_____
5. Does the institution investigate and promptly respond to consumer complaints alleging discrimination in loan pricing?	_____	_____	_____

Fair Lending Risk Indications Checklist (cont.)

	Yes	No	N/A
Indicators of Potential Disparate Treatment by Steering (Residential Lending)			
1. For institutions with one or more subprime mortgage subsidiaries or affiliates, are there no significant differences, by loan product, in the percentage of protected-class applicants of the institution compared with the percentage of protected-class applicants of the subsidiaries or affiliates?	_____	_____	_____
2. For an institution with one or more subprime mortgage subsidiaries or affiliates, does the institution have clear, objective standards for:			
• Referring applicants to its subsidiaries or affiliates?	_____	_____	_____
• Classifying applicants as prime or subprime borrowers?	_____	_____	_____
• Deciding what kinds of alternative loan products should be offered or recommended to applicants?	_____	_____	_____
3. For an institution that offers both conventional mortgage loan products and FHA mortgages, does the institution's record of lending demonstrate *no* significant differences in the percentages of protected-class applicants in each of these two loan products, particularly with respect to loan amounts of $100,000 or more, compared to percentages of originations of these two loan products to nonprotected-class applicants?	_____	_____	_____
4. For an institution that makes both prime and subprime loans for the same purpose, does the institution's record of lending demonstrate no significant differences in the percentages of protected-class borrowers in each of the alternative loan product categories?	_____	_____	_____
5. Does the institution investigate and respond promptly to consumer complaints alleging discrimination in loan pricing?	_____	_____	_____
• If the institution operates a subprime mortgage company subsidiary or affiliate, has the institution integrated loan application processing for both entities?	_____	_____	_____

Note: Integrated loan application processing may allow seamless steering between subprime and prime products (e.g., a single loan processor could simultaneously attempt to qualify an applicant, whether to the bank or the mortgage company, under either the bank's prime criteria or the mortgage company's subprime criteria).

Fair Lending Risk Indications Checklist (cont.)

	Yes	No	N/A
6. Does the institution limit loan officer discretion regarding whether to promote conventional or FHA loans, or both, to applicants and/or has the institution issued guidelines regarding the exercise of loan officer discretion?	_____	_____	_____
7. For an institution with a subprime mortgage affiliate or subsidiary, are the institution's branch offices just as accessible to (or located in) predominantly minority neighborhoods as the subprime mortgage affiliate or subsidiary's offices?	_____	_____	_____
Indicators of Potential Redlining (Residential Lending)			
1. For an institution that reports HMDA data, do the institution's data reflect no significant differences in the number of loans originated in those areas in the lender's market that have relatively high concentrations of minority residents compared with areas with relatively low concentrations of minority residents?	_____	_____	_____
2. Do the institution's lending data reveal *no* significant differences between approval/denial rates for all applicants (minority and nonminority) in areas with relatively high concentrations of minority residents compared with areas with relatively low concentrations of minority residents?	_____	_____	_____
3. Do the institution's lending data reveal *no* significant differences between denial rates based on insufficient collateral for applicants from areas with relatively high concentrations of minority residents?	_____	_____	_____
4. Do the institution's lending data reveal *no* substantial differences in patterns of lending that differ by the concentration of minority residents?	_____	_____	_____
5. Does the institution refrain from explicitly excluding MSAs, political subdivisions, census tracts, or other geographic areas within the institution' lending market that have relatively high concentrations of minority residents from its efforts to originate any or all of its credit products?	_____	_____	_____
6. Do the institution's policies on receipt and processing of applications, pricing, conditions, appraisals and valuation, or any other aspect of providing residential credit apply to all areas within the lender's market regardless of the concentration level of minority residents?	_____	_____	_____
7. Do the institution's officers, employees, or agents refrain from making statements that reflect an aversion to doing business in areas with relatively high concentrations of minority residents?	_____	_____	_____

Fair Lending Risk Indications Checklist (cont.)

	Yes	No	N/A
8. Does the institution investigate and respond promptly to complaints or allegations by consumers or community representatives that the institution excludes or restricts access to credit for areas with relatively high concentrations of minority residents?	_____	_____	_____
9. For an institution with a subprime mortgage subsidiary or affiliate, are the institution's branch offices just as accessible to (located in) predominantly minority neighborhoods as the offices of the subprime subsidiary?	_____	_____	_____
Indicators of Potential Disparate Treatment in Marketing (Residential Lending)			
1. Does the institution refrain from using advertising media, messages, or practices that a reasonable person would believe indicate that members of protected classes are less desirable as customers?	_____	_____	_____
2. Does the institution advertise in media that serves all population segments, including minority residents, within its market?	_____	_____	_____
3. Does the institution market through brokers or other agents that the lender knows (or has reason to believe) serve all racial or ethnic groups present in the market?	_____	_____	_____
4. Does the institution refrain from using marketing programs or procedures for residential loan products that exclude one or more regions or geographies within the lender's assessment or marketing area that have significantly higher percentages of minority residents than the remainder of the assessment or marketing area?	_____	_____	_____
5. Does the institution refrain from using mailing or other distribution lists or other marketing techniques for prescreened or other offerings of residential loan products that explicitly exclude groups of prospective borrowers on a prohibited basis or exclude geographies within the institution's marketing area that have significantly higher percentages of minority residents than the remainder of the marketing area?	_____	_____	_____
6. Do the institution's lending data reveal that the proportion of monitored prohibited-basis applicants is relatively consistent with that group's representation in the total population of the market area?	_____	_____	_____
7. Does the institution investigate and respond promptly to consumer complaints alleging discrimination in advertising or marketing loans?	_____	_____	_____

Update Regarding Implementation of The Dodd-Frank Wall Street Reform and Consumer Protection Act

James W. Morrissey
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Passage of Dodd-Frank Act

- The Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act" or "Dodd-Frank") was signed into law on July 21, 2010
- Dodd-Frank was enacted in response to the financial meltdown in 2008-2009 and was the focus of broad media attention
- The Act was meant to address high-risk practices that were deemed to have been a cause of the meltdown and enable federal regulators to better regulate financial institutions and prevent a similar meltdown from occurring in the future
- Many headlines associated with the Act – End of "Too Big to Fail"; Volcker Rule; Say on Pay Rules; Consumer Finance Protection Bureau; Stress Tests – focused on larger institutions

continued

Passage of Dodd-Frank Act

- In fact, a number of trade groups representing smaller community banks generally supported the Act given its expected impact on larger institutions
- Although the Act contains a number of provisions dealing with larger financial institutions, it has had an impact on community banks as well
- The Act requires the federal banking agencies to develop and implement hundreds of new regulations, many of which will directly or indirectly impact community banks

continued

Passage of Dodd-Frank Act

- Although the Act itself is extremely voluminous, it grants broad discretion to the federal banking agencies, as well as the SEC and CFTC, to interpret and implement many provisions
- The Act requires approximately 380 new rules to be implemented. To date, fewer than half the rules have been proposed or promulgated
- The agencies have already indicated that certain deadlines for rules will not be met – and it is likely that more deadlines will need to be extended
- Clearly, it will take time for the full impact of the rules to be felt by the industry

Completed Rulemaking/Actions to Date

- The federal banking agencies have adopted rules implementing various provisions of the Act to date. For example, the FDIC has:
  - Issued a final rule permanently increasing deposit coverage to $250,000
  - Issued a final rule temporarily extending deposit coverage for non-interest-bearing accounts
  - Revised insurance assessment calculation to be based on total average consolidated assets during the assessment period less average tangible equity (i.e., Tier 1 capital) as opposed to an institution's deposit level
  - Set an interim DIF Reserve Ratio of 1.35% to be achieved by 2020 and eliminated the requirement that it refund amounts in the DIF that exceed 1.50% of insured deposits.

continued

Completed Rulemaking/Actions to Date

- The Federal Reserve has also taken the following actions pursuant to the requirements of Dodd-Frank:
  - Established separate funding for the Consumer Financial Protection Bureau to facilitate establishment of the Bureau
  - Conducted numerous studies required by Dodd-Frank, such as surveys on debit card interchanges, risk retention matters, and Volcker Rule matters
  - Established the Office of Financial Stability Policy and Research to identify and analyze potential risks to the financial system and general economy, track developments at "key" institutions and analyze policies to promote stability
  - Assisted with the establishment of the Financial Stability Oversight Committee, which will oversee large financial and non-financial institutions
  - Developed plan for transitioning supervision of S&L holding companies from the Office of Thrift Supervision ("OTS") to the Federal Reserve

continued

Completed Rulemaking/Actions to Date

- The Office of the Comptroller of the Currency ("OCC") has also taken various actions required by the Act, such as:
  - Established transition plan to facilitate the OCC's supervision and regulation of all federal thrifts commencing on the target date of July 21, 2011
  - Established plan for the transfer of majority of OTS personnel to the OCC in connection with the OCC's assumption of oversight duties of federal thrifts
  - Assisted the Federal Reserve and Treasury with the establishment of the Financial Stability Oversight Committee and its proposed supervision of large financial and non-financial institutions

continued

Completed Rulemaking/Actions to Date

- The Securities and Exchange Commission (the "SEC") has also taken the following actions:
  - "Say on Pay" rule requires publicly traded financial services companies to obtain a non-binding shareholder vote to approve compensation of named executive officers as disclosed in the proxy statement at least once every three years; also requires additional compensation disclosure
  - SEC rule permits shareholders to include their nominees for director elections in the issuer's proxy solicitation materials

Pending Rules/Actions To Be Taken

- **Capital Requirements –** The federal banking agencies have issued proposed rules regarding the market risk capital requirements, but they have not yet defined proposed capital requirements for PCA and safety and soundness purposes
  - Given the impact of the recession and the capital requirements contained in Consent Orders and Written Agreements, it is safe to assume higher capital requirements will be required – it is possible that 8% Leverage Ratio and 12% Total Capital Ratio could be the new "well-capitalized" standard
  - The Act also requires that the agencies develop pro-cyclical ratio requirements – as the industry does well, ratios should increase, and as the industry weakens, ratios should be eased
  - Impact of the Collins Amendment on institutions and their Trust Preferred Securities

continued

Pending Rules/Actions To Be Taken

- **Consumer Financial Protection Bureau** – The Federal Reserve has already funded the Bureau with approximately $60 million to date. According to the government, most of the funding has been used for staffing needs
  - The Bureau does not yet have a director; however, Elizabeth Warren has been directing the establishment of the Bureau to date. It is likely that the President will make a recess appointment given the recent letter from Senate Republicans regarding requested changes to the Bureau
  - The Bureau will have responsibility for developing consumer protection laws for financial institutions and will be responsible for supervising the compliance with consumer protection laws of institutions with $10 billion or more in assets. The federal bank regulatory agencies will continue to supervise compliance efforts of institutions with less than $10 billion in assets

Pending Rules/Actions To Be Taken

- **Incentive Compensation Matters** – The federal bank regulatory agencies have issued a proposed rule regarding incentive compensation paid by financial institutions
  - This proposed rule currently applies only to institutions with $1 billion or more in assets and includes heightened standards for institutions with $50 billion or more in assets
  - Although the rule does not apply to smaller institutions, expect the regulators to use the final rule as a guide for evaluating incentive compensation at smaller institutions

Pending Rules/Actions To Be Taken

- **Incentive Compensation Matters**
  - The proposed rule seeks to: prohibit incentive compensation that encourages inappropriate risks by providing excessive compensation; require policies and procedures for incentive compensation payments that are consistent with the institution's size and complexity; require annual reporting on incentive compensation payments; and require deferral of a certain portion of incentive compensation for senior officers of large institutions ($50 billion or more)

continued

Pending Rules/Actions To Be Taken

- **Debit Card Fee Limitation –** Pursuant to Dodd-Frank, the Federal Reserve has proposed a rule defining reasonable debit card transaction fees that may be charged by financial institutions with $10 billion or more in assets and limiting the ability of such financial institutions and network providers (e.g., Visa, MasterCard) to restrict the networks over which debit transactions are conducted
  - Current proposed rule contains two pricing options – one option caps the fee at $0.12 per transaction with a safe harbor of $0.07, and the other option includes only a cap of $0.12 per transaction. The Federal Reserve has acknowledged that this cap is significantly less than current fees

continued

Pending Rules/Actions To Be Taken

- **Debit Card Fee Limitation**
  - Current proposed rule also contains proposals regarding network availability – at least two unaffiliated networks would need to be available for conducting a debit transactions and the financial institution and network providers could not limit the merchant's ability to select a network
  - Although this rule is applicable only to financial institutions with $10 billion or more in assets, it is expected to impact all financial institutions, as merchants will not be willing to pay higher fees to smaller institutions
  - Federal Reserve has announced delay in implementation given the volume of comments to the proposed rule

Other Pending Rules/Actions To Be Taken

- **Volcker Rule –** Proposed rule regarding conformance period during which banking entities and non-bank financial companies supervised by the Federal Reserve must bring proprietary trading and equity investment activities (and relationships with hedge/equity funds) into compliance with applicable limitations
- **Stress Test Requirement –** The Federal Reserve and FDIC will issue a proposed rule requiring financial institutions with more than $10 billion of assets to develop stress test programs – although not required of smaller institutions, it seems likely that regulators will require some type of stress tests for smaller institutions in the future

continued

Other Pending Rules/Actions To Be Taken

- **TILA/Reg. Z –** Requirement that creditors determine a consumer's ability to repay a mortgage before making a loan; update rule imposes minimum underwriting standards; requirement to extend period for mandatory escrow accounts
- **Credit Rating Alternatives –** Proposed interagency rule regarding alternatives to the use of credit ratings in risk-based capital guidelines

continued

Other Pending Rules/Actions To Be Taken

- **Credit Risk Retention –** Proposed interagency rule that requires sponsors of asset-backed securities to retain at least 5% of the credit risk of the underlying assets
- **ECOA/Reg. B –** Proposed rule to amend Reg. B model notices to include disclosure of credit scores and information relating to credit scores if a credit score is used in taking adverse action
- **S&L Holding Company Reports –** Federal Reserve's proposed rule will require S&L Holding Companies to make the same filings as BHCs beginning with the March 31, 2012 reporting period

CURRENT SUMMARY OF VARIOUS FDIC RULEMAKING INITIATIVES

UNDER THE DODD-FRANK WALL STREET REFORM AND

CONSUMER PROTECTION ACT

The FDIC is responsible for implementing a number of initiatives under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act" or "Dodd-Frank"), sometimes in conjunction with other federal regulatory agencies. The following list outlines some of the FDIC's upcoming plans to carry out its responsibilities under the Act as well as some of the FDIC's completed actions under the Act as identified on the FDIC's website. Timeframes for upcoming initiatives are estimates and may be adjusted.

A. <u>New and/or Open For Comment Notices for Public Rulemaking ("NPRs")</u>:

Margin and Capital Requirements

Issued joint NPR to implement capital and margin requirements for swap dealers, major swap participants, security-based swap dealers, and major security-based swap participants under each prudential regulator's jurisdiction, §731 (April 12, 2011). Comment period closes June 24, 2011.

Amendment to 12 CFR Parts 329 and 330

Issued an NPR to amend FDIC deposit insurance regulations to account for the Dodd-Frank repeal of the prohibition on paying interest on demand deposits; § 627. (April 12, 2011) (repeal effective July 21, 2011) Comment period closes May 16, 2011.

Credit Risk Retention ("Skin in the game") Proposed Rule

Approved a joint NPR requiring credit risk retention for asset backed securitizations (March 29, 2011). Rules require any securitizer to retain at least 5% of credit risk in assets it transfers through a securitization, subject to an exception for securitizations backed by Qualified Residential Mortgages, § 941.

Resolution Plans Joint Proposed Rule

Approved a joint NPR with Federal Reserve Board to implement resolution plan requirements for certain nonbank financial companies and bank holding companies, §165(d) (March 29, 2011). Comment period closes June 10, 2011.

Enhanced Compensation Structure Proposed Rule

Issued an NPR implementing enhanced disclosure and reporting of compensation arrangements and prohibiting incentive-based payment arrangements that encourage inappropriate risk taking by covered financial companies, §956 (February 7, 2011). Comment period closes May 31, 2011.

Phase II Orderly Liquidation Authority Proposed Rule

Issued a proposed rule to build on the Interim Final Rule previously issued, § 209 (March 15, 2011). The proposed rule addresses the following issues: (i) criteria for determining whether a company is "predominantly engaged in activities that are financial in nature or incidental thereto"; (ii) recoupment of compensation from senior executives and directors; (iii) the power to avoid fraudulent or preferential transfers; (iv) the priorities of expenses and unsecured claims; and (v) the administrative process for initial determination of claims. Comment period closes May 23, 2011.

B. <u>Objectives Planned Prior to the Transfer Date (July 21, 2011)</u>:

Minimum Risk-Based Capital Requirements (Collins Amendment)

Implement the required risk-based capital floor Final Rules for the advanced approaches risk-based capital rules (Basel II), §171.

Resolution Plans Joint Final Rule

Issue a joint final rule with the Federal Reserve Board to implement resolution plan requirements for certain nonbank financial companies and bank holding companies, §165(d).

Orderly Liquidation Authority Rules

Issue a final rule that addresses comments on the Interim Final rule and the Phase II Orderly Liquidation rule, including (i) criteria for determining whether a company is "predominantly engaged in activities that are financial in nature or incidental thereto"; (ii) recoupment of compensation from senior executives and directors; (iii) the power to avoid fraudulent or preferential transfers; (iv) the priorities of expenses and unsecured claims; and (v) the administrative process for initial determination of claims; §209.

QFC Recordkeeping Proposed Rule

Issue joint NPR regarding Qualified Financial Contract (QFC) recordkeeping requirements for financial companies, § 210(c)(8)(H). [QFCs are contracts between financial companies — including commodities, forward contracts, and repos — that can pose systemic risks when there are settlement failures. The Dodd-Frank Act requires the Federal primary financial regulatory agencies to adopt rules necessary to assist the FDIC in the event of an orderly liquidation].

Orderly Liquidation Procedures for Broker/Dealers

Issue joint NPR with SEC, in consultation with SIPC, establishing procedures for the FDIC to appoint SIPC as trustee of covered brokers or dealers in receivership, and providing for satisfaction of customer claims against the covered broker or dealer, § 205.

Orderly Liquidation – Maximum Obligation Limitation Proposed Rule

Issue an NPR, jointly with the Secretary of the Treasury, and in consultation with the Financial Stability Oversight Council, governing the calculation of the Maximum Obligation Limitation, applicable to any FDIC borrowing from Treasury for the orderly liquidation of a specific systemically important nonbank financial company or bank holding company, §210(n)(7).

Retail Foreign Exchange Transactions Proposed Rule

Issue an NPR requesting comment on a rule addressing the requirements for retail foreign exchange transactions by entities supervised by the FDIC, § 742.

Identify OTS Regulations and Orders for FDIC Enforcement

Identify and publish a list of the OTS regulations and orders that FDIC will enforce after the transfer of OTS supervision of state thrifts to FDIC, § 316(c)(3).

Stress Tests for Financial Companies Proposed Rule

Issue an NPR (in coordination with FRB and Federal Insurance Office) regarding requirements for self-administered stress tests for FDIC-regulated depository institutions with total consolidated assets of more than $10 billion, § 165(i)(2).

Prohibitions on Proprietary Trading ("Volcker Rule") Proposed Rule

Issue a Joint NPR (with other Federal Banking Agencies with FSOC coordinating) prohibiting proprietary trading and acquisition of an interest in hedge or private equity funds by insured depository institutions, § 619.

Core and Brokered Deposit Study

Complete a study on the use of core and brokered deposits and provide a written report to Congress with legislative recommendations, if any, to address concerns in connection with the definitions of core and brokered deposits, § 1506.

Regulatory Use of Credit Ratings Report to Congress

Review existing references to credit ratings in statutes and regulations; Report to Congress on extent of reliance on credit ratings and availability of alternatives, §939A.

C. <u>Objectives Planned: August – December 2011</u>:

Incentive-Based Compensation Arrangements Final Rule

Review comments on NPR and issue Joint Final Rule to implement enhanced disclosure and reporting of compensation arrangements and to prohibit incentive-based payment arrangements that encourage inappropriate risk taking by covered financial companies, § 956.

Capital and Margin Requirements for Swaps

Issue final rules implementing capital and margin requirements for swap dealers, major swap participants, security-based swap dealers, and major security-based swap participants under each prudential regulator's jurisdiction, §731.

Retail Foreign Exchange Transactions Interim Final Rule

Issue an interim final rule addressing the requirements for retail foreign exchange transactions by entities supervised by the FDIC, § 742.

Enhanced Compensation Structure Final Rule

Review comments on NPR and issue Joint Final Rule to implement enhanced disclosure and reporting of compensation arrangements and to prohibit incentive-based payment arrangements that encourage inappropriate risk taking by covered financial companies, § 956.

Stress Tests for Financial Companies Final Rules

Issue a Final Rule (in coordination with FRB and Federal Insurance Office) regarding requirements for self-administered stress tests for FDIC-regulated depository institutions with total consolidated assets of more than $10 billion, § 165(i)(2).

Credit Risk Retention ("Skin in the game") Final Rule

Review comments on NPR and issue Joint Final Rule to require any securitizer to retain at least 5% of credit risk in assets it transfers through a securitization, with an exception for securitizations backed by Qualified Residential Mortgages, § 941.

Prohibitions on Proprietary Trading ("Volcker Rule") Final Rule

Issue a Joint Final Rule (with other Federal Banking Agencies with FSOC coordinating) prohibiting proprietary trading and acquisition of an interest in hedge or private equity funds by insured depository institutions, § 619.

Source of Strength Proposed Rule

Issue a Joint NPR (with other Federal Banking Agencies) requiring bank holding companies, savings and loan holding companies, and other companies that control insured depository institutions to serve as sources of financial strength for their subsidiary depository institutions, § 616(d).

Orderly Liquidation Procedures for Broker/Dealers

Issue joint Final Rule with SEC, in consultation with SIPC, establishing procedures for the FDIC to appoint SIPC as trustee of covered brokers or dealers in receivership, and providing for satisfaction of customer claims against the covered broker or dealer, § 205.

QFC Recordkeeping Final Rule

Issue, after consideration of comments, a Final Rule regarding Qualified Financial Contract (QFC) recordkeeping requirements for financial companies, § 210(c)(8)(H).

D. Additional Objectives Completed:

Initial Orderly Liquidation Interim Final Rule

Issued Interim Final Rule, with additional questions and 60-day comment period, §209. (Effective January 25, 2011). Comment period closed March 28, 2011.

Assessments, Large Bank Pricing

Issued a Final Rule to implement changes to the assessment base used to determine risk-based premiums for insured depository institutions, §331(b); included in the rule are changes to the risk-based pricing system necessitated by changes to the assessment base.

Diversity

Established new Office of Minority and Women Inclusion, §342 (January 18, 2011).

Designated Reserve Ratio Final Rule

Adopted a Final Rule after consideration of comments on the October NPR proposing a DIF Designated Reserve Ratio of 2% (December 14, 2010).

Minimum Risk-based Capital Requirements

Issued an NPR to implement the required risk-based capital floor for the advanced approaches risk-based capital rules (Basel II), §171 (December 14, 2010). Comment period ended February 28, 2011.

Risk-Based Capital Guidelines: Market Risk

Issued an NPR to implement the required market risk capital rules, §171 (December 14, 2010). Comment period ended April 11, 2011.

Restoration Plan & Deposit Insurance Fund (DIF) Management Proposed Rules

Adopted a revised Restoration Plan to meet the new statutory goal for the DIF reserve ratio, and issued an NPR to set a new designated reserve ratio, implement a dividend policy, and set assessment rates (October 19, 2010). Comment Period closed November 26, 2010.

Unlimited Deposit Insurance Coverage for Non-interest Bearing Transaction Accounts Final Rule

After consideration of comments on NPR, issued final rule implementing temporary unlimited deposit insurance coverage for non-interest bearing transaction accounts (November 9, 2010). Comment Period closed October 15, 2010.

Amended Unlimited Deposit Insurance Coverage for Non-interest Bearing Transaction Accounts Final Rule to include IOLTAs

Issued a Final Rule to implement a new law (Pub. L. No. 111-343 (Dec. 29, 2010)) extending Temporary Unlimited Deposit Insurance for Noninterest-Bearing Transaction Accounts to Interest on Lawyers Trust Accounts (IOLTAs) (January 18, 2011).

Deposit Insurance Coverage Limit Final Rule

Issued Final Rule implementing permanent increase in deposit insurance coverage to $250,000 (August 10, 2010).

Review of Regulatory Use of Credit Ratings and Request for Comment

Issued joint Advance Notice of Proposed Rulemaking (ANPR) to request public comment on other measures of creditworthiness (as alternatives to credit ratings) for use in capital regulations (August 10, 2010). Comment period closed October 25, 2010.

CURRENT SUMMARY OF VARIOUS FEDERAL RESERVE RULEMAKING

INITIATIVES UNDER THE DODD-FRANK WALL STREET

REFORM AND CONSUMER PROTECTION ACT

The Board of Governors of the Federal Reserve System (the "Board") is responsible for implementing numerous provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Act" or "Dodd-Frank"), sometimes in conjunction with other federal regulatory agencies. The following list describes several of the significant initiatives that the Board expects to address over the next few months as well as the implementation initiatives recently completed by the Board as identified on the Board's website. Timeframes for upcoming initiatives are estimates and may be adjusted.

A. Initiatives Planned: April to June 2011:

Residential Mortgages: Prepayment Penalties

The Board will request comment on a proposed rule prohibiting prepayment penalties for non-qualified mortgages and restricting prepayment penalties for qualified mortgages (through phase-out of a penalty over three years). (DFA Section 1414)

Retail Foreign Exchange Transactions

The Board will request comment on a rule addressing the requirements for retail foreign exchange transactions by entities supervised by the Federal Reserve. (DFA Section 742)

Financial Market Utilities (FMUs): Systemic Designation

The FSOC is expected to issue a final rule regarding the FSOC's authority to designate FMUs as systemically important. (DFA Section 804(a))

Registration of Nonbank Financial Companies Designated for Consolidated Supervision

The Board will request comment on a proposed rule to prescribe the forms and information requirements for nonbank financial companies designated for enhanced, consolidated supervision by the Federal Reserve to register with the Board. (DFA Section 114)

Volcker Rule: Activity Restrictions

The Board, along with other federal financial regulatory agencies, will request comment on a proposed inter-agency rule to implement the Volcker Rule's restrictions on proprietary trading, hedge fund, and private equity fund activity by insured depository institutions and their affiliates (including bank holding companies (BHCs)). (DFA Section 619)

Volcker Rule: Financial Sector Concentration Limit

The Board, along with other Federal financial regulatory agencies, will request comment on a proposed rule to implement the Volcker Rule's concentration limit, which prohibits a financial company from making an acquisition if the liabilities of the combined company would exceed 10 percent of the liabilities of all financial companies. (DFA Section 622)

Section 13(3) Policies and Procedures

The Board will request comment on a proposed rule, developed in consultation with the Secretary of the Treasury, to establish policies and procedures for Section 13(3) lending facilities under the Federal Reserve Act. (DFA Section 1101(a)(6))

Debit Interchange

The Board will issue a final rule to establish standards for debit card interchange fees, regulations governing network fees, and prohibitions against network exclusivity arrangements and routing restrictions. (DFA Section 1075)

Incentive Compensation Rule

The Board will issue a final inter-agency rule to prohibit incentive-based compensation arrangements that encourage inappropriate risk-taking by covered financial companies, and to require the disclosure and reporting of certain incentive-based compensation information by covered financial companies. (DFA Section 956)

Volcker Rule Requirements

The Board, along with other Federal financial regulatory agencies, will request comment on a proposed inter-agency rule to implement Volcker Rule requirements that restrict the ability of banking entities to engage in proprietary trading and to invest in or sponsor private equity funds and hedge funds. (DFA Section 619)

Related BHC and Nonbank Financial Company Rules

The Board will issue a final rule defining the terms "significant bank holding company" and "significant nonbank financial company." These terms relate to the factors the Financial Stability Oversight Council (FSOC) must consider in determining whether to designate a nonbank financial company for supervision by the Federal Reserve and the credit exposure reporting requirements applicable to FSOC-designated nonbank financial companies and large BHCs. (DFA Section 113 and 165(d)(2)) The Board will also issue a final rule to define when a nonbank company is "predominantly engaged" in financial activities. (DFA Section 102(a)(7))

Designation of Nonbank Financial Companies for Consolidated Supervision

The FSOC is expected to issue a final rule regarding the FSOC's authority to designate certain nonbank financial companies for enhanced, consolidated supervision by the Federal Reserve. (DFA Section 113)

Enhanced Prudential Standards for Large BHCs and Nonbank Financial Companies Designated for Consolidated Supervision

Section 165 of the Dodd-Frank Act requires the Board to establish stricter prudential standards for all BHCs with total consolidated assets of $50 billion or greater and all non-bank financial companies supervised by the Board. The Board will request comment on a proposed rule or rules incorporating the following:

- **Risk-Based Capital and Leverage Requirements:** heightened risk-based capital and leverage requirements for nonbank financial companies supervised by the Board and BHCs with $50 billion or more in assets. (DFA Section 165(b)(1)(A)(i))

- **Liquidity Requirements:** enhanced liquidity requirements for nonbank financial companies supervised by the Board and BHCs with $50 billion or more in assets. (DFA Section 165(b)(1)(A)(ii))

- **Risk-Management Requirements:** heightened risk-management standards for nonbank financial companies supervised by the Board and BHCs with $50 billion or more in assets. (DFA Section 165(b)(1)(A)(iii))

- **Credit Exposure Limits:** rules to prohibit nonbank financial companies supervised by the Board and BHCs with $50 billion or more in assets from having credit exposure to any unaffiliated entity exceeding a percentage of the company's capital stock and surplus. (DFA Section 165(e))

- **Risk Committee Requirements:** requirement that the board of directors of each publicly traded nonbank financial company supervised by the Board and publicly traded BHC with $10 billion or more in assets establish a risk committee. (DFA Section 165(h))

- **Stress Tests: Board Conducted:** requirement that the Board conduct an annual stress test of each nonbank financial company supervised by the Board and BHC with $50 billion or more in assets. (DFA Section 165(i))

- **Stress Tests: Company Conducted:** requirement that each nonbank financial company supervised by the Board and BHC with $50 billion or more in assets conduct semi-annual stress tests; requirement that other supervised financial companies with $10 billion or more in assets conduct annual stress tests. (DFA Section 165(i))

- **New Prompt Corrective Action (PCA) Regime:** requirement that nonbank financial companies supervised by the Board and BHCs with $50 billion or more in assets take increasingly stringent corrective measures as the company's financial condition deteriorates. (DFA Section 166)

Credit Exposure Reporting Requirement: The Board will request comment on a proposed rule, developed jointly with the FDIC, to require nonbank financial companies supervised by the Board and BHCs with $50 billion or more in assets to report to the Board, FSOC, and FDIC on the credit exposures between the company and other "significant" nonbank financial companies and BHCs. (DFA Section 165(d))

Remittance Transfers

The Board will request comment on a proposed rule to: require new disclosures from remittance transfer providers, including written notices, receipts, and statements detailing transaction specifics; establish standards for remittance transfer errors, cancellations, and refunds; establish standards for liability of remittance transfer providers, including agents; and address the issue of how remittance transfer providers should disclose the amount of currency to be received in a foreign country when that amount is unknown. (DFA Section 1073)

B. Initiatives Planned: July to September 2011:

Intermediate Holding Company Regulations for Nonbank Financial Companies Designated for Consolidated Supervision

The Board will request comment on a proposed rule governing when and how a nonbank financial company designated for consolidated supervision must establish an intermediate holding company to separate its financial activities from its commercial activities. (DFA Section 113(c) and 167)

Intermediate Holding Company Regulations for Grandfathered Unitary SLHCs

The Board will request comment on a proposed rule governing when and how a grandfathered unitary SLHC that is engaged in commercial activities must establish an intermediate holding company to conduct its financial activities. (DFA Section 626)

Prior Notification by Large Financial Holding Companies (FHCs) for Large Nonbank Acquisitions

The Board will request comment on a proposed rule to implement the requirement that nonbank financial companies supervised by the Board and BHCs with $50 billion or more in assets provide the Board prior written notice to acquire a nonbanking company with $10 billion or more in assets under the BHC Act Section 4(k). (DFA Section 163(b))

Applications by Nonbank Financial Companies to Acquire Bank Shares

The Board will request comment on a proposed rule to implement the requirement that a nonbank financial company seek the Board's approval before acquiring more than 5 percent of the voting shares of any bank or bank holding company, thereby aligning this threshold with that currently applied to bank holding company acquisitions of bank shares. (DFA Section 163(a))

Application of Depository Institution Management Interlocks Act to Nonbank Financial Companies Designated for Consolidated Supervision

The Board will request comment on a proposed rule to apply the Depository Institution Management Interlocks Act to a nonbank financial company designated for consolidated supervision by the Federal Reserve. (DFA Section 164)

Financial Stability Considerations in BHC Act and Bank Merger Act Transactions

The Board will request comment on a proposed rule to implement the requirement that it consider the impact on financial stability of bank acquisitions or merger proposals under the BHC Act Section 3 and the Bank Merger Act and notices to acquire a nonbanking company filed under the BHC Act Section 4(j). (DFA Section 604(d), (f))

Financial Stability Factor for Foreign Banking Organization (FBO) Applications

The Board will request comment on a proposed rule to implement the requirement that the Board, when acting on an application by a foreign bank to establish a U.S. office or in determining whether to order a foreign bank to terminate its U.S. offices, consider whether the foreign bank's home country has adopted (or is making progress toward adopting) a financial regulatory system that mitigates any systemic risk the foreign bank may present to the U.S. (DFA Section 173(a) and (b))

BHC Act Amendments: Financial Holding Companies and Credit Card Banks

The Board will request comment on a proposed rule to implement amendments to the BHC Act that include requiring a BHC (as well as its subsidiary depository institutions) to be well capitalized and well managed to qualify as a financial holding company; requiring that a financial holding company obtain the Board's approval before acquiring a nonbank company with more than $10 billion in assets; and permitting a limited-purpose credit card bank to make corporate credit card loans to small businesses. (DFA Sections 604(e), 606, 628)

Thrift Acquisition National Deposit Cap

The Board will request comment on a proposed rule to apply the 10 percent national deposit cap to interstate bank mergers and acquisitions of savings associations or other nonbank insured depository institutions by BHCs and Savings and Loan Holding Companies (SLHCs). (DFA Section 623)

Financial Market Utilities (FMUs): Risk-Management Standards, Advance Notice Requirements

The Board will issue a final rule to implement two provisions of the DFA related to supervision of FMUs designated as systemically important by the Financial Stability Oversight Council. Specifically, it will establish risk-management standards for designated FMUs supervised by the Federal Reserve (DFA Section 805(a)(1)) and will require advance notice of a proposed material change to its rules, procedures, or operations. (DFA Section 806(e)(1)(B))

Remittance Transfers: Congressional Report

The Board will submit a report to Congress on the status of Automated Clearing House (ACH) expansion for remittance transfers to foreign countries. (DFA Section 1073(b)(2))

Designated Clearing Entities: Congressional Report

The Board, along with the SEC and CFTC, will submit a joint report to Congress containing recommendations for promoting robust risk management standards and consistency in supervisory programs for designated clearing entities. (DFA Section 813)

Minimum Leverage and Risk-Based Capital Requirements (Collins Amendment)

Following on a December 2010 proposed rule that would amend the advanced approaches capital adequacy framework consistent with the Act, the Board will request comment on a proposal addressing other aspects of the Collins Amendment including minimum leverage requirements and risk considerations to be taken into account. (DFA Section 171(b)(1), (b)(7), and (2))

OTS Regulations

The Board will publish the list of all Office of Thrift Supervision (OTS) regulations that it will continue to enforce for Savings and Loan Holding Companies (SLHCs). (DFA Section 316(c))

Interest on Demand Deposits

The Board will issue a final rule repealing Regulation Q and allowing payment of interest on demand deposits at depository institutions. (DFA Section 627)

Swaps Margin Requirements

The Board, along with other Federal bank regulatory agencies, will issue a final inter-agency rule implementing the margin requirements for swap dealers, security-based swap dealers, major swap participants, and major security-based swap participants under each prudential regulator's jurisdiction. (DFA Section 731)

Intermediate Holding Company Regulations for Grandfathered Unitary SLHCs

The Board will issue a final rule governing when and how a grandfathered unitary SLHC that is engaged in commercial activities must establish an intermediate holding company to conduct its financial activities. (DFA Section 626)

Government Prepaid Cards Congressional Report

The Board will submit a report to Congress on the use of prepaid cards by government authorities and the interchange transaction and cardholder fees charged with respect to such cards. (DFA Section 1075(a))

Registration of Systemically-Designated Nonbank Financial Companies

The Board will request comment on a proposed rule prescribing the forms and information requirements for a systemically-designated nonbank financial company to register with the Board. (DFA Section 114)

Credit Rating Alternatives

The Board will request comment on changes to existing rules to implement the requirements of section 939A of the DFA relating to use of credit ratings in agency rules. (DFA Section 939A)

Credit Risk Retention

The Board, along with other Federal regulatory agencies, will issue a final inter-agency rule to implement the credit risk retention requirements applicable in connection with the issuance of asset-backed securities. (DFA Section 941)

Credit Rating Alternatives for Bank Financial Subsidiaries

The Board will request comment on a proposed rule, developed with the U.S. Department of the Treasury, to replace the investment grade rating requirement for national and state member banks to invest in or control a financial subsidiary with an alternative standard. (DFA Section 939(d))

Safe Harbor for Nonbank Financial Companies

The Board will request comment on a proposed rule to establish criteria for exempting certain types or classes of nonbank financial companies from potential designation by the FSOC as systemically important. (DFA Section 170)

Truth In Lending Act--Escrow Administration

The Board will issue a final rule expanding the minimum period for mandatory escrow accounts for first-lien, higher-priced mortgages; providing an exemption for certain creditors in “rural or under-served” counties; and implementing new escrow disclosure requirements for all residential mortgages. (DFA Section 1461)

Supervisory Assessment Fees

The Board will request comment on a proposed rule to implement the requirement that the Board impose on bank holding companies (BHCs) and savings and loan holding companies (SLHCs) with assets of $50 billion or more and nonbank financial companies supervised by the Board fees that are sufficient to cover the cost of supervising and regulating these organizations. (DFA Section 318(c))

C. <u>Initiatives Completed</u>:

As of April 2011

Interest on Demand Deposits

On April 6, 2011, the Board requested comment on a proposed rule to repeal Regulation Q and allow payment of interest on demand deposits at depository institutions, effective July 21, 2011. (DFA Section 627)

Swaps Margin Requirements

On April 12, 2011, the Board requested comment on a proposed inter-agency rule, issued with five other agencies, to implement the margin requirements for swap dealers, security-based swap dealers, major swap participants, and major security-based swap participants under each prudential regulator's jurisdiction. (DFA Section 731)

Resolution Plan ("Living Will") Requirement

On April 12, 2011, the Board requested comment on a proposed rule, developed jointly with the Federal Deposit Insurance Corporation (FDIC), to implement the "living will" requirements for nonbank financial companies supervised by the Board and BHCs with $50 billion or more in assets. (DFA Section 165(d))

Supervisory Standards Applicable to Savings & Loan Holding Companies (SLHCs)

On April 15, 2011, the Board requested comment on a notice that outlines how it intends to apply certain parts of its current consolidated supervisory program for bank holding companies to SLHCs after assuming supervisory responsibility for SLHCs. (DFA Sections 606, 624, 625)

Residential Mortgage Requirements

On April 19, 2011, the Board requested comment on a proposed rule to establish ability to repay standards for residential mortgages, along with a safe harbor for qualified mortgages, and to prohibit prepayment penalties for non-qualified mortgages while restricting prepayment penalties for qualified mortgages (through a three-year phase-out period). (DFA Sections 1411, 1412, 1414)

Bankruptcy-Related Studies

On April 21, 2011, the Board requested comment on two bankruptcy-related studies. In consultation with the Administrative Office of the United States Courts (AOUSC), the Board must study the resolution of financial companies under Chapter 7 or Chapter 11 of the United States Bankruptcy Code, as well as the international coordination of the resolution of systemically important financial companies under the Bankruptcy Code and applicable foreign law. (DFA Sections 216 and 217)

As of March 2011

Fair Credit Reporting Act (FCRA): Credit Score Use

On March 1, 2011, the Board requested comment on a proposed rule to implement the amendment to Section 615 of the FCRA to include credit scores and related information in both risk-based pricing notices (under FR Regulation V, jointly with the FTC) and adverse action notices (under FR Regulation B). (DFA Section 1100(F))

Truth in Lending Act (TILA): Exemption Threshold Increase

The Board issued a final rule on March 25, 2011, to raise the exemption threshold from $25,000 to $50,000 for: 1) non-home secured credit (under Regulation Z), and 2) consumer leases (under Regulation M). The final rule will be effective July 21, 2011. (DFA Section 1100(E))

Credit Risk Retention

On March 29, 2011, the Board requested comment on a proposed rule, being issued jointly with five other federal agencies, to implement the credit risk retention requirements applicable in connection with the issuance of asset-backed securities. (DFA Section 941)

Financial Market Utilities (FMUs): Risk-Management Standards, Advance Notice Requirements

On March 30, 2011, the Board requested comment on a proposed rule that would implement two provisions of the DFA related to supervision of FMUs designated as systemically important by the Financial Stability Oversight Council. Specifically, it would establish risk-management standards for designated FMUs supervised by the Federal Reserve (DFA Section 805(a)(1)) and would require advance notice of a proposed material change to its rules, procedures, or operations. (DFA Section 806(e)(1)(B))

Incentive Compensation

On March 30, 2011, the Board requested comment on a proposed inter-agency rule to prohibit incentive-based compensation arrangements that encourage inappropriate risk taking by covered financial companies, and require the disclosure and reporting of certain incentive-based compensation information by covered financial companies. (DFA Section 956)

As of February 2011

Inter-Agency Changes to Reporting Requirements for Office of Thrift Supervision (OTS) Regulated Entities

On February 3, 2011, the Board, Federal Deposit Insurance Corporation (FDIC), Office of the Comptroller of the Currency, and OTS announced proposed changes to reporting requirements for savings associations and savings and loan holding companies regulated by the OTS. The proposed changes would result in uniform reporting systems and processes among

FDIC-insured banks and savings institutions, as well as uniform reporting requirements among all holding companies supervised by the Federal Reserve Board. (DFA Section 327)

Related Bank Holding Company and Nonbank Financial Company Rules

On February 8, 2011, the Board requested comment on a proposed rule to define when a nonbank company is "predominantly engaged" in financial activities. (DFA Sections 102(a)(6) and 102(b)) The proposed rule also defines the terms "significant nonbank financial company" and "significant bank holding company." (DFA Section 102(a)(7)) These terms relate to the factors the Financial Stability Oversight Council (FSOC) must consider in determining whether to designate a nonbank financial company for supervision by the Federal Reserve Board and the credit exposure reporting requirements applicable to FSOC-designated nonbank financial companies and large bank holding companies. (DFA Sections 113 and 165(d)(2))

Volcker Rule Conformance Period

On February 9, 2011, the Board announced its approval of a final rule to implement the provisions of the Dodd-Frank Act that give banking firms a period of time to conform their activities and investments to the prohibitions and restrictions of the Volcker Rule. (DFA Section 619(c)(6))

Truth In Lending Act--Escrow Requirements

The Board issued a final rule on February 23, 2011, to increase the annual percentage rate (APR) threshold used to determine whether a mortgage lender is required to establish an escrow account for property taxes and insurance for first-lien "jumbo" residential mortgage loans, effective April 1, 2011. The Board also requested comment on February 23, 2011, on a proposed rule expanding the minimum period for mandatory escrow accounts for first-lien, higher-priced mortgages; providing an exemption for certain creditors in "rural or under-served" counties; and implementing new escrow disclosure requirements for all residential mortgages. (DFA Section 1461)

As of January 2011

Diversity in the Federal Reserve System's Workforce

The Federal Reserve announced on January 18, 2011, the establishment of offices to promote diversity and inclusion at the Federal Reserve Board and at all 12 of the Federal Reserve Banks that satisfy "Office of Minority Women and Inclusion" requirements in the Dodd-Frank Act. (DFA Section 342)

Designation of Nonbank Financial Companies for Consolidated Supervision

Following on the October 6, 2010, Federal Register Advance Notice, the Board assisted the FSOC in developing a Notice of Proposed Rulemaking released January 18, 2011, regarding the FSOC's authority to designate certain nonbank financial companies for enhanced, consolidated supervision by the Federal Reserve. (DFA Section 113)

Study of Volcker Rule Activity Restrictions

The Board contributed to the FSOC's study on the Volcker Rule's activity restrictions, released January 18, 2011. (DFA Section 619(b))

Office of Thrift Supervision (OTS) Transition Plan

On January 25, 2011, the Federal Reserve, OTS, Office of the Comptroller of the Currency, and FDIC issued a joint report to Congress and the Inspectors General of the participating agencies on the agencies' plans to implement the transfer of OTS authorities. (DFA Section 327)

As of December 2010

Emergency Lending and Other Facilities Disclosure

On December 1, 2010, the Board posted Transaction Data information regarding transactions that occurred between December 1, 2007, and July 21, 2010, under various emergency lending facilities authorized under Section 13(3) of the Federal Reserve Act, the Term Auction Facility, the government-sponsored enterprise mortgage-backed securities purchase program, and foreign currency swap lines. (Provisions of the Dodd-Frank Act require that this information be made publicly available.) The disclosure included information about the identify of entities that received assistance under the facilities, the amount and type of assistance provided, the terms for repayment, and the collateral posted. (DFA Section 1109(c))

Truth in Lending Act (TILA): Exemption Threshold Increase

On December 13, 2010, the Board requested comment on two proposed rules that would raise the exemption threshold from $25,000 to $50,000 for: 1) non-home secured credit (under Regulation Z), and 2) consumer leases (under Regulation M). Under the DFA, the increase will be effective July 21, 2011. (DFA Section 1100(E))

Minimum Risk-Based Capital Requirements (Collins Amendment)

On December 15, 2010, the Board requested comment on a proposed rule that would amend the advanced approaches capital adequacy framework consistent with the Dodd-Frank Act. Specifically, the proposed rule would require a banking organization operating under the advanced approaches standards to meet, on an ongoing basis, the higher of the generally applicable and the advanced approaches minimum risk-based capital standards. The Board anticipates addressing other aspects of DFA Section 171 in subsequent rulemaking. (DFA Section 171(b)(2))

Debit Interchange

On December 16, 2010, the Board requested comments on a proposed rule to establish standards for debit card interchange fees, regulations governing network fees, and prohibitions against network exclusivity arrangements and routing restrictions. (DFA Section 1075)

As of November 2010

Office of Financial Stability Policy and Research

The Board established an Office of Financial Stability Policy and Research on November 4, 2010, to develop and coordinate staff efforts to: identify and analyze potential risks to the financial system and the broader economy, including monitoring of asset prices, leverage, financial flows, and other market risk indicators; follow developments at key institutions; and analyze policies to promote financial stability. The Office also will support the supervision of large financial institutions and the Board's participation on the FSOC.

Volcker Rule--Conformance Period

On November 17, 2010, the Board requested comment on a proposed rule to implement the conformance periods available to banking entities to bring their proprietary trading, hedge fund, and private equity fund activities into compliance with the Volcker Rule's prohibitions. (DFA Section 619(c)(6))

Financial Market Utilities (FMUs)

The Board assisted the FSOC in developing an Advance Notice of Proposed Rulemaking regarding the FSOC's authority to designate FMUs as systemically important that was approved by the FSOC on November 23, 2010. (DFA Section 804(a))

As of October 2010

Establishment of the Financial Stability Oversight Council (FSOC)

The Board assisted in establishing the FSOC, which conducted its first meeting on October 1, 2010. At that meeting, FSOC bylaws were adopted and a transparency policy was established. (DFA Section 111)

Designation of Nonbank Financial Companies for Consolidated Supervision

The Board assisted the FSOC in developing an Advance Notice of Proposed Rulemaking regarding the FSOC's authority to designate certain nonbank financial companies for enhanced, consolidated supervision by the Federal Reserve. The Notice was published in the *Federal Register* on October 6, 2010. (DFA Section 113)

Appraisal Independence Rule

The Board issued an interim final rule on October 18, 2010, that is intended to ensure that real estate appraisers are free to use their independent professional judgment in assigning home values without influence or pressure from those with interests in the transactions. (DFA Section 1472)

As of September 2010

Surveys Issued on Debit Card Interchange

On September 13, 2010, the Board issued surveys to three groups--debit card issuers, payment card networks, and merchant acquirers. The surveys were designed to assist the Board in developing proposed new rules relating to debit card interchange fees and network routing and exclusivity. (DFA Section 1075)

As of August 2010

Credit Ratings

The Board requested comment on August 10, 2010, on an Advance Notice of Proposed Rulemaking regarding alternatives to the use of credit ratings in the risk-based capital rules for banking organizations. (DFA Section 939A)

Consumer Financial Protection Bureau (CFPB) Transition Funding

The Federal Reserve established an account for the CFPB at the Federal Reserve Bank of New York. (DFA Section 1017(b)(1)) Pursuant to a request from the Treasury Department, the Federal Reserve provided initial transition funding of $18.4 million to the account for the establishment of the CFPB on August 12, 2010. (DFA Section 1017(a)(3) & (b)(2))

Truth in Lending Act--Escrow Requirements for Jumbo Loans

The Board requested comment on August 16, 2010, on a proposed rule to increase the annual percentage rate (APR) threshold used to determine whether a mortgage lender is required to establish an escrow account for property taxes and insurance for first-lien jumbo mortgage loans. (DFA Section 1461)

Guidance on Sound Incentive Policies

Philip L. Mowery
Shareholder
Executive Compensation
Vedder Price P.C.

- Interagency Guidance on Sound Compensation Policies
- Issued June 25, 2010
- First time agencies have agreed on a statement regarding compensation

- Three principles that should be a part of every incentive compensation system

Principle One

- The compensation should not be the same regardless of the ultimate outcome
- The example of a loan officer who receives a bonus that is tied only to loan generation

Principle Two

- The need for compatibility between the incentive compensation and effective controls and risk management
- The creation and maintenance of documentation that allows an audit that can measure the effectiveness of the program
- Involve risk management personnel in the process

Principle Three

- Active and effective oversight by the Board of Directors
- Approval of plans for senior officers and review of the risk control systems

Ellen M. Costello

President and Chief Executive Officer, Harris Financial Corp.

Ellen Costello is President and Chief Executive Officer of Harris Financial Corp., a large regional retail, business and wealth bank serving more than 1.3 million personal and business customers in Illinois, Indiana and Wisconsin through its network of 312 branches. Harris is part of Toronto-based BMO Financial Group, one of North America's leading financial services providers.

Ms. Costello is responsible for the U.S. personal and commercial business, driving profitable business growth organically and through acquisition. She also has corporate and regulatory governance responsibilities for the BMO enterprise in the United States and is a member of the BMO management and performance committees.

After joining BMO Financial Group in 1983, Ms. Costello held progressively senior positions in Corporate Banking and Treasury, serving in leadership positions in Derivatives, as Regional Treasurer in Asia in 1993 and in 1995 as Senior Vice-President and Deputy Treasurer. In 1997, she was appointed Executive Vice-President, Global Treasury Group, responsible for the foreign exchange, financial products, money markets, loan syndication/trading and managed futures businesses. In 2000, she was named head of Securitization and Credit Investment Management; in 2003, Head of BMO Capital Markets, New York; and in 2006 she assumed responsibility for Merchant Banking. She was appointed to her current role in August 2006.

Ms. Costello holds a BBA from St. Francis Xavier University and earned her MBA from Dalhousie University. She serves on a number of nonprofit boards, including the United Way of Metropolitan Chicago, the Chicago Council on Global Affairs, the Chicago Symphony Orchestra, After School Matters, the Economic Club of Chicago, the Executives' Club of Chicago and the Financial Services Roundtable. She is a member of the Commercial Club, its Civic Committee, the Chicago Network and the Trustees Committee of The Chicago Community Trust.

Jeffrey Brand

Managing Director, Keefe, Bruyette & Woods, Inc.

Mr. Brand focuses on merger and acquisition, capital markets and valuation activities for Midwestern financial institutions. Mr. Brand has over a decade of investment banking experience and has been involved in transactions totaling over $5B in the last nine years.

James Hemmer

Managing Director, Investment Banking , Sandler O’Neill & Partners L.P.

James Hemmer is a Managing Director in the Investment Banking Group of Sandler O’Neill & Partners, L.P. He is responsible for advising Sandler O’Neill’s Midwest investment banking clients and is based in the firm’s Chicago office.

Mr. Hemmer has more than 20 years of experience working with Midwestern banks, thrifts and other financial companies. His transaction experience includes First Western Bank’s acquisition by First Interstate Bancsystem and Great Banc’s sale to Royal Banc of Scotland. Mr. Hemmer has also has also led several significant capital issuances for companies such as First Midwest Bancorp and Associated Bancorp.

Prior to joining Sandler O’Neill, Mr. Hemmer was a Senior Vice President at Lehman Brothers with responsibility for advising banks and thrifts on mergers and acquisitions and assisting in capital raising transactions. He previously held positions with McDonald Investments and The Chicago Corporation.

Mr. Hemmer holds a Master of Business Administration from Kellogg School of Management and a Bachelor of Arts from Dartmouth College.

Jerry L. Miller

President of Regulatory Compliance Associates, Inc. (also known as REGCOM)

Mr. Miller was formerly with Peat Marwick Main & Co., where he served as practice leader for the Midwest Financial Institutions Regulatory Compliance Consulting practice. In this role, Mr. Miller advised management and directorates of financial institutions on understanding and complying with banking regulations, including the development and implementation of formal policies and procedures. Prior to joining Peat Marwick, Mr. Miller served as an OCC field examiner and member of the OCC regional/district management team.

With a wide range of regulatory examination and financial institution experience, REGCOM's staff has experience in assisting management and directorates of financial institutions on a number of focus areas, including understanding and complying with regulations, training, and assisting problem institutions. REGCOM's publications cover a variety of management and regulatory focus areas, and guide management through the design and implementation of individual regulatory compliance programs for financial institutions of all asset sizes. REGCOM offers proactive information and solutions to all levels of staffing within the financial services industry.

Charles K. Smith

Manager, Sandler O'Neill Mortgage Finance, L.P.

Charles K. Smith is a Principal of Sandler O'Neill & Partners, L.P. Mr. Smith's career in the Mortgage Banking industry spans 24 years, representing Sandler O'Neill Mortgage Finance L.P., Thompson McKinnon Mortgage Finance, Indiana Mortgage Company, Olympic Mortgage Company and Lincoln Service Corp.

Mr. Smith has been a member of Sandler O'Neill & Partners L.P. for the last 20 years and is currently the Principal responsible for managing Sandler O'Neill Mortgage Finance L.P. In that capacity, he guides the company in the securitization, sale, or acquisition of residential, multi-family, commercial and consumer loans. These range in quality and performance from performing "A" paper assets to non-performing assets. In the last eight years, an excess of $23 billion of product has been successfully executed under his guidance.

Mr. Smith assists with constructing asset valuations in accordance with FASB/GAAP guidelines and asset bid price levels to support bank acquisitions and portfolio restructurings involving multi-billion dollar loan and servicing portfolios. He was responsible for overseeing and contributing to the Firm's development of a static life of loan projected cumulative loss model to provide innovative solutions for current asset valuation methodologies applied to portfolio valuations, FDIC assisted bids, and open bank acquisitions. Mr. Smith oversees the valuation of over $3.0 billion of servicing rights quarterly. He coordinates all transaction related activities to ensure professional execution, realization of client objectives and integration of multiple transaction requirements for analytical, underwriting, delivery, and valuation resources.

Additionally, Mr. Smith is a co-manager of the firm's Information Technology Group and is an active board member for the not-for-profit Christian ministries, Have a Standard Foundation and Samaritans Heart International.

VEDDER PRICE

JAMES M. KANE

Shareholder

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Emphasis

Corporate

Financial Institutions Group

Education

- J.D., Chicago-Kent College of Law, 1977
- B.A., Loyola University of Chicago, 1974

Chair, Financial Institutions Group

James M. Kane joined Vedder Price P.C. in 1993 as a shareholder and is a member of the firm's Financial Institutions Group. From 1981 until joining Vedder Price, he was the district counsel in Chicago for the Office of the Comptroller of the Currency. As the chief legal officer for the Six-State Central District (Illinois, Wisconsin, Michigan, Ohio, Indiana and Kentucky), he was responsible for providing legal and policy advice to the Deputy Comptroller and the 500 examiners of the Central District. In this capacity, he authored opinions on a wide variety of banking law issues and represented the OCC in numerous enforcement actions involving national banks, bank officers and directors.

Mr. Kane counsels clients in the banking and financial industry on a wide variety of issues, including all regulatory matters. He also provides advice on all corporate matters, including mergers and acquisitions, and on the development of new financial products. He is a past chairman of the Financial Institutions Committee of the Chicago Bar Association (CBA). He remains a member of the CBA and is also a member of the American Bar Association.

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DANIEL C. MCKAY, II

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Emphasis

Bank and Thrift Regulation and Enforcement

Bank Formation (*de novo*)

Finance and Transactions

Financial Institutions

Mergers and Acquisitions

Subprime Lending and Mortgage Task Force

White Collar Criminal Defense

Education

- M.A. (Political Science: Public Policy Analysis), Loyola University Graduate School, 1985
- J.D., Loyola University of Chicago School of Law, 1984
- B.A. (Economics and Philosophy), University of Notre Dame, 1980

Chair of Financial Institutions Group

Daniel C. McKay, II concentrates his practice in the representation of financial institutions and corporations and their officers, directors and shareholders in connection with mergers and acquisitions, securities offerings, corporate finance, corporate governance and regulatory and compliance matters. He has been involved in more than 150 bank or thrift mergers and acquisitions/securities offerings, with aggregate consideration of these deals totaling over $50 billion.

He also assists financial institutions in strategic growth initiatives including new products, services and franchise expansion, including assisting with the organization of de novo state and national banks. He is a frequent speaker on financial institution law matters, serves as an executive editor of the *Financial Services Report* and was selected by *Crain's Chicago Business* as one of the top business leaders in Chicago. Mr. McKay was selected by his peers as a "Leading Lawyer." Mr. McKay was selected for inclusion in 2006, and from 2009 to 2011 in *Illinois Super Lawyers*. As an authority on bank mergers and acquisitions, Mr. McKay has been cited in publications such as the *Bank Director Magazine*, *The Wall Street Journal*, *American Banker, Crain's Chicago Business* and the *Chicago Tribune.*

Mr. McKay has held various management positions at Vedder Price P.C., including Chair of the Corporate Practice Area, Chair of the Financial Institutions Group and Chair of the Associate Evaluation Committee, as well as membership on the Firm's Board of Directors, Compensation Committee and Strategic Planning Committee.

For a number of years, Mr. McKay taught banking law and regulation at Loyola University School of Law. Prior to joining Vedder Price, Mr. McKay served as an attorney with a banking boutique law firm in Washington, D.C., and he was a bank regulatory attorney with the Federal Home Loan Bank of Chicago, where he was assigned to the Securities and Corporate Division and Office of Enforcement of the Federal Home Loan Bank Board, Washington, D.C. Mr. McKay has also received training from the U.S. Securities and Exchange Commission.

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JAMES W. MORRISSEY

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Emphasis

Financial Institutions

Bank and Thrift Regulation and Enforcement

Corporate Mergers and Acquisitions

Corporate Securities

Education

- J.D., *with honors,* Order of the Coif, DePaul University College of Law, 2000
- M.B.A., DePaul University, Kellstadt Graduate School of Business, 2000
- B.A., *cum laude*, Boston College, 1993

James W. Morrissey is a shareholder and a member of the firm's Financial Institutions Group and Finance and Transactions Group.

Mr. Morrissey concentrates his practice in the representation of financial institutions and corporations and their officers, directors and shareholders in connection with mergers and acquisitions, securities offerings, corporate finance, corporate governance and regulatory and compliance matters. He has represented clients in numerous bank and thrift mergers and acquisitions and securities transactions. In addition, he has represented clients with respect to various bank regulatory matters, including advising clients with respect to preparing for regulatory exams and responding to enforcement actions.

Mr. Morrissey also assists financial institutions with other strategic matters, such as new products and services and the establishment of de novo branches and banking institutions. He also speaks and writes on various financial institutions topics.

Mr. Morrissey is a member of the Illinois State Bar Association.

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Emphasis

Benefit Plans

ERISA

Executive Compensation

Education

- J.D., University of Chicago Law School, 1988
- A.B., University of Chicago, 1985

Chair, Employee Benefits Group

Philip L. Mowery joined the Chicago office of Vedder Price P.C. in the Employee Benefits Group in 1988 and became a shareholder in 1995. He counsels a variety of corporations in the manufacturing and service industries on all aspects of employee benefits law, including the design, tax qualification, legal compliance, interpretation and communication of retirement plans and welfare benefit plans. He also counsels employers and executives in the negotiation and implementation of executive compensation agreements and programs.

Mr. Mowery is a member of the American Bar Association and is a frequent speaker before legal and other professional organizations. Mr. Mowery was selected for inclusion in 2006, and from 2009 to 2011 in *Illinois Super Lawyers*.

Recent Publications

- Co-author, "Roth Conversions Inside Savings Plans: Option Now Available," *Employee Benefits Briefing*, September 30, 2010
- Co-author, "Health Care Dependent Coverage Regulations Issued," *Employee Benefits Briefing*, May 21, 2010
- Co-author, "Retiree Reinsurance Regulations Issued: Program Effective June 1, 2010," *Employee Benefits Briefing*, May 12, 2010
- Co-author, "IRS Issues Guidance on Tax Treatment of Health Care Coverage for Adult Children Under Age 27," *Employee Benefits Briefing*, April 30, 2010
- Co-author, "New Stopgap Extension of Cobra Subsidies—Further Extension Pending," *Employee Benefits Briefing*, April 19, 2010
- Co-author, "Health Care Reform Enacted: Reconciliation Continues," *Employee Benefits Briefing*, March 23, 2010
- Co-author, "Stopgap Extension of Cobra Subsidies—Further Extension Likely," *Employee Benefits Briefing*, March 3, 2010
- Co-author, "Health Care Reform Enacted... Now the Learning Curve Begins," *The Illinois Manufacturer*, Spring 2010
- Co-author, "The Senate's Turn at Shaping Health Care Reform—Reconciliation Awaits," *Employee Benefits Briefing*, January 2010
- Co-author, "Health Care Reform Passed by the U.S. House of Representatives—Future Unknown," *Employee Benefits Briefing*, November 2009

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Emphasis

Bank and Thrift Regulation and Enforcement

Finance and Transactions Group

Financial Institutions Group

Mergers and Acquisitions

Education

- J.D., Georgetown University Law Center, 1972
- Editor, *Law & Policy in International Business*
- B.A. (Economics), College of the Holy Cross, 1969 (Omicron Delta Epsilon)

Daniel O'Rourke is a senior member of the firm's Financial Institutions Group. The Financial Institutions Group (FIG), now in its 22nd year, has been recognized as one of the Ten Best U.S. Banking Law Firms by Bank Director Magazine. As a member of FIG, Dan represents banks and thrifts and their officers and directors, as well as investment banks that specialize in financial intermediaries. Dan was the first Chair of the Financial Institutions Group, which he helped organize in 1989.

Dan has been recognized annually by *Best Lawyers in America*, *Illinois Super Lawyers* and *Illinois Leading Lawyers* for his expertise in banking and corporate law. His practice includes mergers and acquisitions, corporate governance and fiduciary duty issues, bank regulatory and enforcement matters, contested corporate matters and distressed asset and institutions transactions.

Dan has authored more than twenty published articles on the strategic, legal and regulatory affairs of financial institutions and their affiliates. He is also a frequent panelist at industry conferences regarding these issues.

Dan is active in pro bono matters and is Vice Chair of Vedder Price P.C.'s Pro Bono Committee. Dan's pro bono activity includes his representation of indigents seeking to adopt disadvantaged children through the Chicago Volunteer Legal Services Foundation, where he serves on the Board of Directors. In recognition of his efforts, Dan was awarded the CVLS Distinguished Service Award twice—in 2003 and 2004. The Chicago Bar Association honored Dan for his pro bono efforts in both 1997 and 1998.

Dan is the father of five and grandfather of thirteen. He resides with his wife Kate in Winnetka, Illinois. Besides his family, Dan enjoys American history, gardening, golf, golden retrievers, weight training and college sports—especially college football (he attended Holy Cross on a football scholarship).

Bar Admissions:

- Illinois, 1972

Memberships:

- Member, The Economic Club of Chicago
- Member, American Bar Association (Banking Law Committee, Committee on Bank and Bank Holding Company Acquisitions)
- Director, Chicago Volunteer Legal Services Foundation

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Emphasis

Corporate Transactions

Financial Institutions

Executive Compensation

Education

- J.D., University of Chicago, 1970
- B.A., *cum laude*, Georgetown University, 1967 (Phi Beta Kappa)

Chairman, Vedder Price P.C.
Chairman, Executive Compensation Practice Group

Robert J. Stucker is the Chairman of Vedder Price P.C. He is also Chairman of the firm's Executive Compensation Group and a member of the firm's Board of Directors.

Mr. Stucker's practice includes advising corporations and financial institutions with respect to executive compensation, mergers and acquisitions, corporate finance, and governance matters. His corporate engagements have included acting as advisor to compensation, audit, governance, and other special committees of the boards of directors of public corporations.

Mr. Stucker is also nationally recognized for his representation of corporations, compensation committees and executives regarding the recruitment of and employment arrangements for chief executive officers. His assignments in this area have included the new CEO compensation and employment arrangements at **Albertson's**, **Aon**, **Boeing**, **Cable & Wireless**, **Campbell's Soup**, **Chubb**, **Clorox**, **Cooper Tire**, **Delta Air Lines**, **Electronic Data Systems**, **The Gap**, **Hershey Foods**, **Hertz**, **Hewitt**, **Home Depot**, **Honeywell International**, **J.C. Penney**, **Kraft Foods**, **Levi Strauss**, **Liz Claiborne**, **Mattel**, **3M**, **Nike**, **Nortel**, **Office Depot**, **Pharmacia**, **Quaker Oats**, **R.R. Donnelley**, **Tyco**, **TXU**, and **SPX Corporation**. He has also lectured and written on executive compensation and governance issues, and has been the subject of feature articles on these matters in ***The Wall Street Journal***, ***New York Times*** and the ***Chicago Tribune***.

As a current or former member of the Board of Directors for a number of private and public companies and financial institutions, Mr. Stucker served from time to time as the Chairman or a member of the Compensation Committees for several of those companies.

Active in charitable organizations, Mr. Stucker is currently a director of Northwestern Memorial Foundation; trustee of the John G. Shedd Aquarium; former member of the Alexis de Tocqueville Society Advisory Board of the United Way Campaign; former Chairman of the Board of Directors, Chicago Chapter of the March of Dimes Birth Defects Foundation; former trustee of the Glenwood School for Boys; and past Chairman of the Illinois Crusade–American Cancer Society. Mr. Stucker is also a member of the American Bar Association, The Economic Club of Chicago, and The Commercial Club.

Mr. Stucker is listed in *The Best Lawyers in America*, *Illinois Leading Lawyers* and has been recognized by his peers as one of the *Top 100 Super Lawyers* in Illinois. In 2010, Mr. Stucker was ranked in *Chambers USA*

VEDDERPRICE

Vedder Price is a thriving, business-oriented law firm that has a proud tradition of maintaining long-term relationships with our clients, many of whom have been with us since we were founded in 1952. We are an active, growing firm with offices in Chicago, New York and Washington, D.C., composed of over 265 attorneys who practice in three general areas: corporate law, labor and employment law and general litigation.

Corporate Services

The corporate practice of Vedder Price is the firm's largest practice area and provides legal services to clients ranging from large, publicly held corporations to small, emerging companies, as well as numerous partnerships and individuals. This highly regarded practice efficiently handles all types of business and financial matters for clients including:

- Antitrust
- Bankruptcy and Reorganizations
- Business Immigration
- Corporate and Commercial Finance
- Environmental
- Equipment Finance
- Estate Planning and Administration
- Executive Compensation
- Financial Institutions
- Fund Formation
- Health Law
- Insurance and Risk Management
- Intellectual Property
- International Transactions
- Investment Management
- Mergers and Acquisitions
- Project Finance
- Real Estate, Land Use and Zoning
- Records Management and eDiscovery
- Securities
- Tax
- Trade and Professional Association Law
- Venture Capital and Private Equity

Labor and Employment

Vedder Price is acknowledged as having one of the premier labor and employment law practices in the country. Clients of this practice include large national corporations, smaller professional and business corporations, multi-employer trust funds, investment managers and other plan fiduciaries in matters involving:

- Arbitration
- Collective Bargaining
- Employment Discrimination
- Equal Employment Opportunity
- ERISA and Employee Benefits
- NLRB Proceedings
- Occupational Safety and Health Law
- Union Welfare Plan Litigation
- Wrongful Discharge Cases

Litigation

Attorneys in our litigation practice handle client matters in trial and appellate courts, before administrative agencies and in arbitration and other alternative dispute resolution contexts. Our litigation attorneys have extensive experience in representing clients in matters involving:

- Alternative Dispute Resolution
- Antitrust and Unfair Competition
- Bankruptcy
- Business Torts
- Commercial Disputes
- Construction Law
- Contracts and General Business
- Distribution, Dealer Termination and Franchise Matters
- Environmental
- ERISA
- Federal Tax
- Financial Institutions
- Health Law/Medicare–Medicaid
- Insurance Coverage and Defense
- Intellectual Property
- Lender Liability
- Manufacturer Liability
- Product Liability and Toxic Tort
- Professional Liability
- Real Estate and Condemnation
- Records Management and eDiscovery
- Restrictive Covenants and Trade Secrets
- Securities Litigation and Shareholder Disputes
- Trust and Fiduciary
- White Collar Criminal Defense

Commitment to Diversity

Diversity is a high priority at Vedder Price. We are committed to enhancing the diversity of our workforce and promoting the likelihood of success for all people at Vedder Price to the best of our ability. We dedicate time, energy and financial resources to achieve our goal. Our focus includes the recruitment, hiring, retention, training, professional development and advancement of a diverse group of attorneys and other employees on the basis of demonstrated merit and performance. We also maintain and enhance an inclusive culture at Vedder Price in which individual differences are respected and appreciated, recognized as a source of strength for the firm and valued as qualities that enrich our working environment and our ability to serve our clients.

Tradition of Public Service

In addition to serving our clients, many of our attorneys participate in or otherwise support legal assistance for the indigent and other forms of community service. Vedder Price has a long history of support for pro bono services. One of the firm's founders helped establish the Legal Assistance Foundation of Chicago, and his commitment to pro bono activities was instilled in the firm and continues to this day. Additionally, the firm strongly endorses bar association and other professional activities. A number of our attorneys have served on and chaired committees of the American, Illinois and Chicago Bar Associations. The Chair of the firm's Construction Law Practice Group served as the first woman President of the Seventh Circuit Bar Association. A Litigation Shareholder served as President of the Chicago Inn of Court. Other attorneys have authored treatises or undertaken various teaching, writing and speaking responsibilities and continue to do so. The firm encourages and supports the public service activities of its attorneys.