WE HELP COMMUNITY BANKS COMPETE MORE EFFECTIVELY

AUGUST 2016

ACBB

ATLANTIC COMMUNITY BANKERS BANK

In This Issue:

DE NOVO BANKING

BY JON EVANS

Jon Evans
President & CEO, ACBB

The question of new chartered banks surfaced again when FDIC shortened the period of increased capital requirements for de novos from seven years back to three. This should help the TWO de novo banks that have been chartered since 2010 but really doesn't address the full scope of regulatory actions which could be implemented to further stimulate de novo activity.

First a look at the numbers. From 2000 to 2010 there were 1,215 de novos banks chartered in the U.S. Since 2010 there have been two – Bank of Bird-in-Hand (Bird-in-Hand, PA) and Primary Bank (Bedford, N.H.) During the same period the number of insured commercial banks declined from 9,904 to a little over 6,000 institutions.

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There are too many headwinds such that a new regulatory approach is needed. Granted, investor enthusiasm is lacking. Albeit, even with a flat yield curve, an uncertain economy, and misguided legislation, much more can be done from the regulatory agencies.

First, FDIC needs to establish reasonable capital requirements and be transparent about them. I have gotten calls from potential organizing groups expressing their frustration that they cannot get a straight answer relative to the capital requirements needed. How about this, establish a minimum range for rural de novos (i.e. $12mm - $15mm) and a range for metropolitan de novos ($15mm - $25mm). The various state banking departments would be forced to follow suit because of the insurance aspect.

Next, implement a simplified approach to the examination process that focuses on the quality of audits, basically audit the audits and this includes compliance. This could also be applied to all banks under $1 billion in assets. Having a dozen examiners in a small bank for three weeks is not only an inefficient use of resources but inhibits the entrepreneurial spirit.

Finally, a new regulatory approach to concentrations, specifically CRE lending. The 300 bucket is too restrictive and more emphasis should be given as to how the institution is managing its risk,

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WELCOME NEWEST CUSTOMERS

Optima Bank and Trust Company
Portsmouth, NH

Commonwealth Cooperative Bank
Hyde Park, MA

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Follow us now!

FINANCIAL HIGHLIGHTS (consolidated)

BALANCE SHEET (in thousands)

	Unaudited	Unaudited
ASSETS	**6/30/16**	**6/30/15**
Cash and Due from Banks	$188,874	$162,405
Investment Securities	85,816	80,929
Federal Funds Sold	54,981	79,639
Loans, net	208,130	202,660
Other Assets	35,176	30,953
Total Assets	**$572,977**	**$556,586**
LIABILITIES AND CAPITAL		
Deposits	$357,782	$378,111
Federal Funds Purchased	84,997	70,745
Other Borrowed Money	46,817	28,031
Other Liabilities	6,720	7,001
Total Liabilities	496,316	483,888
Equity Capital	76,661	72,698
Total Liabilities and Capital	**$572,977**	**$556,586**
INCOME STATEMENT (in thousands)		
Interest Income	$6,682	$5,816
Interest Expense	1,244	965
Net Interest Income	5,438	4,851
Provision for Loan Losses	(395)	(410)
Realized Gains (Losses) on Securities	0	0
Non-interest Income	6,983	6,222
Operating Expenses	9,223	8,928
Taxes	1,124	769
Net Income	**$2,469**	**$1,786**

SAME DAY ACH-FASTER PAYMENTS PUSH AND WHAT IT MEANS FOR YOUR BANK

BY VIRGINIA WRIGHT, AAP

NACHA, acting as the gatekeeper to the Automated Clearing House network, has been working relentlessly to provide faster payments to all entities involved in the ACH network. Their efforts have resulted in an almost unanimous vote from the membership to add a rules change incorporating the ability to send ACH payments and have these payments settle on the same day that they are sent through the network. This new rule, commonly referred to as Same Day ACH, has community banks anxious to fully understand how it will affect their operational process, as well as concern for the changes they will be required to make in order to comply. The Same Day ACH rule does not allow any institutions that receives ACH to "opt out" as this would have an adverse affect on the Originating Depository Financial Institutions that offer this service to their originators of ACH.

Ultimately, this new rule will allow for approximately 99% of the ACH payments to be eligible for same day processing. The exclusions to the rule are IAT entries and any transactions over $25,000. Once the rule is completely implemented, funds will need to be made available to the receiver by 5pm local time. In addition, this rule includes compensation from the ODFI to the RDFI per same day entry.

Although the rule seems clear, many questions may arise from

(Continued on next page)

SUMMARY OF FINANCIAL HIGHLIGHTS AS OF JUNE 30TH

YTD Net income of $2,469,000, was $683,000 above 2015 year to date. Several one-time income events helped drive non-recurring profits, including additional interest income from the resolution of problem loans, a gain on the sale of an OREO property, one-time extraordinary gain from ACBB-BITS and a $395,000 credit to the loan loss provision in June. Excluding all non-recurring items, core income was ahead of June 2015 by 13.8% and exceeded the 2016 budget by an average of $38 thousand per month.

STRONG CAPITAL LEVELS:

Total Risk-Based Capital ratio = 26.26%

Tier 1 Risk-Based Capital Ratio = 24.97%

Leverage Capital Ratio = 12.92%

FUNDING DIVERSIFICATION AND BALANCE SHEET RESTRUCTURING:

Net loans increased $5.5 million year over year.

Other borrowed money increased by 67% over June 2015 as maturing CDs have been replaced with long-term FHLB advances to fund new long-term loans.

CREDIT QUALITY:

2016 YTD charge-offs were $12,000, while recoveries totaled $24,000.

Past due loans still accruing were 0.1% of gross loans as of June 30, 2016

Robust loan loss allowance despite provision credit as illustrated below:

- ALLL to Total Non-Current Loans of 445.68%
- ALLL to Total Loans of 3.41%
- Texas ratio of only 4.29%

OTHER RATIOS

Return on Average Assets	0.86%
Return on Average Equity	6.57%
ALLL to Non-performing Loans*	294.30%
Non-performing Assets to Total Assets	0.63%

* Includes performing TDRs

("Same Day ACH" continued from Page 2)

banks as they navigate the rule. In particular, agreements and disclosures will need to be updated. Decisions will need to be made about how much your bank will embrace Same Day ACH. This may include exception processing, pricing and consideration for offering the product to your originators. Policies and procedures will require reviewing and updating as well as more concentration on monitoring for additional fraudulent activity.

As this is the biggest change the ACH network has ever experienced, NACHA has implemented three phases to ease all participants into their new role. The first phase, which focuses on credits, begins on September 23, 2016. The second phase introduces the debits into the Same Day ACH arena. This phase is scheduled to begin on September 17, 2017. The third and final phase will begin in March of 2018. Many people believe this last phase that begins on March 16, 2018 is the most concerning as the 5pm availability of ACH credits for the receivers may result in operational staff scheduling changes.

As this is the biggest change the ACH network has ever experienced...

There is a considerable amount of good information to help all participants steer clearly through this new rule. You can access resources, guidelines, checklists and support networks by simply doing a web search and typing in "Same Day ACH". NACHA, FRB, as well as your Regional Payment Associations are all terrific resources to assist your bank. Both NACHA and FRB frequently post and update Same Day ACH information to their websites so remember to check in periodically for the latest available information. Phase One is right around the corner; do you know what your bank is doing to prepare for Same Day ACH?

ACBB wants to congratulate Virginia for becoming certified by NACHA as an Accredited ACH Professional. Virginia is also a member of The Clearing House Payments Authority AAP Alliance group. Virginia's primary focus here at ACBB, is training and implementation of our new customers as well as specializing in products that ACBB offers our member banks. You may meet Virginia personally as she has begun visiting our banks to manage customer relations and offer personalized customer support. If you'd like to schedule a meeting with Virginia or simply have a question, call (717) 441-4506 or email vwright@acbb.com .

ACBB DIRECT LENDING

BY WILLIAM SAYRE

As you likely have read in various industry publications and heard at trade events and conventions, the subordinated debt market for bank holding companies, and to a lesser extent banks, has become popular as an option within the capital/debt structure for community banks. After being largely quiet and untapped throughout the financial crises and its aftermath, this has become an increasingly viable option over the past 18 to 24 months, particularly as the rate on SBLF increased to 9%.

What you may not be aware of is that ACBB has a potential financing alternative to subordinated debt and has provided credit to bank holding companies for the past decade. ACBB provides senior debt to bank holding companies both for liquidity purposes as well as for capital purposes where the holding company down streams funds to its subsidiary bank to supplement equity capital and/or more recently to assist with

("Direct Lending" continued on next page)

("De Novo Banking" continued from page 1)

the institution's historical performance, and their level of capital. What better way to foster jobs than facilitating small business lending, which usually has commercial real estate attached to it.

We must also acknowledge some progress made with regulations. We now have an eighteen month examination cycle with the above mentioned elevated capital requirement of only three years for de novos. There are also other initiatives to lower regulatory burdens, especially for the community banks.

Positives for the community banking industry include: new technologies to level the playing field, great relationship bankers, strong balance sheets, and state and national banking trade agencies that continue to gain legislative and regulatory victories for smaller banking institutions.

De novo banks, which help maintain a community bank presence in the country, are vital for providing access of capital to the little guy. In my personal travels, I see this more than ever when rural banks are acquired and no de novo banks replace them. The community has less access to capital, fewer jobs, and far less in the way of charitable efforts, including contributions.

The people who live in these towns are people of character. Let us not forget Amadeo Pietro Giannini who started a de novo bank in San Francisco, California in 1904. Two years later, after the earthquake and fire, he made character loans so the people could rebuild. That institution is now Bank of America and his actions were the best example of CRA lending I can think of.

YOUR BULLETIN BOARD

Compliance Anchor 2016 Upcoming Events

Compliance Anchor®

Webinars

Sept 13 - Harnessing Social Media Fears for Community Banks

Oct 13 - Cyber Security Trends and Their Impact on Community Banking

Nov 29 – HMDA - Change is A-Comin'!

*Look for a Marijuana webinar in November!

Veterans' Venues:

BSA	Compliance
Sept 7	Sept 29
Oct 4	Oct 27
Nov 1	Nov 17
Dec 6	Dec 15

Please visit www.acbb.com/compliance for more information on Compliance Anchor.

Interested in becoming a Compliance Anchor Subscriber? Contact Nancy Lake at (717) 441-4507 or via email at nlake@ acbb.com.

("Direct Lending" continued from page 3)

real estate concentration issues. ACBB initiated this product during the time de novo bank activity was strong to assist as a bridge to secondary capital offerings and subsequently supported a number of member banks with facilities through the financial crisis. More recently we have experienced increased demand as the Small Bank Holding Company Act increased its asset threshold to $1 Billion (helpful for the Holding Company's minimum capital requirements, but not critical) and member banks considered options to payoff SBLF and supplement capital as loan and asset growth has picked up.

ACBB offers both short term annually renewable facilities for liquidity and intermediate term facilities, typically up to 36 months on an interest only basis as a "bridge". Loan size generally ranges from $2 to $5 Million with larger loan facilities and longer term facilities typically entailing a pledge of the bank's stock. For banks that do not need to retain all of their earnings to support growth but can pay down the principal via strong dividends from the bank, amortizing term options are available. Pricing is generally significantly cheaper than subordinated debt, and ACBB is strictly interested in supporting its member banks – not buying them. Both fixed and floating rate options are available, and the facilities carry limited covenants and conditions with relatively simple and cost effective documentation.

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A core part of ACBB's business is providing direct loans to bank holding companies, loans to directors, executive officers and major shareholders, which are secured by member community banks' stock, and assisting in Reg "O" situations. Loans underwritten based on the personal credit and cash flow of the borrower are generally margined at 50% of the value (book or market, bank dependent) of the stock and are typically offered on an amortizing term basis, although interest only lines are also considered.

For more information please contact William Sayre at 717-441-4714 or WSayre@acbb.com.

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COMPLIANCE ANCHOR WELCOMES PATTI WEAVER, CRCM!

Our Compliance Anchor monthly subscriber number continues to grow as we have a number of new banks that have joined us over the past few months. Those banks are enjoying the wealth of information provided in our Compliance and BSA Veterans' Venues as well as the various webinars we present. Others have purchased our Director Training that covers all the recommended training topics in over 110 Power Point slides.


Patti Weaver
Compliance Consultant

Now we are pleased to announce that Patti Weaver has joined our Compliance Anchor team as a Compliance Consultant. Patti has over 20 years experience in banking and received her Certified Regulatory Compliance Manager (CRCM) certification in 2015. She has held a variety of roles in community banks. Starting her career as a teller, Patti quickly moved up the ranks by becoming a Head Teller, an Accounts Representative and eventually a Branch Manager. As a Branch Manager her responsibilities expanded into the lending area and included secured/ unsecured loans, real estate consumer lending as well as small Commercial and Agriculture lending. She then utilized her wealth of experience to train other employees in all levels of banking from new hires to Board of Directors. Most recently, she was a Compliance and BSA Officer at a de novo community bank responsible for all aspects of the bank's compliance management program.

Most recently, she was a Compliance and BSA Officer at a de novo community bank responsible for all aspects of the bank's compliance management program.

When she is not busy assisting our community banks, Patti enjoys running not only in Lancaster County, where she was born and raised, but all across the country. She combines her desire to see new places with races in various states. Her races have taken her to 12 states so far including New York, Texas, and California. Her proudest moment was when she recently completed a marathon that qualified her to run in the Boston marathon. Patti also enjoys traveling internationally. She lived in Germany several years and has visited Thailand, Bali, Austria, Switzerland and Italy. Her favorite place to visit is Italy as her 5 trips there confirm.

Patti is the proud mother of two sons and one grandson and enjoys playing her flute and gardening. She also volunteers in various ways including as a merit badge counselor for the Boy Scouts of America, serving on the Youth Aid Panel, and teaching with Junior Achievement. You might also see her with a hard hat and a hammer in her hand or driving a back-hoe helping to rebuild homes with Habitat for Humanity or the Lutheran Disaster Relief teams after natural catastrophes.

Patti will be utilizing her compliance and banking experience to help Compliance Officers apply regulations to everyday processes. She will also be developing training and tools to assist bankers in meeting compliance challenges. Patti can be reached at 717-441-4696 or via email at pweaver@acbb.com.