Testimony of

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Before the
United States House of Representative
Committee on Financial Services
And
Committee on Small Business

Hearing on Lending
February 26, 2010
Washington, DC

Chairman Frank, Chairwoman Velazquez, Ranking Member Bachus, Ranking Member Graves and Members of the Committees, my name is David Bridgeman, and I am the CEO and President of Pinnacle Bank in Orange City, Florida. I have risen through the ranks in community banking, starting out as a teller 28 years ago. I have been with Pinnacle Bank since it opened for business in 1999, and became the CEO in 2003. I care deeply about the success of the Bank, small-business customers, and my community.

I am honored to have this opportunity to share my experiences and give you a current capsulized assessment of community banking, and the challenges impacting small business and commercial real estate credit availability. Community banks are the life blood for small business in America. It is the community banker that makes the $10,000 loan for equipment, inventory, or working capital--not the TBTF (too big to fail) banks. I do not compete against the TBTF institutions for the small owner-occupied real estate loan or small business loan; however, I compete every day for the deposits that those institutions are taking out of my community.

Although community banks hold only around 11% of total industry assets, community banks originate 38% of all small business and farm loans. According to the Federal Deposit Insurance Corporation ("FDIC"), banks with less than $1 billion in assets make more than half their loans to small businesses. In such a precarious point in our economic cycle, cutting lending to small businesses and farms could exacerbate existing pressures on the economy, leading to an increased probability of a double-dip recession.

Community banks understand the economic problems facing their respective communities. We know our customers by name. For example, recently a man sat across from me and wept because his business was struggling to the point that he had to lay off several long-term employees. We see first-hand what is happening to the small businesses in our communities. Community banks across my state and around the nation are seeing the same crisis as their business customers. It is the small business person who creates 60% of the jobs in this country and, therefore, it is through the efforts of the community banks that local economies, and ultimately our national economy, will be revitalized.

Pinnacle Bank

Pinnacle Bank is a state non-member bank regulated by the FDIC and the Florida Office of Financial Regulation, with $220 million in total assets. Pinnacle did not make the subprime or exotic risky mortgages nor did we invest in complex derivative securities that led to the current economic crisis. Pinnacle Bank ranks well in asset quality among its Florida peers. Pinnacle Bank has always been an active business oriented institution, providing credit to small businesses, the creators of most jobs in communities. The focus of our lending has been toward owner-occupied commercial real estate and C&I loans, with the loan portfolio mainly consisting of loans to local businesses. Pinnacle Bank is also one of the most active SBA lenders in Florida.

In spite of the economic turmoil of the last two years, we have continued to lend. In November and December of last year, Pinnacle Bank was the second largest SBA lender in North Florida. Our modest loan growth, however, was criticized as being too aggressive by the FDIC field examiners during our most recent examination.

In April 2008, Pinnacle Bank chose to participate in the TARP Capital Purchase Program to infuse $4.4 million into capital. We did not need a bailout. To qualify for the TARP-CPP, unlike the TBTF banks, a community bank had to be in a strong position in terms of capital, composite ratings and other factors that regulators use to determine a bank's condition. We saw the capital as a way to continue lending--as traditional sources of capital ceased to exist. During our recent examination exit meeting, however, the FDIC Examiner in Charge advised our Board of Directors that "TARP-CPP funds should specifically be used for increasing capital ratios and loan loss reserves." We understand that Congress' intent for TARP was to ensure access to credit for business customers. There exists a glaring disconnect between Congress and the field examiners' message to community banks.

We ended 2009 in a strong capital position. Pinnacle Bank is a "Well-Capitalized" institution by all regulatory measures. For year-end 2009, the Bank had a Total Risk-Based Capital to Assets Ratio of 11.61%, a Tier 1 Leverage Ratio of 8.14% and a Tier 1 Risk-Based Capital Ratio of 10.34%. To be considered well capitalized under regulations, a bank should have a total risk-based capital ratio of 10%, a Tier 1 leverage ratio of 5% and Tier 1 risk-based ratio of 6%. Despite the Bank's strong capital position following its field examination, the FDIC field examination staff is recommending that our capital status be downgraded to "Adequately Capitalized." Why, because we are a Florida bank, with Florida real estate as collateral. We believe this arbitrary capital downgrade will impede lending and place Pinnacle Bank under unnecessary stress. This example of heavy handedness from the regulators is ultimately obstructing the economic recovery.

Challenges

There are several challenges for community banks to continue to lend to small businesses. First, there is a shortage of small businesses that can qualify for loans. Small businesses throughout the country have suffered significantly during this recession and their financial statements are in shambles. Viable businesses with good credit histories and reasonable equity cannot obtain loans because their income and liquidity to support debt repayment are not sufficient for banks to make a loan using prudent underwriting standards. We believe attempts by community banks to lend to these viable businesses are being met with significant criticism from the regulators.

A second challenge to community banks is the current regulatory environment. I would like to refer to the letter written by Congressmen Barney Frank and Walt Minnick dated October 29, 2009. Their letter very accurately describes what I and many of my CEO peers have experienced, that the field examiners have become "overzealous." My bank was examined in November / December 2009.—The FDIC field examiners, in my opinion and the opinion of external auditors, were unduly harsh in their examination. They used PCA (Prompt Corrective Action) as a tool to require subjectively higher capital ratios, as well as much higher unjustifiable loan loss reserves.

Additionally, the FDIC examiners are downgrading other components of a bank's CAMELS ratings, based solely on deteriorating asset quality without recognizing the significant economic down-turn that has negatively impacted our entire nation. The examination manuals require that examiners take into account the current economic environment that a bank is operating under, but from our recent experience, this does not appear to be happening. Instead examiners rate the bank without considering the effect of the economy and then express concern about the bank's condition and future in light of the economy, applying a double effect of the economic environment to the bank. These actions have forced community banks to stop lending in an effort to meet these new higher ratios in an attempt to correct regulatory criticisms.

After the toughest examination in my 28 years in banking, Pinnacle Bank, which is well-capitalized and well reserved by all measures provided in the regulations, is about to find itself in the position of having to suspend lending to satisfy unwritten capital and reserve requirements imposed by FDIC examiners. If we are to get our economy growing, we need to support community bank lending to small businesses, not impose arbitrary regulatory barriers to lending and unreasonable criticism for working with our customers.

Policies set in Washington and the policies that are enforced in the field by the federal examiners should be one and the same. Congress, the Administration and the heads of the banking agencies have designed programs and instituted regulatory policies to encourage community banks to lend to small businesses and to work with existing borrowers. As an example, the FFIEC policy statement entitled *Prudent Commercial Real Estate Loan Workouts* dated, October 30, 2009, encourages banks to work with our borrowers in an effort to keep businesses open and people employed. The FDIC examiners during my examination, however, were critical of work out arrangements (Troubled Debt Restructures – "TDR's") with customers even though our customers were paying as agreed, keeping businesses open and people employed. We were told these businesses were highly likely to fail and, therefore, have a negative impact on the Bank.

Another problematic regulatory issue for small business lending is the Community Real Estate ("CRE") Guidance. The CRE Guidance is for measuring risk in loan portfolios and developing policies and procedures to monitor and mitigate those risks. Currently, regulators are taking categories of concentrations within loan portfolios and criticizing banks for having too much concentration in areas that they deem to be risky, even if the risk has been mitigated and proper monitoring put in place. Federal regulators are taking the CRE Guidance and applying it as though it were a regulation. Federal regulators are using CRE concentrations as a yardstick for risks inherent in the portfolio, even if the portfolio is geographically diversified. Federal regulators are also recommending that community banks reduce CRE lending and even sell some existing CRE loans that have been rated "Substandard" or worse. Of course, any loan sales in the current real estate environment yield only a fraction of the value of the loan and cause community banks to take additional losses. This action, combined with arbitrarily higher capital requirements and higher reserve requirements, is again forcing banks to cease funding on lines of credit, demanding that lines be paid and withdrawing funding from new or existing commercial real estate projects.

Summary

The current regulatory environment is having a debilitative affect on local lending. Regulators must take a more positive approach to the examination process and understand that their actions are having a profoundly negative effect on the economy, communities, and job creation. It is imperative that the goals of Congress, the Administration and the federal banking regulatory agencies be the same— regrettably today they are not. Community banks want to lend to our small businesses and be a catalyst to economic recovery, but the federal regulators need to change their Supervisory Policy toward community banks to allow viable community banks to work through their issues and these difficult economic times.

Thank you for the opportunity to allow me to express my views on some of the more pressing challenges facing community banks.

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