

# How a troubled bank used listing service deposits to avoid failure

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Internet listing service deposits helped one South Carolina community bank avoid failure long enough to recapitalize, but its CEO believes they will play a minor role in the bank's healthy future.

Executives at Loris, S.C.-based HCSB Financial Corp. and unit Horry County State Bank are working to turn around the institution. One of those steps will be reducing the certificates of deposits that came from listing service websites. Listing service CDs share some similarities with brokered CDs, including their high-rate and nonlocal nature, but do not face the same regulatory prohibitions as brokered deposits, which are prohibited from being acquired by troubled banks.

## Financial snapshot for Horry County State Bank

	2012	2013	2014	2015	Q1'16
<b>Balance sheet (\$M)</b>					
Total assets	469.0	434.6	421.5	361.4	363.4
Total loans	302.2	256.4	235.5	209.4	199.6
Total deposits	436.1	406.3	391.5	330.9	335.6
<b>Balance sheet ratios (%)</b>					
Loans/deposits	69.31	63.12	60.17	63.28	59.49
Tier 1 capital	2.23	3.07	3.79	4.67	3.91
<b>Profitability (%)</b>					
ROAA	-1.52	0.45	0.25	0.30	-3.21
ROAE	-63.70	33.65	14.54	11.47	-121.71
Net interest margin	3.24	3.19	3.12	3.07	2.96
Efficiency ratio	92.94	97.90	86.25	91.78	203.40
<b>Asset quality (%)</b>					
NPAs/assets	13.59	13.23	11.56	12.46	10.88
NCOs/average loans	5.20	1.15	1.89	0.53	4.50
Reserves/loans	4.68	3.68	2.46	2.20	1.86

Data compiled July 6, 2016.

Based on regulatory filings as of March 31, 2016.

Total loans includes those held for sale.

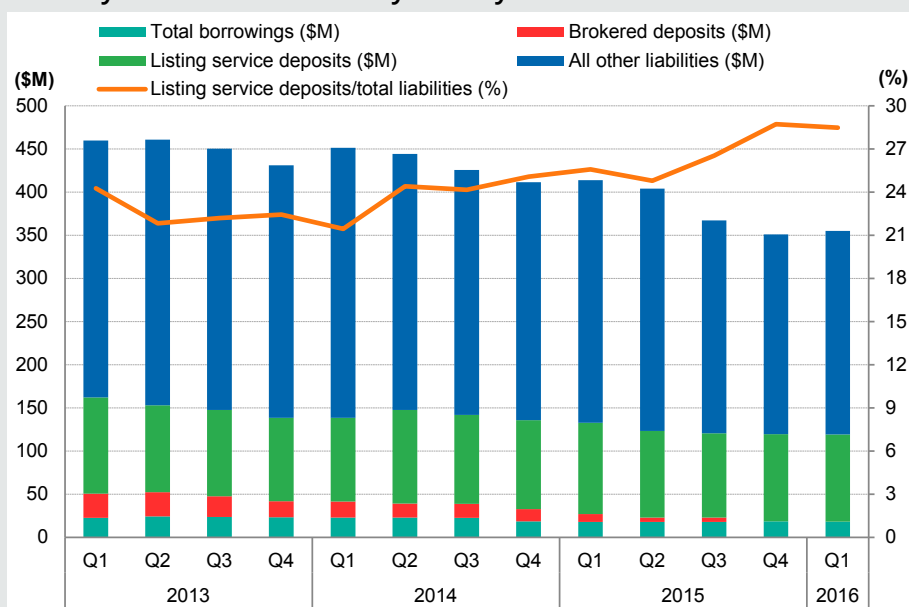
Net interest margin and efficiency ratio are on a fully-taxable equivalent basis.

ROAA = return on average assets; ROAE = return on average equity

NPAs = nonperforming assets; NCOs = net charge-offs

Source: SNL Financial, an offering of S&P Global Market Intelligence

## Liability breakdown for Horry County State Bank



Data compiled July 6, 2016.

Based on regulatory filings as of March 31, 2016.

Total liabilities exclude minority interest.

The FDIC defines a brokered deposit as any deposit that is obtained, directly or indirectly, from or through the mediation or assistance of a deposit broker. This can include brokered CDs, prepaid cards and various other relationships or products.

Listing service deposits are reported in call reports as estimated deposits obtained through the use of listing services that are not classified as brokered deposits. Listing services advertise rates from depository institutions and receive compensation from either those companies soliciting deposits or customers shopping for deposit accounts.

Source: SNL Financial, an offering of S&P Global Market Intelligence

Horry County's troubles stemmed from a combination of rapid growth, bad timing and expensive funding sources, said CEO Janet Hollar. Horry fueled rapid growth between 2007 and 2009 and replenished its capital with a mix of funds consisting of subordinated debt and TARP but ran into financial stress that resulted in a 2011 cease and desist order prohibiting it from accepting, renewing or rolling over brokered deposits.

Horry went to QuickRate to replace the brokered deposits, Hollar said, referring to one of two popular websites for listing service deposits. "The thing I don't quite understand is why the regulators don't allow banks to have brokered deposits but they do allow them to have internet deposits. My honest feeling is that many banks and possibly this one would've failed without internet deposits."

QuickRate declined to comment directly on the subject matter and referred to listing service deposit resources from the FDIC. National CD

## Undercapitalized banks, thrifts by reliance on deposit listing services

Company (top-level ticker)	Total assets (M\$)	CET1 ratio (%)	Deposits from listing services*			Brokered deposits/ deposits (%)
			Estimated balance (\$M)	Concentration <sup>1</sup>		
				Q1'16 (%)	YOY change (pps)	
Proficio Bank	106.7	4.19	97.7	96.91	-0.19	0.00
First State Bank	34.5	4.71	14.4	43.17	1.60	0.00
Pinnacle Bank	126.5	4.15	50.4	42.59	2.14	4.36
Affinity Bank	275.1	6.12	76.2	33.88	-1.97	0.00
Horry County State Bank (HCFB)	363.4	3.91	101.1	30.12	3.30	0.00
Bank of Commerce	211.3	3.83	45.6	26.84	-7.05	0.00
First City Bank of Florida	216.8	3.38	46.3	23.06	-2.24	0.00
Fayette County Bank	34.4	6.49	7.3	22.31	-5.32	38.12
McHenry Savings Bank	253.1	6.60	42.6	18.53	3.53	0.00
Beach Community Bank (BCBF)	538.3	3.99	81.6	16.66	1.41	0.00
Farmers & Merchants Bank	543.2	4.21	78.2	15.06	-0.48	0.00
Seaway Bank and Trust Co.	373.0	5.53	35.6	11.89	7.01	0.53
Lafayette State Bank	78.9	5.18	8.3	11.06	-5.37	5.30
Cecil Bank (CECB)	253.2	3.53	13.3	6.88	-0.15	0.00
American Patriot Bank	62.6	2.03	4.1	6.70	-3.10	0.00
First South Bank (FSBS)	244.4	5.20	14.5	6.63	-1.10	0.00
Civis Bank	108.7	5.93	3.0	2.93	-3.34	0.00
Foothills Community Bank	69.7	2.52	1.8	2.71	-2.98	0.00
Gulf Coast Community Bank	132.5	5.03	0.8	0.72	-3.05	0.00
Cornerstone Bank	240.7	5.36	0.2	0.10	-1.78	0.00
Community Bank & Trust - West Georgia	84.2	6.85	0.0	0.00	0.00	0.00
First Southern Bank	107.5	6.71	0.0	0.00	0.00	0.00
Guaranty Bank (MHC) (GFCJ)	1,025.1	-3.81	0.0	0.00	0.00	0.00
Gwinnett Community Bank	335.0	3.89	0.0	0.00	0.00	0.00
Harvest Community Bank (HCBP)	138.8	2.92	0.0	0.00	0.00	0.00
Illinois-Service Federal Savings and Loan Association	101.0	4.19	0.0	0.00	0.00	0.00
Woodbury Banking Co.	22.4	4.91	0.0	0.00	0.00	0.00
<b>Group median</b>		<b>4.21</b>		<b>6.88</b>	<b>-0.85</b>	<b>0.00</b>
<b>Industry median</b>		<b>12.89</b>		<b>3.96</b>	<b>0.22</b>	<b>2.62</b>

Data compiled July 6, 2016.

Based on regulatory filings as of March 31, 2016.

Company analysis includes currently operating commercial banks, savings banks, and savings and loan associations with a Tier 1 leverage ratio less than 4%, a common equity Tier 1 capital ratio less than 4.5%, a Tier 1 capital ratio less than 6% or a total capital ratio less than 8%.

Industry analysis includes commercial banks, savings banks, and savings and loan associations that reported a non-zero balance of estimated deposits from listing services for the first quarter of 2016. Excludes banker's banks.

\* Reported by banks and thrifts in call reports as estimated deposits obtained through the use of listing services that are not classified as brokered deposits. Listing services advertise rates from depository institutions and receive compensation from either those companies soliciting deposits or customers shopping for deposit accounts.

The FDIC defines a brokered deposit as any deposit that is obtained, directly or indirectly, from or through the mediation or assistance of a deposit broker. This can include brokered CDs, prepaid cards and various other relationships or products.

<sup>1</sup> Represents banks' estimated deposits from listing services as a percentage of total deposits.

CET1 = common equity Tier 1; YOY = year-over-year; pps = percentage points

Source: SNL Financial, an offering of S&P Global Market Intelligence

Rateline, another popular listing service website, did not return calls seeking comment.

The FDIC defines a listing service as a company that compiles information about CD interest rates, whereas a deposit broker actually "facilitates" the placing of a deposit, according to a 2004 Advisory Opinion authored by

agency counsel Christopher Hencke. The FDIC can prohibit undercapitalized banks from accepting, renewing or rolling over brokered deposits, including CDs. But there are no such prohibitions on accepting nonlocal CDs from listing services, which also count as core deposits for regulatory purposes. Listing service deposits have been found in rela-

tively high concentrations at failed banks in recent years since the FDIC began requiring banks to report concentrations on call reports in 2011.

Regulators have noted that listing service deposits may be an unstable source of funding for banks; they allow banks to acquire a high amount and volume of deposits “simply by increasing interest rates,” according to a 2011 FDIC Study on Core Deposits mandated by the Dodd-Frank Act. The study said examiners have viewed them as “potentially more volatile” than local deposits.

“The analysis also suggests that high rate deposits and non-brokered listing services appeared likely to pose problems similar to most brokered deposits,” the regulator’s study stated. At time of publication, there was not enough evidence to undertake a statistical analysis of listing service deposit data; the regulator has not done a study on the issue since or considered updating the treatment or approach to these deposits.

Listing service deposits make up a small part of the total deposit market. They represented a median of 3.96% of the banking industry’s deposits and declined nearly 9% in aggregate from year-ago levels.

But they are more common among undercapitalized banks. An S&P Global Market Intelligence analysis found that of 27 undercapitalized banks, 13 reported concentrations of listing service deposits that exceeded 10%. These banks are excluded from the brokered deposit marketplace; only well-capitalized banks can accept those funds without regulatory restrictions, said Paul Clark, a partner at

Seward & Kissel LLP who represents the brokerage industry. A bank that is experiencing asset problems may also benefit from the deposits counting as core for regulatory purposes, but Clark disputed that they behave like other core funds that are normally “very stable” because of relationships between the customer and bank.

“If you have to go into the marketplace and bid up the rate to get it from people you don’t know or otherwise have a relationship with, it does raise a question of how stable it really is,” he said.

Listing service deposits staved off a liquidity crisis at Horry County even as it faced serious asset-quality issues, with nonperformers exceeding 10% of assets since 2011. Listing service deposits made up 30.12% of total deposits at the end of the first quarter. Shortly after that, the bank conducted a \$2.3 million capital raise and hired Hollar as CEO. Horry County’s Tier 1 risk-based ratio was 3.91% and its overall risk-based capital ratio was 5.17% at the end of the first quarter.

For her part, Hollar recommended that any bank nearing a troubled situation or liquidity crisis utilize listing service deposits, but she said the funds will play a much-reduced role as Horry County moves toward financial health. She said listing service deposits and brokered deposits should never make up more than 10% of total deposits. The deposits are more expensive than a local deposit, and she said Horry County needs to be focused on servicing its surrounding community and hopes the recap will restore local depositors’ confidence in the bank.