www.theBHCA.org — Summer 2012

Bank Owner

The magazine of the Bank Holding Company Association

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Spring Seminar speakers encourage unified ERM approach

Advantages — and disadvantages — of subchapter S incorporation

Source of strength in the Dodd-Frank era

List: Holding companies in North and South Dakota

The BHCA 2012 Board of Directors welcomes Spring Seminar attendees

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The following associations also have BHCA Associate Member status:

Wisconsin Bankers Association

Community Bankers of Wisconsin

North Dakota Bankers Association

Independent Community Banks of North Dakota

Independent Community Bankers of Minnesota

Iowa Bankers Association

Minnesota Bankers Association

South Dakota Bankers Association

Independent Community Bankers of South Dakota

Montana Bankers Association

Upper Midwest Automated Clearing House Association

Independent Community Bankers of America

The Bank Holding Company Association

Our mission:

The mission of the Bank Holding Company Association is to provide educational information through seminars, forums and publications useful to bank owners and holding company managers.

Our organization:

The Bank Holding Company Association, founded in 1981, welcomes Members from around the country. Holding companies of all sizes from throughout the Midwest make up a majority of the current membership. Companies that serve bank owners, their holding companies and banks, are welcomed as Associate Members. The BHCA is run by a 10-member board of directors and a managing director.

Our magazine:

Bank Owner magazine is the quarterly publication of the BHCA. It is your best source for information about bank holding company and bank ownership issues. The magazine also is your best source for BHCA information, including upcoming events. Members receive the magazine in the mail and have access to an online version in the members-only section of our web site, www.theBHCA.org. The magazine also is distributed to bank owners and holding company professionals who are excellent candidates for membership.

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Summer 2012

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Note the date

CALENDAR

July 17 — BHCA-ICBM Regulatory Forum, Riverwood National Golf Course, Otsego, Minn.
Sept. 13 —Webinar: *Bank acquisition and valuations...to sell or not to sell*
Oct. 4-5 — 2012 Fall Seminar, Bloomington, Minn.
Oct. 5 — BHCA annual meeting, election of new officers
Oct. 5 — Night out at the Chanhassen Dinner Theater, "Bye Bye Birdie"
Fall — Three-part webinar series for outside directors. Time and dates TBA
Nov. 15 — Webinar: *Emotional issues surrounding succession planning*
May 6-7, 2013 — 2013 Spring Seminar
Register for events online at www.theBHCA.org

BHCA offers first-rate education through webinars, seminar breakout sessions

By Bruce Ferden
Frandsen Financial Corporation, Arden Hills, Minn.

One of the things I am most pleased about at the Bank Holding Company Association is the association's foray into the world of webinars. BHCA is an educational organization and in addition to our two seminars each year, webinars are proving to be an excellent way to deliver educational information.

We have scheduled four webinars this year; in my first quarter column I wrote about the February 9 webinar we presented on "Making the most of your holding company charter." We had another webinar on May 24 (Tax and estate planning for bank owners) and future webinars are scheduled for Sept. 13 (Bank acquisitions and valuations... to sell or not to sell) and Nov. 15 (Emotional issues surrounding succession planning). You can register for either of the upcoming webinars on our website, www.theBHCA.org.

Also, at our last board meeting we agreed to create a three-part webinar series aimed specifically at outside directors, addressing bank board essentials, key ratios and the Bank Secrecy Act. We expect to offer these in October, November and December. Watch for specific information to come out soon on these new webinars.

The Spring Seminar was a great success. You can read about it in this magazine. Our coverage focuses on material presented by consultants Jeff Gerrish, Tom Farin and Tim Koch. Gerrish and Farin also presented during our breakout sessions. Jerry Kissell of McGladrey & Pullen was another breakout session presenter; his comments on the differences between subchapter S incorporation and C corporations are the subject of another article in this magazine.

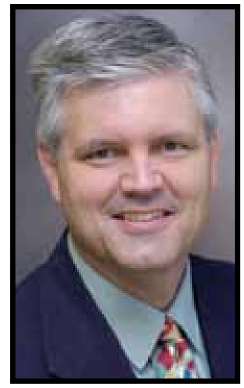
I want to acknowledge the work of two other breakout session presenters. Josh Kiefer of County Club Capital Markets presented a very interesting session on mortgage backed securities, and Tom Lynch of the Executive Compensation Institute provided an informative session on succession planning. Part of Kiefer's presentation had to do with adjustable rate mortgages, specifically five-year ARMs with agencies such as Fannie Mae and Freddie Mac. He explained how they can be used to reduce risk in the investment portfolio.

Lynch provided a great overview of the bank ownership landscape. I particularly liked his comment about family-owned businesses being the most common form for a company. He said 90 percent of the companies in the United States are family owned, and around the world family ownership is even more common. One-third of all Fortune 500 companies are family-controlled and family-owned companies produce 50 percent of the GDP in this country, as well as provide 60 percent of the employment.

The BHCA web site gives members the opportunity to listen to any of our previously presented webinars or to any of our seminar breakout sessions. They are all recorded and archived at www.theBHCA.org. In the "members only" section of the web site, click on "webinar archives" or "seminar audio files." Each option will present you with recordings to select from. If you registered for the webinars and would like to hear the webinar again, you can access the recording at no cost. If you did not register but would like to listen to a webinar, you can access the recording for just $49.

The arrangement is similar on the seminar breakout sessions. If you attended the seminar, you can listen to any breakout session at no cost. If you did not attend the seminar, each session is available for just $49. These recordings are a great member benefit.

Senate considered, but ultimately dropped, additional sub S tax idea



By Tom Bengtson
BHCA Managing Director

Earlier this year, members of the U.S. Senate were considering whether to hit subchapter S shareholders with additional taxes in order to buy down the interest rate of federal student loans. Given that we focus on bank ownership issues, we were watching this closely at the Bank Holding Company Association. Although BHCA does not engage in lobbying, we like to keep our members informed of legislative developments which might affect them as owners or as holding company professionals/officers so they can appropriately engage in the advocacy process, either directly or through other groups.

Fortunately, S. 2343 died in the Senate, but the mere fact that Senators were actually considering this misguided legislation should concern anyone with a subchapter S holding company and/or bank. About 32 percent of the banks in the country are subchapter S organizations; in Midwest states such as Minnesota (69 percent), North Dakota (67 percent), South Dakota (47 percent), Iowa (59 percent), and Illinois (36 percent), the percentages are even higher.

Specifically, S. 2343 would have levied payroll taxes on all sub S earnings (wages and dividends) going to active shareholders. The idea ultimately was recognized as impractical and unworkable for a lot of reasons, but I know that I find it particularly upsetting that lawmakers would consider using the payroll tax to offset the cost of random government expenditures. Payroll taxes currently are used for Social Security and Medicare; income taxes fund other government expenses. Using the payroll tax to fund general government spending would eliminate the distinction between the payroll and income taxes, which would be a significant breach of the current philosophy behind our tax system.

In early May, several industry organizations, including the ABA and ICBA, co-wrote a compelling letter to Senate leadership against the concept. Perhaps individuals wrote letters as well. Ultimately, the Senators saw reason and abandoned the notion. Had the concept advanced into law, it would have cost subchapter S shareholders an estimated $9 billion.

Fall Seminar Plans Taking Shape

I hope you have Thursday and Friday, Oct. 4-5, 2012 set aside on your calendar to attend the BHCA Fall Seminar. Set for the familiar Minneapolis Airport Marriott Hotel in Bloomington, Minn., the meeting features a tremendous line-up of general session speakers.

Our after-dinner speaker on Thursday, Oct. 4 is Steve Russell, the retired U.S. Army infantry officer who captured Saddam Hussein. Russell served 21 years, deploying to Kosovo, Kuwait, Afghanistan and Iraq. He was covered widely by Time magazine, CNN, Fox News and others. He is the subject of numerous books and is featured on the Discovery Channel's "Ace in the Hole" documentary about Hussein's capture.

Friday morning, we welcome Don Musso, president and founder of FinPro, Inc., which provides consulting services to more than 300 community banks across the country. Following up on the enterprise risk management discussion initiated at the Spring Seminar, Musso will zero in on the essential components of a customized plan for your holding company. Musso is the founder of two *de novo* banks and has invested in several other banks.

J. Michael Woody, a well-known industry consultant, will share thoughts on how to build a strategy for finding earning assets and generating fee income. He will talk about how to make the most of your board of directors, typically one of the bank's most underutilized resources. Woody serves on the faculty of several banking schools, and has held senior officer positions at several banks. He currently works with more than 165 banking clients in 46 states on everything from strategic planning to staffing, to regulatory interface and much more.

FTN Financial economist and market analyst Lindsey Piegza gives us a market update during our luncheon session. Piegza, a frequent guest on Fox Business News, the BBC, CNBC, Bloomberg TV and National Public Radio, specializes in consumer, labor markets and macro economic trends.

We will close out our seminar with a presentation by Rich Chapman. Many bankers know him as the former president/owner of Bank Compensation Strategies. Chapman will share more than 25 years of CEO/business ownership experience in and around the banking industry through his "True Line of Sight" presentation on leadership.

That Friday evening (Oct. 5), BHCA will host an informal a la carte social event at the Chanhassen Dinner Theater. Guests will enjoy dinner and the classic musical Bye Bye Birdie. We have done these dinner-and-a-show events with our Spring Seminar and they have been so successful that we have decided to add something similar to our Fall Seminar.

We are excited about the new Thursday-Friday format because it minimizes time away from the bank, and it offers a great lead-in to a weekend in the Twin Cities. Add one or two nights to your stay at the Marriott and make the most of your seminar experience by staying through the weekend.

Spring seminar speakers focus on

More than 220 people participated in the Spring Seminar of the Bank Holding Company Association, conducted May 7-8 at the Minneapolis Airport Marriott Hotel in Bloomington, Minn. The theme for the 62nd semi-annual seminar was "Climb to New Heights."

The seminar opened and closed with speakers from the world of sports. University of Minnesota football coach Jerry Kill took questions for more than half an hour during his after-dinner presentation on Monday evening.

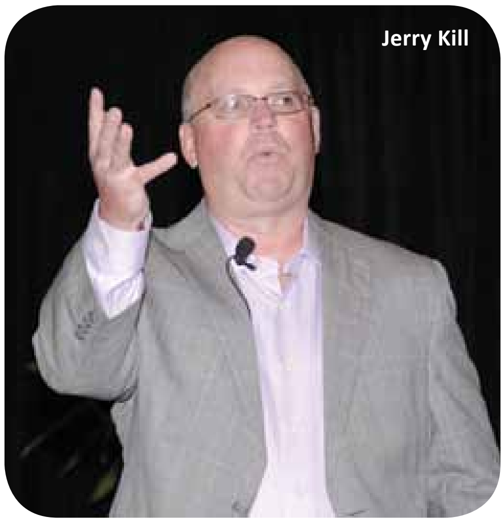
Participants got down to business Tuesday morning when attorney Jeff Gerrish and consultant Tom Farin took bank owners through some of the industry's greatest challenges. Following a round of break-out sessions (there were five one-hour sessions to choose from) luncheon speaker Tim Koch rounded out Farin's presentation with additional thoughts on enterprise risk management. Koch is president of the Graduate School of Banking-Colorado.

Joe Schmit, the Twin Cities area television sports broadcaster, closed the seminar with a series of stories about local sports personalities and his own story about beating back cancer.

Tuesday evening, some 30 bankers and guests concluded their seminar experience with dinner at Sea Change in downtown Minneapolis, followed by the Guthrie Theatre's presentation of Time Stands Still.

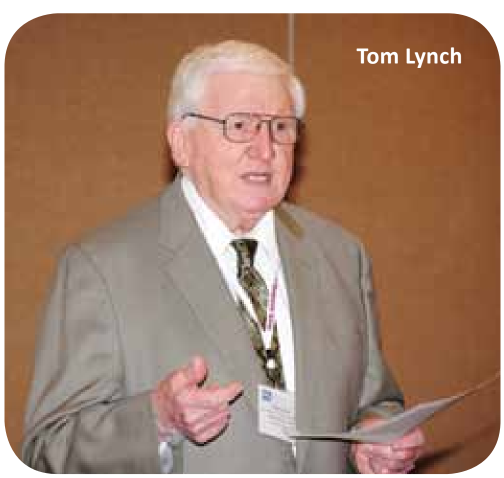
Strategic initiatives help closely held banks compete

Gerrish said nearly half of the nation's financial institutions are family held or closely held. Gerrish, a partner at Memphis-based Gerrish McCreary Smith Consultants, said closely held banks that want to compete from a position of strength may want to consider the following strategic initiatives:



Jerry Kill

Josh Kiefer



Tom Lynch

Board succession. There needs to be a plan in place for board succession. The board's purpose, Gerrish said, is to provide for adequate board and management succession to enhance shareholder value. When considering board succession, Gerrish advised bankers to start with the fundamental issues of board size. Boards should be prepared to handle vacancies, and they should know how to create vacancies if necessary. Mandatory retirement, is "better than nothing." The downside of mandatory retirement is that it doesn't take the individual into account. "Your 75-year-old director may be the smartest director on the board…." Gerrish said. The mechanics of board succession typically involve having a structure such as a nominating committee that deals with succession and identifying qualified candidates.

Management succession. In order for a bank to thrive, the issues of short-term and long-term management succession must be addressed. Gerrish said a board needs first to consider its goals for management succession. "How will you protect your investment?" he asked. Management succession is especially critical for closely held banks. Gerrish suggests a proactive approach: "You need to know when the CEO is going to retire. Someone needs to ask the question so you can figure out how to plan for it."

Also key to management succession is knowing the domino effect. If the CEO goes, will others leave?

Ownership structure. Should the bank be a sub S? Is it time to revert to a C corp? For closely-held banks, Gerrish said the sub S structure

ownership issues, risk management

makes sense in the current environment. "If your goal is to continue to serve your community, the only way to do that is to enhance the value for your shareholders," Gerrish said. "The only thing you have going for you at this time is subchapter S."

Tracking and retaining key personnel. "How do you convince family members to come back to the bank?" Gerrish asked. Also critical to a bank's success is retaining non-family professional help. Bankers, he said, have to deal with family issues while also attracting non-family personnel who will be key to their success. "You have to be able to retain key personnel — and keep them — by providing incentives that look like equity," Gerrish advised.

Profitability. It's time for bankers to climb out of the recession bunker and start making money, Gerrish said. "Sit down with your senior management group and break down the income statement to figure out what you are doing," he said. A renewed focus on profitability will drive earnings and, in turn, drive cash flow to shareholders. "And that is going to drive our ability to allocate capital," he added.

Compliance issues, of course, are an increasing drag on profitability. Gerrish encouraged bankers to appeal exam findings in order to lower their FDIC premiums. "You can appeal your exam findings, revised CAMELS ratings, or violations. If it can save you money, then you should think about an appeal."

Capital. Capital is a tough issue for closely-held family banks, Gerrish said. "You have retained earnings, you can use debt leverage, you can still get bank stock loans to redeem shares, or you can consolidate equity until you are over $500 million," Gerrish said. Or, closely-held banks that need capital can bring in new shareholders, but Gerrish called that process dicey.

"Do you use it to create liquidity for the family, or do you use it in case someone needs liquidity for an event such as a death? Do you grow the company? Does it support the growth? Does it off-set losses? Do you increase cash flow to shareholders?" Management of closely-held banks must weigh these issues in the context of retaining attractive stock.

Remaining independent. Gerrish said there is a ripple of merger and acquisition activity being seen in the community banking sector. A subchapter S bank has tremendous after-tax cash flow and a nice return on equity, Gerrish said. If bankers are thinking about doing a deal, the issues of who gets what, and what the resulting company looks like, aren't all that challenging to figure out, he said.

New lines of business. Traditional banks may be tempted to boost income by doing something crazy. Gerrish advised bankers to stick to their core business, especially if their market is growing. Do what you understand and get thinking about building non-interest income, he said.

Strategic planning is critical to all organizations but it must be done correctly. Gerrish said the indications that strategic planning won't work for banks are: 1) There is no buy-in from the directors and officers; 2) If it is not enjoyable for the participants; 3) Participants get hung up on the process instead of focusing on the planning; 4) Participants aren't honest or one person dominates the

Seminar coverage continues on next page

Right: Enjoying the reception, which was held outdoors, from left, are: Bernie Gaytko, Frankson Investment Corporation, Waseca, Minn.; Dana Carrington, Continuity Control, St. Paul, Minn.; and Tom Sankovitz of Frankson Investement Corporation.

Left: Sharing ideas at the reception, from left, are: Charles Robasse, Wabasso Bancshares, Inc., Wabasso, Minn.; Joshua Kiefer, Country Club Bank Capital Markets Group, Prairie Village, Kan.; Karen Grandstrand, Fredrikson & Byron, Minneapolis; and Dwight Larson, United Bankers' Bancorporation, Inc., Bloomington, Minn.

meeting; 5) It becomes a budgeting session or focus shifts too much on mission, vision and values; and, 6) There is no accountability, action plan, or assignment of personnel to move things forward.

"In order to do anything, you have to have some kind of planning process," Gerrish said. "My suggestion is to focus on the substance of what you are doing when you engage in a planning process … and have an agenda, a specific agenda."

Integrated ERM modeling can reveal exposures

Tim Koch of the Graduate School of Banking at Colorado, and Tom Farin of Farin & Associates, Madison, Wis., teamed to explain that integrated enterprise risk management techniques can be used to unveil bank vulnerabilities, helping bank managers understand their challenges.

While stress tests for interest rate fluctuations or credit risk have long been an ALCO staple, bankers have traditionally approached risk assessment separately or in "silos." But both Farin and Koch urged bankers to adopt an integrated approach along the framework of the CAMELS rating system. It's a regulatory approach that could impact decision-making throughout the institution.

Integration is driven by increases in regulatory scrutiny and expected increases in capital requirements, Farin said. As a result, bankers might want to think about integrated stress testing when they set capital goals. "There were many institutions that came into the financial crisis with inadequate capital reserves to deal with the risks they were taking, and that's what integrated stress testing gets to," Farin explained. "We're likely to see the stress test will test to see if an institution has sufficient capital to remain well capitalized after a severe stress ... What the regulator is really looking for is what would happen if you encounter a nightmare scenario that hits you in multiple areas."

Koch touted the integrated approach as a management tool. "Use it for planning, budgeting and risk management – one model can do it all," he said. Without integration, it's difficult to know the exposure beyond a static impact in one area.

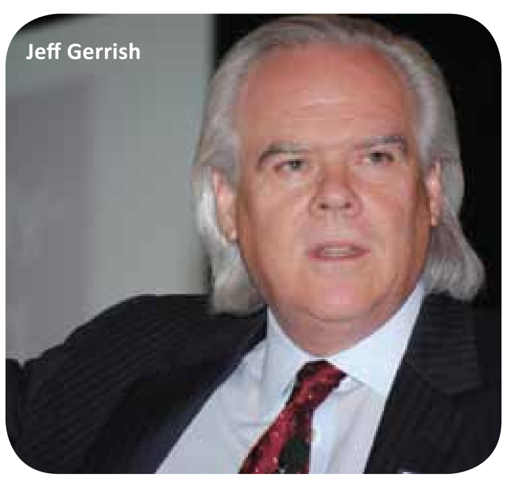
Integrated stress testing requires account-by-account data, Koch said, acknowledging that most banks don't have the information they need to launch integrated ERM. "Start collecting the data now and you can start these tests in about a year," Koch advised. Depending on the complexity of the bank, Koch added, once account data is compiled bankers can perform integrated ERM without a third-party vendor.

"We're seeing a movement from static measures of risk to dynamic measures of risk," Farin said. "In dynamic interest rate management, we test the interest rate risk not just in the balance sheet, but in a business plan or strategy. We saw liquidity regulations saying we need to move toward cash flow oriented measurement systems. You have to have some sort of a plan to come up with cash flows. So cash flow oriented measurement systems are part of the liquidity regulations and we're seeing more and more indications that we ought to be evaluating interest rate risk in a business plan or strategy.

"You put a lot of money into asset management technology and most of you look at it as a compliance cost, but we're not very far away from turning it into a decision-making tool that helps us make better decisions," Farin said.

The largest banks and regional banks set capital goals by running integrated stress tests. How formal integrated stress testing becomes for community banks remains to be

Tim Koch



Jeff Gerrish

Tom Farin

Right: From left: Phil Hoover, Kevin Christians and Kevin Burr of Community Bankers Financial Services, Eagan, Minn.

Left: Tim (left) and Aaron Siegle of First Holding Company of Cavalier, Inc., Cavalier, N.D.

seen, but it's something that both Koch and Farin strongly encouraged bankers to include in their strategic planning. "You should be at least thinking about it and talking about it," Farin said.

Koch, who served for two years on an FDIC advisory committee, is a senior advisor to FinPro of Liberty Corner, N.J., which has developed an integrated ERM model for banks. Koch touted properly executed integrated ERM also as a way to avoid costly enforcement actions.

"The regulators at the senior level are smart, they care, but most of them haven't been in a community bank for 10 or 15 years so they don't understand the kind of banking most of you do," Koch told bankers. "They're making the rules, you're living under the rules, and they don't know what the impact is."

Framing his argument for integrated ERM against a meager jobs picture and another 5 percent to 10 percent decline in home values in the nation's 20 largest metropolitan areas, Koch called bankers' exposure great and said bank failures will continue. "Banks that are in trouble are downgraded and it's almost impossible for them to earn their way out of trouble," Koch said.

The FinPro eight-phase process, as Koch laid it out, prioritizes risks. The approach is basically an internal CAMELS risk assessment. It includes:

- *Pre-analysis*. Set up a risk committee and adopt a CAMELS approach.
- *Identification and quantification of risk*. Set risk thresholds and tolerances and perform a horizontal risk assessment.
- *Prioritization of risk*. Set up a vertical risk assessment for the dynamic impacts on the entire enterprise.
- *Ensure data integrity*.
- *Prepare alternative scenarios*. Risk modules for the entire enterprise
- *Stress testing*. Identify trigger events using a variable stress test and an enterprise-wide stress test.
- *Establish mitigation strategies*. Name the people and define the policies and procedures to follow.
- *Review*. What is the impact in context of overall ERM?

If you do not perform according to plan, the regulators will be on you, Koch said. "ERM is a tool to buy you time to come up with a plan for survival," Koch said. "If you present this analysis to a regulator who comes in, and you've already identified mitigation strategies to pursue, what can the regulator ask you to do beyond that, other than raise more capital?"

By Jackie Hilgert

From Left: Barb and Greg Raymo, First Rushmore Bancorporation Inc., Worthington, Minn.; and Jason Mork, BMO Capital Markets, Milwaukee.

A look at the advantages — and disadvantages –

Editor's note: *There are 7,273 FDIC-insured banks and thrifts in the country; currently 2,298 are sub S organizations. Given the current economic climate and market conditions, some bankers are reconsidering their incorporation format. Jerry Kissell, a tax partner with McGladrey & Pullen LLP, presented a break-out session at the BHCA Spring Seminar titled "S Corp versus C Corp: Should I change my corporate status?" Following is a summary of the primary advantages and disadvantages of the subchapter S incorporation election, based on Kissell's presentation.*

The economy, the banking industry, and income tax laws have all changed dramatically since banks first became eligible to be S corporations on January 1, 1997. As the regulators have placed restrictions on bank dividends, restricting the ability to provide shareholders with cash to pay income tax when taxable income is often times greater than book income, and the potential for increased individual income tax rates may have many of you questioning whether it is still a good idea to remain an S corporation.

For tax purposes, an S corporation is a "pass-through" entity. This means that each shareholder's pro rata share of the company's taxable income or loss is passed through to his or her personal tax return and is subject to individual tax rates. The character of the income or loss (i.e., capital versus ordinary) is also passed through to the S corporation's shareholders. As a general rule, shareholders in an S corporation are taxed on the earnings of the corporation, not on the distributions received from the S corporation. This is in sharp contrast to the tax treatment of shareholders of a C corporation who are taxed on the dividends of the corporation as opposed to the taxable earnings of the corporation.

Because S corporation shareholders are taxed on the earnings of the S corporation, shareholders typically look to the corporation for a distribution stream that at a minimum covers the personal tax liability associated with the company earnings. To the extent that a shareholder has tax basis in the S corporation, the distribution of previously taxed S corporation earnings is not taxable to the shareholder.

With this background in mind, we can review the pros and cons of remaining an S corporation.

ADVANTAGES OF REMAINING AN S CORPORATION

Double taxation of C corporation dividends – Dividends paid by a C corporation are generally subject to double taxation. First, C corporations pay tax on their taxable income. When the previously taxed income is distributed to the shareholders as dividends, the individual shareholders pay a second tax on the same income, generally at the qualified dividends tax rate (currently 15 percent), plus state taxes where applicable.

S corporation earnings are taxed only once — at the shareholder level. Undistributed earnings are recorded in the Accumulated Adjustments Account (AAA), a corporate level account. Because the earnings have previously been "passed-through" to the shareholders and subjected to tax on the shareholders' returns, subsequent distributions of the earnings out of AAA are generally tax-free to the shareholders. The 15 percent tax rate on dividends noted above is a historically low tax rate, but is scheduled to expire at the end of 2012. Unless Congress acts to change the law, in 2013 and forward, dividends will be taxed at ordinary tax rates. For a bank paying out distributions in excess of the amounts required to pay taxes, this will be an even greater benefit to be an S corporation.

Increase in stock basis for undistributed profits — As a shareholder in an S corporation, the tax basis in your stock is increased or decreased by the income or loss that is passed through to the shareholders, including tax-exempt interest. Generally, distributions of cash reduce your basis in the stock. As you are aware, stock basis is used to compute the gain or loss upon the sale of the stock. Thus, one advantage of an S corporation is that undistributed income increases basis in stock and thereby reduces the recognition of gain on the disposition of the S corporation stock.

Elimination of double tax on sale of assets or liquidation — Generally a buyer of a corporation would like to buy the assets of a corporation if they are paying a premium. If a C corporation were to sell all of its assets, a gain is first recognized at the corporate level and tax is paid on the gain. If the net proceeds are distributed in liquidation, there is another tax at the shareholder level. The gain on the sale of assets (and on subsequent liquidation) by an S corporation is generally taxed only once at the shareholder level, other than gains subject to the Built-in Gains (BIG) tax.

Reasonable compensation — The Internal Revenue Service

– of subchapter S incorporation status

allows corporations to deduct reasonable compensation paid to the stockholders and their family members. Stockholders in closely-held C corporations sometimes attempt to maximize compensation in order to get cash to the stockholders and avoid the double taxation that would apply to dividend distributions. If the IRS determines that the compensation is unreasonably high, they will attempt to reclassify the excess as a dividend to the shareholder.

Because all income of an S corporation is passed through and taxed to shareholders, there is less reason for the IRS to challenge the amount of compensation paid to shareholders. However, the IRS may scrutinize compensation that is unreasonably low if they feel the compensation is structured as an attempt to minimize or avoid payroll taxes or if compensation is manipulated in an attempt to steer income to a different taxpayer/shareholder who has a lower marginal tax rate.

Capital losses — It is unusual for a bank to generate capital gains or losses, although it occurs more frequently for bank holding companies. To the extent capital losses are generated, a C corporation cannot deduct capital losses against ordinary income; it may only use those losses to offset capital gains. Generally, a C corporation may carry the loss back three years and forward five years. An S corporation is allowed to pass the losses through to the individual shareholders, who may use the losses to offset other capital gains. Net capital losses of individual shareholders are limited to $3,000 per year, but there is no limit on the number of years the excess losses can be carried forward.

Charitable contribution limitations — A C corporation's charitable contribution deduction is limited to 10 percent of its pre-contribution taxable income. An S corporation passes through all contributions to its shareholders without any corporate level limit. While deductibility is limited at the shareholder level, the limitations are significantly less stringent than the 10 percent limit imposed on C corporations. For example, a shareholder may deduct cash charitable contributions of up to 50 percent of his/her adjusted gross income. However, the deductibility of itemized deductions, including charitable contributions, is reduced for certain high-income taxpayers. In a time of depressed earnings, the benefit of being of an S corporation is even greater regarding this item.

Passive shareholders — If the shareholder of the S corporation were a passive investor, the "trade or business" income passed through to this individual on Schedule K-1 would be considered "passive income" on the shareholder's personal income tax return. This passive income may be offset by passive losses the shareholder incurs in other individual activities. The determination of whether a shareholder is active or passive can be complex, and you should consult with your tax advisor regarding your individual status.

Shareholder interest expense on acquisition debt — When a shareholder purchases the stock of a C corporation and borrows the funds to acquire the stock, the interest expense is classified as "investment interest." In general, investment interest is only deductible against investment income (e.g. interest and dividends).

If the same shareholder borrows funds to purchase S corporation stock, the treatment of the interest expense follows the character of the income passed through from the S corporation K-1 (i.e., it generally offsets K-1 ordinary income and is deductible on Schedule E). The nature of the shareholder's participation (i.e., passive or materially participating) is critical. For example, for a passive shareholder, the acquisition interest expense would reduce the K-1 "passive" income or increase the "passive" loss.

Cash basis method of accounting — Bank S corporations can retain or switch to the cash basis method of accounting even if their gross receipts exceed $5,000,000 (the limitation for C corporations). The cash basis of accounting typically allows for a significant, long-term deferral of income for tax purposes for banks that have elected this method.

DISADVANTAGES OF REMAINING AN S CORPORATION

Fringe benefit treatment — S corporation shareholder/employees (and their family members) owning more than 2 percent of the outstanding stock must include certain company-provided fringe benefits in their gross income, whereas C corporation shareholder/employees do not. Affected fringe benefits include:

- Amounts paid under accident and health plans
- Amounts paid by employer to accident and health plans
- Meals or lodging furnished for the convenience of an employer

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• Group term life insurance

Additionally, 2 percent shareholder/employees are not allowed to participate in benefits provided under cafeteria plans such as flexible spending accounts. They are, however, allowed to participate in qualified retirement plans.

Cash flow — As noted above, in today's environment many regulatory agencies are limiting the amount of distributions the bank can pay to its holding company or to the shareholders directly if there is no holding company. There are a number of banks that are reporting little or no income due to substantial loan loss provisions. If there are not corresponding charge-offs, you can end up in a situation where there is little or no book income and substantial taxable income. Since there is no guarantee or requirement that the S corporation will or must pay distributions to pay the individual shareholders' taxes, this can cause a cash flow crunch for the individual shareholders.

Estimated payments — Because S corporation income is passed through to the shareholders, the shareholders are likely required to make (or increase) quarterly federal and state estimated tax payments. Additionally, the S corporation may need to make quarterly state income tax payments if the state imposes a corporate-level tax (e.g., California). As noted in the cash flow section above, if the bank is not making distributions, this can be a hardship for the shareholders.

State apportionment/state filing requirements — Corporations are required to file state tax returns and generally pay state taxes in every state in which sufficient business activity is established. Generally, the income is apportioned to a particular state based on the ratio of property, payroll and/or gross income in that state to the corporation's total property, payroll and/or gross income.

To the extent the bank has business in states outside of its home state and those states recognize the S corporation election; all of the individual shareholders are required to file in that state. Also, to the extent shareholders don't live in the state the bank is located in, they will have to file in their home state and in the state the bank is located in. As the concept of "economic nexus" gains traction, it is possible that the S corporation shareholders will have to file in more and more states and their individual returns will become more complex. Some states allow a composite income tax filing for the S corporation and its shareholders, eliminating the requirement for the shareholder to file a separate return; however, the income on a composite return is generally taxed at the highest marginal individual tax rate for the state.

In states that do not recognize the S election, the corporation files a return and pays a corporate level tax.

Eligibility issues — An S corporation cannot have more than 100 shareholders. Shareholders of an S corporation must be individuals, certain types of trusts and estates or qualified nonprofit entities. A partnership or corporation cannot own S corporation stock. A C corporation can generally have any type or number of shareholders. The restrictions on the types of eligible shareholders can limit the sources of capital should the bank be required to increase its capital.

S corporations can have no more than one class of stock issued and outstanding; however, differences in voting rights are allowed. The IRS can re-characterize certain debt and stock with unequal distribution rights as a second class of stock. A termination of the S corporation election will occur if a second class of stock is issued. Safe harbors are available to minimize this possibility. C corporations can have various classes of stock, including preferred stock. This can also be a valuable source of capital if needed.

Tax rates — A C corporation's top federal income tax rate is generally 34 percent (a 39 percent marginal rate applies to income between $100,000 and $335,000, as the graduated brackets phase out on income over $100,000.) Corporations earning in excess of $10,000,000 are subject to a 35 percent federal rate. C corporations are also subject to state taxes of varying rates. An S corporation shareholder pays federal tax at his or her individual marginal tax rate, which is currently as high as 35 percent, plus state taxes of varying rates. The highest individual rate of 35 percent is scheduled to expire at the end of 2012. If Congress does nothing to change this, effective January 1, 2013, the highest individual tax rate will be 39.6 percent. Taking into account phase-out of itemized deductions, the actual rate is even higher. Finally, the health care bill created a Medicare surtax of 3.8 percent on investment income for individuals with adjusted gross income in excess of $250,000. Investment income for this purpose includes income passed out to S corporation shareholders who do not actively participate in the operations of the S corporation. If your bank is only making limited distributions to cover the tax liabilities associated with the S corporation income and assuming similar C and S corporation state tax rates, there may be a significant tax cost to remaining an S corporation.

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Do you have a comment on this article? Please contact Ron Feldman, senior vice president, Federal Reserve Bank of Minneapolis, at 612-204-5176 or ron.feldman@mpls.frb.org.

Holding companies as a 'source of strength'

Dodd-Frank puts new emphasis on long-standing doctrine

By John Yanish

In response to the recent financial crisis, Congress passed the Dodd Frank Act (DFA), a wide ranging body of law designed to address a myriad of issues. While many matters addressed in the DFA are new, such as the creation of the Consumer Financial Protection Bureau, the statute also took an important step in addressing a long-standing staple of the banking regulatory framework: the requirement that a bank holding company serve as a "source of strength" for its subsidiary bank(s), a principle sometimes referred to as the source of strength doctrine.

To understand the significance of the source of strength provisions within the DFA, it is useful to revisit some of the history regarding the doctrine. The Bank Holding Company Act of 1956 doesn't specifically mention source of strength, but directs the Federal Reserve Board of Governors to "take into consideration the financial and management resources and future prospects" of a company that applies for the Board's approval to become a bank holding company. In 1978, the United States Supreme Court interpreted this provision to mean that the Board could deny an application to become a bank holding company if it determined the company "would not be a sufficient source of financial and managerial strength to its subsidiary Bank."

The source of strength doctrine gained momentum in the 1980s. The Federal Reserve amended its Regulation Y in 1984 to state that a "bank holding company shall serve as a source of financial and managerial strength to its subsidiary banks and shall not conduct its operations in an unsafe or unsound manner." Then, in 1987, the Board published a policy statement making plain its view that source of strength was not merely a factor for consideration when a company sought to become a bank holding company. The policy states that a bank holding company "should stand ready to use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress." Failure of a bank holding company to do so on an ongoing basis is deemed an "unsafe and unsound" practice.

The Board's approach reflected in the policy, asserting a bank holding company must provide ongoing financial support to its subsidiary banks, drew criticism from some quarters and was addressed in litigation. In 1991, a federal court of appeals considered source of strength requirements and determined that the Board did not have statutory authority to order a bank holding company to transfer its funds to its troubled subsidiary banks. That same year, the United States Supreme Court reversed the appeals court decision on procedural grounds, but did not give an opinion on the scope of source of strength. While this resulted in a victory for the Board in that case, it arguably left some uncertainty as to the appropriate scope of source of strength requirements.

In light of this history, the new DFA provisions are a significant clarification of the law in this area. The DFA makes clear that a bank holding company's obligation to serve as a source of strength is a substantial ongoing obligation. The DFA provides that the "appropriate Federal banking agency for a bank holding company or savings and loan holding company shall require the [holding company] to serve as a source of financial strength for any subsidiary of the bank holding company or savings and loan holding company that is a depository institution." It further provides that such a company may be compelled to file reports, under oath, for the purposes of assessing the company's compliance with this obligation.

This strong statement in the DFA bolsters the Board's policy and long standing interpretation of the source of strength doctrine. Significantly, it also directs the Board and other banking regulators to adopt regulations to carry out the statutory provisions. This rulemaking is underway and will be completed in coming months. Proposed rules have not been published at this point so the content is presently uncertain. That being said, topics to be addressed may include further details regarding (1) what it means for a bank holding company to be a source of financial strength, (2) the circumstances under which a holding company may be called to provide such support to a subsidiary, and (3) the extent of ongoing reporting requirements.

Interested parties should follow the development of the regulations closely, as the interagency regulations will likely have a substantial impact on the nature and scope of a bank holding company's obligations in this area.

John Yanish is vice president and deputy general counsel at the Federal Reserve Bank of Minneapolis.

Holding Company Transaction Report

Here are selected second quarter 2012 bank holding company filings with the Federal Reserve Banks of Chicago, Minneapolis, Kansas City and St. Louis.

▷ GNB Bancorporation, Grundy Center, Iowa, granted a waiver of application to acquire First State Bank, Manchester, Iowa, in connection with the merger of First State Bank into GNB Bancorporation's subsidiary bank, GNB Bank, Grundy Center. As a result of merger, GNB Bank will establish a branch in Manchester.

▷ Chemical Bank, Midland, Mich., filed to purchase 21 branches of Independent Bank, Ionia, Mich.

▷ First Community Bank, Harbor Springs, Mich., filed to merge with Select Bank, Grand Rapids, Mich.

▷ The Elberfeld State Bank, Elberfeld, Ind., filed to establish a branch in Evansville, Ind.

▷ Old National Bancorp, Evansville, Ind., filed to merge with Indiana Community Bancorp, Columbus, Ind.

▷ Adams Bancshares, Inc., Adams, Minn., filed to merge with Elkton Bancshares, Inc., Elkton, Minn., and thereby indirectly acquire Farmers State Bank of Elkton.

▷ Notice filed by Russell S. King, North Oaks, Minn., to acquire 10 percent or more of Northfield Bancshares, Inc., Northfield, Minn., and thereby indirectly gain control of Community Resource Bank, Northfield, Minn.

▷ Valley Bank Shares, Inc., proposes to acquire through its wholly-owned subsidiary, First National Agency Company, both in Valley, Neb., the insurance agency assets of Avoca Company, Avoca, Nebraska.

▷ Exchange Bank of Missouri, Fayette, Mo., authorized to establish a branch in Marshall.

▷ State Bank Financial, La Crosse, Wis., authorized to establish a branch in La Crosse.

▷ Northeast Indiana Bancorp, Inc., Huntington, Ind., authorized to become a bank holding company on conversion of its subsidiary thrift, First Federal Savings Bank, Huntington, to a state-chartered bank.

▷ Community Bank, Inc., Ronan, Mont., authorized to merge with Community Bank-Missoula, Inc., Missoula, and thereby establish three branches.

▷ Adams Bank and Trust, Ogallala, Neb., filed to establish a branch in Longmont, Colo.

▷ Notice filed by Elizabeth A. Murphy, Omaha, Neb., to acquire control of Ameriwest Corporation, parent of First Westroads Bank, Inc., both in Omaha, Neb.

▷ First Nebraska Bank, Valley, Neb., filed to purchase certain assets and assume certain liabilities of Heartland Community Bank, Bennet, Neb., and incident thereto, to establish branches in Avoca, Bennet, Nebraska City, and Weeping Water, all in Nebraska.

▷ FirstBank, Lakewood, Colo., filed to establish a branch in Glenwood Springs, Colo.

▷ Vintage Bancorp, Inc., Wichita, Kan., filed to become a bank holding company through the acquisition of Vintage Bank Kansas, Leon, Kan., and CornerBank, N.A., Winfield, Kan. Vintage Bancorp, Inc., elects to become a financial holding company.

▷ Old National Bancorp, Evansville, Ind., filed to merge with Indiana Community Bancorp, Columbus, Ind.

▷ CIC Bancshares, Inc., Denver, filed to acquire Millennium Bancorp, Inc., parent of Millennium Bank, both in Edwards, Colo. Centennial Bank, Centennial, Colo., filed to merge with Millennium Bank, Edwards, and incident thereto, establish branches in Breckenridge, Edwards, Englewood, Steamboat Springs, Vail, and Fraser, all in Colorado.

▷ FNB Bancshares, Inc., Independence, Kan., authorized to become a bank holding company by acquiring First National Bank, Independence.

▷ The Lumpkin Family Foundation, and others intend to apply to the Federal Reserve Board for permission to acquire 25 percent or more and thereby control of First Mid-Illinois Bancshares, Inc. of Mattoon, Illinois. First Mid-Illinois Bancshares, Inc., controls First Mid-Illinois Bank & Trust, N.A. , Mattoon.

▷ Northwest Investment Corp., Davenport, Iowa, filed to become a bank holding company following the conversion of its subsidiary, Northwest Bank & Trust Company, Davenport, Iowa, from a federally chartered savings bank to a state chartered bank.

▷ Notice filed by Steven D. Spector of Glenview, Ill., and others to acquire and/or retain 25 percent or more of the shares of Spector Properties, Inc., Chicago, and thereby acquire/retain control of Andalusia Community Bank, Andalusia, Ill.

▷ Mercantile Bancorp, Inc., Quincy, Ill., filed to merge with its wholly owned subsidiary, The Royal Palm Bancorp, Inc., Naples, Fla., and thereby cause its subsidiary bank, The Royal Palm Bank of Florida, Naples, Florida, to become a direct subsidiary of Mercantile Bancorp, Inc.

▷ Notice by Elizabeth A. Murphy, Omaha, Neb., filed to acquire control of Ameriwest Corporation, parent of First Westroads Bank, Inc., both in Omaha.

▷ Prime Time Investments Group, LLC, Wray, Colo., filed to become a bank holding company through the acquisition of 79.2 percent of Investment Opts, LLC, Bethune, Colo., and the indirect and direct acquisition of 48 percent of FarmBank Holding, Inc., Greeley, Colo., parents of First FarmBank, Greeley.

▷ Town Bank, Hartland, Wis., authorized to establish a branch in Menomonee Falls, Wis.

▷ Leackco Bank Holding Company, Inc., Wolsey, S.D., authorized to acquire ASB Bank Holding Company, Pierre, S.D., and thereby acquire American State Bank of Pierre; and for ASB Interim Bank, Wessington Springs, to merge into American State Bank of Pierre.

▷ Sheldon B. Lubar, River Hills, Wis., and others filed to acquire Ixonia Bancshares, Inc., Ixonia, Wis., and thereby to acquire ISB Community Bank, Ixonia.

▷ Johnston Growth Corporation, Johnston, Iowa, filed to become a bank holding company following the conversion of its subsidiary, Charter Bank, Johnston, from a federally chartered savings association to a state chartered bank.

▷ Frank A. Peplinski and others filed to acquire 25 percent or more of Northstar Financial Group, Inc., and indirectly, Northstar Bank, Bad Axe, Mich., and Seaway Community Bank, St, Clair, Mich.

▷ Prime Time Investments Group, LLC, Wray, Colo., filed to become a bank holding company through the acquisition of 79.2 percent of Investment Opts, LLC, Bethune, Colo., and the acquisition of 48 percent of the FarmBank Holding, Inc., Greeley, Colo., parents of First FarmBank, Greeley.

▷ Ipswich Community Bancshares, Inc., Ipswich, S.D. , authorized to become a bank holding company and to acquire Yellowstone Trail Bancorporation, Ipswich, and its subsidiary bank, Ipswich State Bank.

▷ Wells Financial Corp., Wells, Minn., authorized to become a bank holding company on conversion of Wells Federal Bank, Wells, from a federal savings bank to a state-chartered commercial bank.

NORTH DAKOTA BANK HOLDING COMPANIES

HOLDING COMPANY, LOCATION Subsidiary Bank, Location	CONSOLIDATED ASSETS*	SUBSIDIARY ASSETS*
1. STATE BANKSHARES, INC., FARGO	**2,265,782**	
STATE B&T, FARGO		2,226,619
FIRST NATIONAL BANK[1], HAWLEY, MN		93,257
2. ALERUS FINANCIAL CORPORATION, GR. FORKS	**1,156,263**	
ALERUS FINANCIAL, N.A., GR. FORKS		1,154,398
3. WATFORD CITY BANCSHARES, INC.	**1,089,768**	
FIRST INTERNATIONAL B&T, WATFORD CITY		1,088,724
4. STARION BANCORPORATION, BISMARCK	**924,935**	
STARION FINANCIAL, BISMARCK		924,641
5. AMERICAN BANCOR, LTD, DICKINSON	**897,870**	
AMERICAN BANK CENTER, DICKINSON		896,529
6. WESTBRA, INC., MINOT	**712,081**	
FIRST WESTERN B&T, MINOT		707,745
7. BNCCORP, INC., BISMARCK	**665,158**	
BNCCORP, INC., GLEALE, AZ		662,437
8. CHOICE FINANCIAL HOLDINGS, INC., GRAFTON	**610,257**	
CHOICE FINANCIAL GROUP, GRAFTON		593,779
9. DAKOTA COMMUNITY BANSHARES, INC., HEBRON	**570,096**	
DAKOTA COMMUNITY B&T, N.A., HEBRON		570,006
10. WESTERN STATE AGENCY, INC., DEVILS LAKE	**492,203**	
WESTERN STATE BANK, DEVILS LAKE		488,840
11. SECURITY STATE BANK HOLDING CO., FARGO	**473,550**	
BANK FORWARD, HANNAFORD		471,627
12. AMERICAN STATE BANK HLDG. CO., INC.,WILLISTON	**467,256**	
AMERICAN STATE B&T CO. OF WILLISTON		467,132
13. JORGENSON WILLISTON HOLDING CO., KENMARE	**352,555**	
FIRST NATIONAL B&T CO. OF WILLISTON		352,555
14. BLACKRIDGE FINANCIAL, INC.[2], FARGO	**350,300**	
BLACKRIDGEBANK, FARGO		348,257
15. LAKESIDE BANK HOLDING CO., NEW TOWN	**326,699**	
LAKESIDE STATE BANK, NEW TOWN		223,523
MCKENZIE COUNTY BANK, WATFORD CITY		102,959
16. FIRST FINANCIAL CORPORATION, ARTHUR	**283,625**	
FIRST STATE BANK OF NORTH DAKOTA, ARTHUR		283,605
17. CORNERSTONE HOLDING CO., INC., FARGO	**264,100**	
CORNERSTONE BANK, FARGO		265,833
18. RAMSEY FINANCIAL CORP., DEVILS LAKE	**241,345**	
RAMSEY NATIONAL BANK, DEVILS LAKE		241,087
19. LEEDS HOLDING CO., LEEDS	**235,981**	
UNITED COMMUNITY BANK OF NORTH DAKOTA, LEEDS		235,981
20. FIRST HOLDING CO. OF CAVALIER, INC.	**226,661**	
UNITED VALLEY BANK, CAVALIER		225,584
21. DAKOTA WESTERN BANKSHARES, INC., BOWMAN	**216,263**	
DAKOTA WESTERN BANK, BOWMAN		216,263
22. NORTH STAR HOLDING CO., INC., JAMESTOWN	**209,951**	
UNISON BANK, JAMESTOWN		209,870
23. FIRST HOLDING CO. OF PARK RIVER, INC.	**188,624**	
FIRST FINANCIAL BANK, ANETA		39,603
FIRST UNITED BANK, PARK RIVER		148,310
24. JORGENSON HOLDING CO., KENMARE	**180,851**	
CITIZENS STATE BANK, MOHALL		59,643
STATE B&T OF KENMARE		121,208
25. KIRKWOOD BANCORPORATION CO, BISMARCK	**179,581**	
KIRKWOOD BANK A TRUST CO., BISMARCK		167,844
KIRKWOOD BANK OF NEVADA, LAS VEGAS		41,827
26. H.O.M.E., INC., FARGO	**178,109**	
NORTHLA FINANCIAL, STEELE		176,859
27. MCLEAN BANK HOLDING CO., GARRISON	**169,286**	
BANK OF TURTLE LAKE		34,940
FARMERS SECURITY BANK, WASHBURN		46,907
GARRISON STATE B&T, GARRISON		86,683
28. BELFIELD BANCSHARES, INC., BELFIELD	**160,578**	
GREAT PLAINS NATIONAL BANK, BELFIELD		160,499
29. PEMBINA COUNTY BANKSHARES, LTD., CAVALIER	**148,325**	
CITIZENS STATE BANK - MIDWEST, CAVALIER		148,325
30. FULL SERVICE INSURANCE AGENCY, INC., BUXTON	**145,626**	
FIRST STATE BANK, BUXTON		145,486
31. VISION BANK HOLDINGS, INC., FARGO	**143,399**	
VISIONBANK, FARGO		140,214
32. OLIVER BANCORPORATION, INC., CENTER	**141,000**	
SECURITY FIRST BANK OF N.D., NEW SALEM		140,532
33. HUNTER HOLDING CO., HUNTER	**127,828**	
DAKOTA HERITAGE BANK OF N.D., HUNTER		126,087
34. FIRST BOTTINEAU, INC., BOTTINEAU	**125,807**	
FIRST NATIONAL BANK A TRUST CO. OF BOTTINEAU		125,779
35. CITIZENS BANK HOLDING CO., FINLEY	**121,492**	
THE CITIZENS STATE BANK OF FINLEY		120,822
36. TIOGA BANK HOLDING CO., TIOGA	**111,689**	
THE BANK OF TIOGA		111,689
37. GOOSE RIVER HOLDING CO., MAYVILLE	**111,248**	
THE GOOSE RIVER BANK, MAYVILLE		111,379
38. MUNICH BANCSHARES, INC., MUNICH	**110,280**	
THE FIRST STATE BANK OF MUNICH		109,086
39. HAZEN BANCORPORATION, INC.[3] , HAZEN	**99,341**	
UNION STATE BANK OF HAZEN		97,929
40. SARGENT BANKSHARES, INC., FORMAN	**98,625**	
SARGENT COUNTY BANK, FORMAN		98,625
41. DRAYTON BANCOR, INC., DRAYTON	**88,991**	
KODABANK, DRAYTON		87,507
42. MCINTOSH CTY. BANK HOLDING CO., INC.[4], ASHLEY	**88,028**	
MCINTOSH COUNTY BANK, ASHLEY		83,033
43. COMMERCIAL BANK OF MOTT ESOP[5], MOTT	**79,428**	
COMMERCIAL BANK OF MOTT		79,428
44. PEOPLES STATE HOLDING CO., WESTHOPE	**78,396**	
PEOPLES STATE BANK, WESTHOPE		78,286
45. UNION HOLDING CO., HALLIDAY	**77,497**	
THE UNION BANK, BEULAH		77,497
46. F&M BANCSHARES, INC., LANGDON	**71,652**	
FARMERS A MERCHANTS STATE BANK, LANGDON		71,593

*Source: Regulatory financial reports filed by bank holding companies and banks, data as of Dec. 31, 2011. *Dollar amounts in thousands*

NORTH DAKOTA BANK HOLDING COMPANIES

HOLDING COMPANY, LOCATION Subsidiary Bank, Location	CONSOLIDATED ASSETS*	SUBSIDIARY ASSETS*
47. FIRST HARVEY BANCORPORATION, INC., HARVEY	**70,377**	
FIRST STATE BANK OF HARVEY		70,127
48. UNION BANCSHARES, INC., FARGO	**69,906**	
UNION STATE BANK OF FARGO		69,906
49. WISHEK BANCORPORATION, INC., WISHEK	**69,534**	
SECURITY STATE BANK, WISHEK		68,982
50. HANISCH BANKSHARES, LTD., CROSBY	**69,236**	
FARMERS STATE BANK OF CROSBY		69,236
51. FNB BANKSHARES, INC., MILNOR	**67,463**	
FIRST NATIONAL BANK, MILNOR		67,463
52. DAVIS BANCSHARES, INC., MCCLUSKY	**63,653**	
NORTH COUNTRY BANK, N.A., MCCLUSKY		63,241
53. NAPOLEON BANCORPORATION, INC., NAPOLEON	**61,182**	
STOCK GROWERS BANK, NAPOLEON		61,182
54. LIBERTY BANCORPORATION, INC., POWERS LAKE	**56,746**	
LIBERTY STATE BANK, POWERS LAKE		56,746
55. JBS, INC., KULM	**56,384**	
HEARTLA STATE BANK, EDGELEY		56,384
56. STATE BANK OF BOTTINEAU HOLDING CO.	**55,177**	
STATE BANK OF BOTTINEAU		54,493
57. TOLNA BANCORP, INC., TOLNA	**54,710**	
THE FARMERS A MERCHANTS STATE BANK OF TOLNA		54,710
58. STRASBURG BANSHARES, INC., STRASBURG	**54,319**	
STRASBURG STATE BANK, STRASBURG		54,319
59. LINCOLN HOLDING CO., HANKINSON	**54,283**	
LINCOLN STATE BANK, HANKINSON		54,283
60. LAKOTA BANK HOLDING CO., INC., LAKOTA	**53,574**	
STATE BANK OF LAKOTA		53,556
61. CAO HOLDING CO., INC., CAO	**50,141**	
FIRST STATE BANK OF CAO		49,142
62. FIRST A FARMERS BANK HOLDING CO., PORTLA	**47,843**	
THE FIRST A FARMERS BANK, PORTLA		47,843
63. FIRST BANK HOLDING CO., INC., HARVEY	**47,380**	
NATIONAL BANK OF HARVEY		46,704
64. TRINITY INVESTMENTS, INC., GLEN ULLIN	**42,465**	
BANK OF GLEN ULLIN		42,465
65. CITIZENS STATE BANCSHARES, INC., LANKIN	**40,422**	
CITIZENS STATE BANK OF LANKIN		40,422
66. MCVILLE FINANCIAL SERVICES, INC.,MCVILLE	**40,342**	
MCVILLE STATE BANK, MCVILLE		40,342
67. FIRST WILTON BANCSHARES, LTD., WILTON	**33,851**	
FIRST STATE BANK OF WILTON		33,800
68. HSB FINANCIAL CORP, HARWOOD	**31,494**	
HARWOOD STATE BANK, HARWOOD		31,494
69. GRANT COUNTY BANCORPORATION, INC., CARSON	**30,574**	
GRANT COUNTY STATE BANK, CARSON		30,347
70. HATTON BANCSHARES, INC., FARGO	**27,468**	
THE FARMERS A MERCHANTS NATIONAL BANK OF HATTON		27,312
71. QUALITY BANKSHARES, INC., PAGE	**25,407**	
QUALITY BANK, FINGAL		25,391
72. DAKOTA BANKSHARES, INC., FAIRMOUNT	**21,586**	
PEOPLES STATE BANK, FAIRMOUNT		21,586
73. WALL STREET HOLDING CO., HAMILTON	**19,144**	
BANK OF HAMILTON		19,144

1 Acquired during 2012.
2 Blackridge Financial, Inc., reports an ownership interest (17%) in Union Bancshares, Inc., Fargo.
3 Hazen Bancorporation, Inc. reports an ownership interest (16%) in North Star Holding Co., Inc., Jamestown.
4 McIntosh County Bank Holding Co., Inc. reports an ownership interest (33%) in North Star Holding Co., Inc., Jamestown.
5 Bank assets reported as consolidated size for Commercial Bank of Mott Employee Stock Ownership Plan.

*Source: Regulatory financial reports filed by bank holding companies and banks, data as of Dec. 31, 2011. *Dollar amounts in thousands*

Next edition to feature holding company lists for Wisconsin.

SOUTH DAKOTA BANK HOLDING COMPANIES

HOLDING COMPANY, LOCATION Subsidiary Bank, Location	CONSOLIDATED ASSETS*	SUBSIDIARY ASSETS*
1. DACOTAH BANKS, INC., ABERDEEN	**1,905,762**	
DACOTAH BANK, ABERDEEN		1,902,620
2. UNITED NATIONAL CORPORATION, SIOUX FALLS	**1,799,837**	
FIRST PREMIER BANK, SIOUX FALLS		1,119,448
3. FISHBACK FINANCIAL CORP., BROOKINGS	**1,666,810**	
FIRST BANK & TRUST, BROOKINGS		847,317
FIRST BANK & TRUST OF MILBANK, MILBANK		153,891
FIRST BANK & TRUST N.A., PIPESTONE, MN		184,275
FIRST BANK & TRUST, SIOUX FALLS		435,944
FIRST BANK OF WHITE[1]		54,728
4. SECURITY NATIONAL CORP., DAKOTA DUNES	**1,108,490**	
NORTHWESTERN BANK, ORANGE CITY, IA		185,969
SECURITY NATIONAL BANK OF S.D., DAKOTA DUNES		145,315
THE SECURITY NATIONAL BANK OF SIOUX CITY, IA		716,906
5. MINNEHAHA BANSHARES, INC., SIOUX FALLS	**1,059,823**	
THE FIRST NATIONAL BANK IN SIOUX FALLS		1,054,086
6. STOCKMENS LIMITED PARTNERSHIP, RAPID CITY	**856,361**	
SECURITY FIRST BANK, LINCOLN, NE		830,520
7. FIRST DAKOTA FINANCIAL CORP., YANKTON	**848,046**	
FIRST DAKOTA NATIONAL BANK, YANKTON		846,417
8. SOUTH DAKOTA BANCSHARES, INC., PIERRE	**740,564**	
BANKWEST INCORPORATED, PIERRE		739,907
9. CAPITOL BANCORPORATION, INC., BRITTON	**712,810**	
FIRST NATIONAL BANK, FORT PIERRE		696,810
10. HOPKINS FINANCIAL CORPORATION, MITCHELL	**671,018**	
CORTRUST BANK N.A., MITCHELL		666,827

*Source: Regulatory financial reports filed by bank holding companies and banks, data as of Dec. 31, 2011. *Dollar amounts in thousands*

SOUTH DAKOTA BANK HOLDING COMPANIES

HOLDING COMPANY, LOCATION / Subsidiary Bank, Location	CONSOLIDATED ASSETS*	SUBSIDIARY ASSETS*
11. BELLE FOURCHE BANCSHARES, INC., SPEARFISH	**467,271**	
PIONEER BANK & TRUST, BELLE FOURCHE		467,298
12. LEACKCO BANK HOLDING CO., INC., WOLSEY	**378,221**	
AMERICAN BANK & TRUST, WESSINGTON SPRINGS		378,139
13. FIDELITY CORPORATION, BURKE	**310,764**	
FIRST FIDELITY BANK, BURKE		310,748
14. FIRST SLEEPY EYE BANCORP., INC., SIOUX FALLS	**281,682**	
CAPITAL BANK, SAINT PAUL, MN		36,642
FIRST SECURITY BK - SLEEPY EYE, MN		184,095
FIRST SECURITY BANK - CANBY, MN		59,039
BIG SIOUX FINANCIAL, INC., ESTELLINE		223,406
RELIABANK DAKOTA, ESTELLINE		222,993
15. FULDA BANCORPORATION, INC., BRITTON	**199,155**	
FIRST NATIONAL BANK, SLAYTON, MN		193,502
16. PHILIP BANCORPORATION, INC., PHILIP	**165,315**	
FIRST NATIONAL BANK IN PHILIP		164,720
17. ASB BANK HOLDING CO., PIERRE	**148,463**	
AMERICAN STATE BANK OF PIERRE		148,463
18. PARKSTON INVESTMENT CO., PARKSTON	**140,173**	
FARMERS STATE BANK, PARKSTON		138,760
19. H & W HOLDING CO., FREEMAN	**138,732**	
MERCHANTS STATE BANK, FREEMAN		138,697
20. BEULAH BANCORPORATION, INC., SIOUX FALLS	**134,992**	
FIRST SECURITY BANK - WEST, BEULAH, ND		62,096
VALLEY BANK & TRUST, MAPLETON, IA		72,086
21. M & H FINANCIAL SERVICES, INC., MILLER	**130,916**	
QUOIN FINANCIAL BANK, MILLER		130,688
22. COMMERCIAL HOLDING CO., WAGNER	**130,530**	
COMMERCIAL STATE BANK OF WAGNER		130,483
23. HOWARD CTY. LAND & CATTLE CO., RAPID CITY	**117,930**	
CITIZENS BANK & TRUST CO., SAINT PAUL, NE		115,364
24. FIRST STATE BANKING CORPORATION, ALCESTER	**107,229**	
STATE BANK OF ALCESTER		106,990
25. BHCB HOLDING CO., RAPID CITY	**102,552**	
BLACK HILLS COMMUNITY BANK, N.A., RAPID CITY		102,552
26. LEWIS BANSHARES, INC., SIOUX FALLS	**101,396**	
FIRST STATE BANK, ARMOUR		101,354
27. ROSCOE COMMUNITY BANKSHARES, INC., ROSCOE	**98,058**	
FIRST STATE BANK OF ROSCOE		98,058
28. NORTHEAST BANCORP, INC., BRANDON	**94,452**	
FIRST STATE BANK, WILMOT		38,652
PEOPLES STATE BANK, SUMMIT		55,697
29. GREAT PLAINS BANK CORPORATION, EUREKA	**94,041**	
GREAT PLAINS BANK, EUREKA		93,700
30. MERCHANTS HOLDING CO., SIOUX FALLS	**84,620**	
MERCHANTS BANK, RUGBY, ND		82,930
31. PAGE HOLDING CO., PLANKINTON	**84,560**	
FARMERS AND MERCHANTS STATE BANK, PLANKINTON		84,586
32. MIDWEST BANCSHARES, INC., TYNDALL	**73,200**	
DAKOTA HERITAGE STATE BANK, CHANCELLOR		39,236
SECURITY STATE BANK, TYNDALL		34,440
33. WESSINGTON BANKSHARES, INC., WESSINGTON	**70,964**	
HEARTLAND STATE BANK, REDFIELD		70,964
34. UPTOWN BANCORPORATION, INC., BRITTON	**68,312**	
FIRST NATIONAL BANK, DAVENPORT, IA		67,411
35. LINCOLN INVESTMENT CO., LENNOX	**62,966**	
VALLEY EXCHANGE BANK, LENNOX		62,936
36. ELKTON HOLDING CO., ELKTON	**61,747**	
BANKSTAR FINANCIAL, ELKTON		61,747
37. DCNB HOLDING CO., CLEAR LAKE	**60,769**	
DNB NATIONAL BANK, CLEAR LAKE		60,835
38. DRAPER HOLDING CO., INC., FORT PIERRE	**59,006**	
DAKOTA PRAIRIE BANK, FORT PIERRE		59,010
39. YELLOWSTONE TRAIL BANCORPORATION, IPSWICH	**56,662**	
IPSWICH STATE BANK, IPSWICH		56,571
40. RCN HOLDING CO., SISSETON	**52,270**	
THE ROBERTS COUNTY NATIONAL BANK OF SISSETON		52,172
41. FIRST BANK SHARES CORPORATION, WARNER	**49,630**	
FIRST STATE BANK OF WARNER		49,630
42. FAITH BANK HOLDING CO., FAITH	**44,903**	
FARMERS STATE BANK, FAITH		44,782
43. LINCOLN HOLDING CO., CANTON	**44,775**	
FARMERS STATE BANK OF CANTON		44,775
44. THE ADINO CO., ONIDA	**43,394**	
SUNRISE BANK DAKOTA, ONIDA		43,374
45. NORTH CENTRAL FINANCIAL SERVICES, INC., VOLGA	**42,845**	
THE FIRST NATIONAL BANK OF VOLGA		42,562
46. THE BELLINGHAM CORPORATION, SIOUX FALLS	**37,569**	
STATE BANK OF BELLINGHAM, MN		37,207
47. EMERY SECURITY BANCORPORATION, INC., EMERY	**36,828**	
THE SECURITY STATE BANK, EMERY		36,828
48. MENNO HOLDING CO., MENNO	**33,931**	
MENNO STATE BANK, MENNO		33,931
49.BLUNT BANK HOLDING CO., BLUNT	**31,626**	
THE DAKOTA STATE BANK OF BLUNT		31,626
50. WESTERN DAKOTA HOLDING CO., TIMBER LAKE	**30,546**	
WESTERN DAKOTA BANK, TIMBER LAKE		30,546
51. CONSOLIDATED HOLDING CO., OLDHAM	**28,544**	
AMERICAN STATE BANK, OLDHAM		28,544
52. SCOTLAND HOLDING CO., SCOTLAND	**25,744**	
THE FARMERS AND MERCHANTS STATE BANK, SCOTLAND		25,744
53. BRYANT BANCSHARES, INC., BRYANT	**24,860**	
BRYANT STATE BANK, BRYANT		23,394
54. RANDALL BANCSHARES, INC., LAKE ANDES	**21,237**	
ANDES STATE BANK, LAKE ANDES		21,239
55. H2H BANCSHARES, INC., HOSMER	**17,941**	
FARMERS STATE BANK, HOSMER		17,941

[1] Merged with affiliated bank in 2012.

*Source: Regulatory financial reports filed by bank holding companies and banks, data as of Dec. 31, 2011. *Dollar amounts in thousands*

New to BHCA

Join the growing list of Bank Holding Company Association Members and Associate Members. The value of the education members receive through our seminars, publications and unparalleled networking opportunities far exceeds our modest annual dues. See page 13 for more information and join today.

The Bank Holding Company Association welcomes the following holding companies which recently have joined the association:

John Marchell, president
Full Service Insurance Agency Inc.
Buxton, N.D.

Mark J. Sexton
Bart Bank Group, St. Paul, Minn.

Steve Huston, Chairman
Shirley Huston, President
Dan Rodelius, Director
Bankwest Financial Inc., Rockford, Minn.

John E. Babcock, Chairman, CEO
Metro North Bancshares, Inc.
Elk River, Minn.

Luke Jacobson, Assistant Vice President
BMO Harris Bank, Minneapolis

In addition, we are pleased to welcome the following new Associate Members:

Jason Mork, Director – Fixed Income
BMO Capital Markets, Milwaukee

BMO Capital Markets is a leading North American financial services provider offering investment and corporate banking, advisory services, treasury and market risk management, institutional investing, and research.

Jon C. Bruss, Managing Principal & CEO
Fortress Partners Capital Management, LTD.
Hartland, Wis.

Fortress Partners, founded in 1991, advises banks and bank holding companies throughout the United States to assist them in developing and implementing strategic and capital plans. We provide pragmatic advice based upon hands-on experience in the management and oversight of banks and bank investments. We are active investors and investment managers in publicly traded and privately owned bank equities. In addition, we draw on strong working relationships with banking professional s in legal, accounting, investment banking and regulatory arenas to identify appropriate expertise. Fortress Partners also manages investments in banks. Fortress Partners is registered with the state of Wisconsin as an investment advisory firm.

Eric Hilgenberg, Consultant
Equias Alliance, Prior Lake, Minn.

Equias Alliance has successfully helped nearly 800 financial institutions with BOLI placement and with plans to recruit, retain, and reward key officers and directors with nonqualified benefit plans. They also provide administration of BOLI and nonqualified benefit plans.

In Focus,* *Continued from page 12

Income and losses – passive or active — Each shareholder's item of income or loss from an S corporation is treated as active or passive, depending on the shareholder's level of involvement in the activity. For example, if a shareholder actively participates in the management of an S corporation, and the S corporation has a loss, the loss is treated as an active loss to that shareholder. The same loss would be considered a passive activity loss to shareholders who do not actively participate in the business.

Shareholders who do not actively participate in the business may not be able to deduct their passive losses on their individual tax returns. In contrast, C corporation operating losses can generally be carried back to offset prior taxable earnings, with certain limitations.

Increased AGI limitations — Because S corporation income is passed through to the shareholders, the shareholders' adjusted gross income will be increased. The increase in the shareholders' adjusted gross income may negatively impact other individual tax return items, such as: credits for education expenses, IRA limitations, itemized deductions, personal exemptions, taxation of social security benefits, and other items.

The BHCA: A UNIQUE VALUE
for bank owners, officers and directors

If you are a bank owner, the Bank Holding Company Association is the *right* organization for you. Whether your ownership consists of a few shares or 100 percent, you will find BHCA membership delivers unique value to bank owners like you.

Seminars

Members receive discounted registration fees on BHCA's annual Spring and Fall Seminars.
The BHCA seminars consistently deliver informative presentations from industry experts, consultants and analysts. They educate as well as entertain. Break-out sessions give seminar participants the opportunity to go in-depth on very specific topics to bank owners, such as succession planning, tax issues, merger and acquisition preparation, legal/accounting issues and more.

Networking

Get access to other bank owners.
One of the most valuable features of our twice-a-year seminars is the opportunity to visit with other bank owners between scheduled presentations.
It has been said that more merger and acquisition deals have been initiated at BHCA seminars than almost anywhere else.
No other group brings together so many bank owners from across the Upper Midwest.

Insight

Appreciate our regional focus.
With holding company members from Minnesota, Wisconsin, North Dakota, South Dakota, Iowa and Illinois, the BHCA brings together bank owners, directors and officers with common regional interests, but if you don't want to talk to a competitor, you can always find similarly-situated members from outside your holding company's trade area.

Access

Gain access to regulators.
BHCA frequently hosts events featuring representatives from the Federal Reserve, Federal Deposit Insurance Corp., Office of the Comptroller of the Currency, and state regulatory agencies.
Forums permit anonymous questions, as well as opportunities for you to visit directly with regulators.

Gain access to experts.
The BHCA features a healthy associate membership sector, providing bank owners with access to attorneys, accountants, investment professionals, consultants and others who can address virtually any need a bank owner may have.

Read what some long-time BHCA members have to say:

Serious, useful education…

"We chose to join BHCA in about 1990, shortly after we formed a new holding company to purchase a divested First Bank System bank in 1987. We were new at the process and thought that joining BHCA would be a great educational experience. Since that time several of us have managed to attend nearly every seminar.

Ideas we implemented from the seminars include mandatory retirement of both bank and holding company directors, general director responsibilities, audit and compliance committee ideas, and excellent presentations by economists over the years to assist us in funds management. And, of course, there is always the exchange of ideas with fellow bankers." - *Gary Paulson, First Holding Company, Park River, N.D.*

Building relationships…

"I have been a member of the Bank Holding Company Association for more than 20 years, during which I have attended Spring and Fall Seminars regularly. The value of this association is the great contacts and speakers who inevitably become business relationships. The BHCA brings together bank owners who have the same problems and concerns within their own organization. I challenge bankers to find a better value for an annual membership which is as little as $400." *- Douglas Jilek, Prairie Bancshares, Inc., Lester Prairie, Minn.*

A great value…

"Our holding company is a charter member of the BHCA. The association provides excellent value as evidenced by the networking opportunities, top-notch speakers, and the wide range of educational opportunities available through the concurrent breakout sessions. In this day of aggressive cost-cutting, our BHCA membership is a certain renewal!" *- Pat Gates, Security Financial Services, Inc., Hibbing, Minn.*

Membership:

Annual dues to the Bank Holding Company Association range from $400 to $1,000 per year, depending on the size of your organization.

For more information, please call us at 952-835-2248 or 1-800-813-4754

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WEBINAR

The Bank Holding Company Association presents…

Bank acquisitions and valuation... To sell or not to sell

This presentation will look at the environment for bank mergers and acquisitions. We will look at the factors that are affecting M&A activity. Topics will include the current banking environment (regulation, interest rates, and Basel III), M&A trends and statistics, and future opportunities for both buyers and sellers of banks.

Our presenter is **John Hense, Jr.**, managing director of CC Capital Advisors, the Kansas City-based investment banking arm of County Club Bank. Utilizing more than 25 years of diversified financial experience, Hense manages projects in the areas of mergers and acquisitions, private placements of debt and equity, financial and strategic planning, and general business advisory.

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