VIA ELECTRONIC MAIL to SIGTARP.response@do.treas.gov
AND VIA UPS NEXT DAY AIR

March 5, 2009

Mr. Neil M. Barofsky
Special Inspector General
Troubled Asset Relief Program
1500 Pennsylvania Ave., N.W.
Suite 1064
Washington, D. C. 20220

Dear Mr. Barofsky:

On December 19, 2008, Union Bankshares Corporation ("UBSH") received a $59 million investment in its Series A preferred stock from the U. S. Treasury through the Capital Purchase Program ("CPP") under the Troubled Asset Relief Program ("TARP"). Our participation in this program was predicated upon the U. S. Treasury's stated objective to attract broad participation by healthy financial institutions to expand the flow of credit to consumers and businesses and promote the sustained growth and vitality of the U. S. economy.

In response to your letter of February 6, 2009, we submit the following responses to the specific information requested:

(1)(a) Anticipated use of TARP funds

It has been and remains our intent to continue to lend money to qualified borrowers in the markets we serve using sound lending practices. As demonstrated by the various advertisements, press releases and news articles included in the attached appendix, we have been actively promoting public awareness of our sound capital position (with or without the Treasury investment) and our desire to make loans to qualified borrowers in each of our markets. We think these efforts will result in increased consumer, and business confidence and demand for loans.

While the capital investment itself did not increase loan demand or change what constitutes sound lending practices, it does provide flexibility in our approach to lending. One example of this is a new program we have just introduced to provide consumer mortgage financing on purchases of unsold homes from our home builder customers. (b) (4) [redacted]

We will continue to work with our borrowers to work through credit problems and develop creative ways to solve them. We will also continue to work with small businesses and consumers to meet their current credit needs.

(1)(b) Whether the TARP funds were segregated from other institutional funds

Union Bankshares Corporation is a three bank holding company whose subsidiary banks are Union Bank and Trust Company ("UBT"), Northern Neck State Bank ("NNSB"), and Rappahannock National Bank ("RNB"). As a multi-bank holding company, we can utilize the proceeds from the Treasury's investment in two principal ways. The first is to deposit the proceeds in our corporate checking account at one of our subsidiary banks. This increase in deposits on the bank's balance sheet provides liquidity/funding for the bank to use to make loans to its customers. The second method is to contribute capital to our subsidiary banks. This provides the funding to make loans as well as adequate capital for the bank to leverage such new capital approximately ten times and still maintain its required risk-based and other capital ratios.

(1)(c) Actual use of TARP funds to date

At this time, we have contributed capital totaling $10 million to two of our subsidiary banks to provide capital to support their lending initiatives. We have $29 million on deposit at one of our subsidiary banks, providing liquidity to that bank including funding for loans. The remaining $20 million has been invested in short-duration agency securities to provide a relatively safe return to offset a portion the 5% cost of the Treasury investment. [redacted] (b) (4)

While this summarizes the flow of the proceeds from the Treasury, it is only part of the story. Since December 19, 2008, when we received these proceeds, through January 31, 2009, our gross loans, including loans held for sales by our mortgage origination subsidiary, have increased from $1,895 million to $1,915 million. The message to our bankers and the consumers is the same and constant -- we are making loans.

(1)(d) Expected use of unspent TARP funds

It is expected that as loan demand increases and loans continue to be made, the remaining funds which reside at the parent company will be transferred to the subsidiary banks in the form of capital needed to support lending and maintain capital ratios. [redacted] (b) (4)

(2) Specific plans and status thereof for addressing executive compensation requirements associated with the funding

We have reviewed the executive compensation requirements for banks that have received the Treasury investment and believe we are compliant with such requirements. For example, on February 24, 2009, UBSH's Compensation Committee reviewed with senior risk officers the senior executive officers' ("SEOs") incentive compensation arrangements and made reasonable efforts to ensure that such arrangements do not encourage the SEOs to take unnecessary and excessive risks that threaten the value of the Company. We expect to include the Compensation Committee's certification of the foregoing in the 2009 Proxy Statement to be issued later this month. We also recognize that as a CPP participant, during the period in which any obligation arising from assistance provided under the CPP remains outstanding, UBSH is to permit a separate and non-binding shareholder vote to approve the compensation of executives, as disclosed pursuant to the compensation disclosure rules of the Securities and Exchange Commission (the "SEC"). Such a proposal, commonly known as a "say-on-pay" proposal, which gives shareholders the opportunity to endorse or not endorse UBSH's executive pay program, will be included in the 2009 Proxy Statement along with a proposed resolution for approval. We will continue to monitor the Treasury website to assure ongoing compliance.

In addition, we previously announced a reduction of our February 28, 2009 dividend from $0.185 to $0.12 per share based on fourth quarter earnings of $0.17 per share. This was a difficult decision because it was one of the few dividend reductions in the 100+ year history of our banking organization but a necessary step under current economic conditions and in light of our current profitability.

We hope this information is helpful to you. Should you have questions, please feel free to contact me at [redacted], our Chief Financial Officer, D. Anthony Peay at [redacted], or our General Counsel, Janis Orfe at [redacted].

By my signature below, as UBSH's President and Chief Executive Officer, I certify that I have reviewed this response and the enclosed supporting documentation provided. Based upon my knowledge, this response and the supporting documents do not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading.

Very truly yours,

William Beale

G. William Beale
President and Chief Executive Officer

Attachments

Itemization of Attachments to letter dated March 5, 2009

Page #s	Description	Date
1-2	Safety and Soundness Letter to Customers	10/10/08
3	"Where We Stand" Ad (UBT)	Oct.-Dec. '08
4	"Where We Stand" Ad (NNSB)	Oct.-Nov. '08
5	"Where We Stand" Ad (RNB)	Oct. '08
6	Capital Purchase Program Press Release	12/15/08
7	Capital Purchase Program Letter to Customers/Shareholders	12/16/08
8	"Where We Stand on Lending" Ad (UBT)	Jan.-Feb. '09
9	"Where We Stand on Lending" Ad (NNSB)	Jan.-Feb. '09
10	"Where We Stand on Lending" Ad (RNB)	Jan.-Feb. '09
11	Medical Lending Ad (UBT)	Jan. '09
11	Small Business Lending Ad (UBT)	Jan. '09
12	"Family Stimulus Plan" Ad (UBT)	Mar.-Apr. '09
13	"Challenge Us" Business Banking Ad (UBT)	Mar.-Apr. '09
14	Mortgage/Equity Lending Ad (NNSB)	Spring '09
15-19	Richmond Times-Dispatch Article, "Safe and Sound"	02/08/09
20-22	The Washington Post Article, "Federal Aid/Revive Lending"	02/03/09
23-26	Richmond Times-Dispatch Article, "Richmond Bank Loans"	03/01/09

Safety and Soundness Letter

- Mailed October 10, 2008
- Delivered to all customers

UNION BANKSHARES
CORPORATION

October 10, 2008

To our valued customers of our community banks:

For many of us, the recent turmoil in *investment* banking circles seemed far away from community banking as we know it. Then, recently, the largest bank operating in Virginia, Wachovia, was sold - basically for losses related to its acquisition of a California savings institution that was heavily invested in the sub-prime mortgage industry.

That news brought the credit market crisis home to all Virginians and generated a mix of emotions, including our own genuine disappointment as bankers with the practices of some financial institutions.

First, despite what has happened in a few instances, banks are still the safest place you can put your money and the only place where those savings are guaranteed to grow. Second, your deposits with us are insured by the FDIC, which ranks all of our banks as "well-capitalized," its highest designation. Finally, because we are a multi-bank holding company, we can distribute large deposits that exceed FDIC limits among our member banks to increase your FDIC insurance protection.

The national financial crisis may have raised questions in your mind about how our community banks operate. We'd like to tell you where we stand:

- We stand on solid banking ground . . . on sound principles and honest dealings.
- We stand by our customers and their communities through changes in their lives and changing times.
- We stand against financial fads, against risks we would not take for our own families and against products no one understands.
- We stand where we've stood since 1902 . . . on Virginia soil with the people who live and work around us.
- Stated simply, we stand for you.

This approach has worked for customers of our banks through ups and downs of the economy from the Great Depression to smaller, more recent disruptions. We have had *no* exposure to sub-prime mortgages; we have never been in that business. Our investment portfolio did not include stock issued by Fannie Mae or Freddie Mac, or any of the investment banking and brokerage firms in the recent

A UNION OF COMMUNITY BANKS

P.O. Box 446 • Bowling Green, Virginia 22427-0446 • (804) 633-5031 • www.ubsh.com

Safety and Soundness Letter – Page 2

headlines with solvency problems. We use your deposits to invest in the best and safest places we know: our own communities.

We are not immune to disruptions or downturns in the economy but we are equipped to deal with them. Our credit quality and credit management has received heightened attention. We will build loan loss reserves, taking into consideration analysis of our loan portfolio and the uncertainties in the economy. Our annualized loan charge-offs and non-performing loans remain well below levels reported by most publicly traded banks based in Virginia. Because our overall credit quality is strong, we continue to be able to support the credit requirements of our customers.

In these difficult times, the Union Bankshares member banks remain profitable. We will continue to serve the people and businesses in our communities.

We value you as a customer. You have placed your financial assets with us because you trust us. Thank you. We will continue to manage our banks in a prudent manner that reinforces the trust you have placed in us.

G. William Beale
President and CEO
Union Bankshares Corporation

D. Anthony Peay
Executive Vice President and CFO
Union Bankshares Corporation

John C. Neal
President and CEO
Union Bank and Trust Company

N. Byrd Newton
President and CEO
Northern Neck State Bank

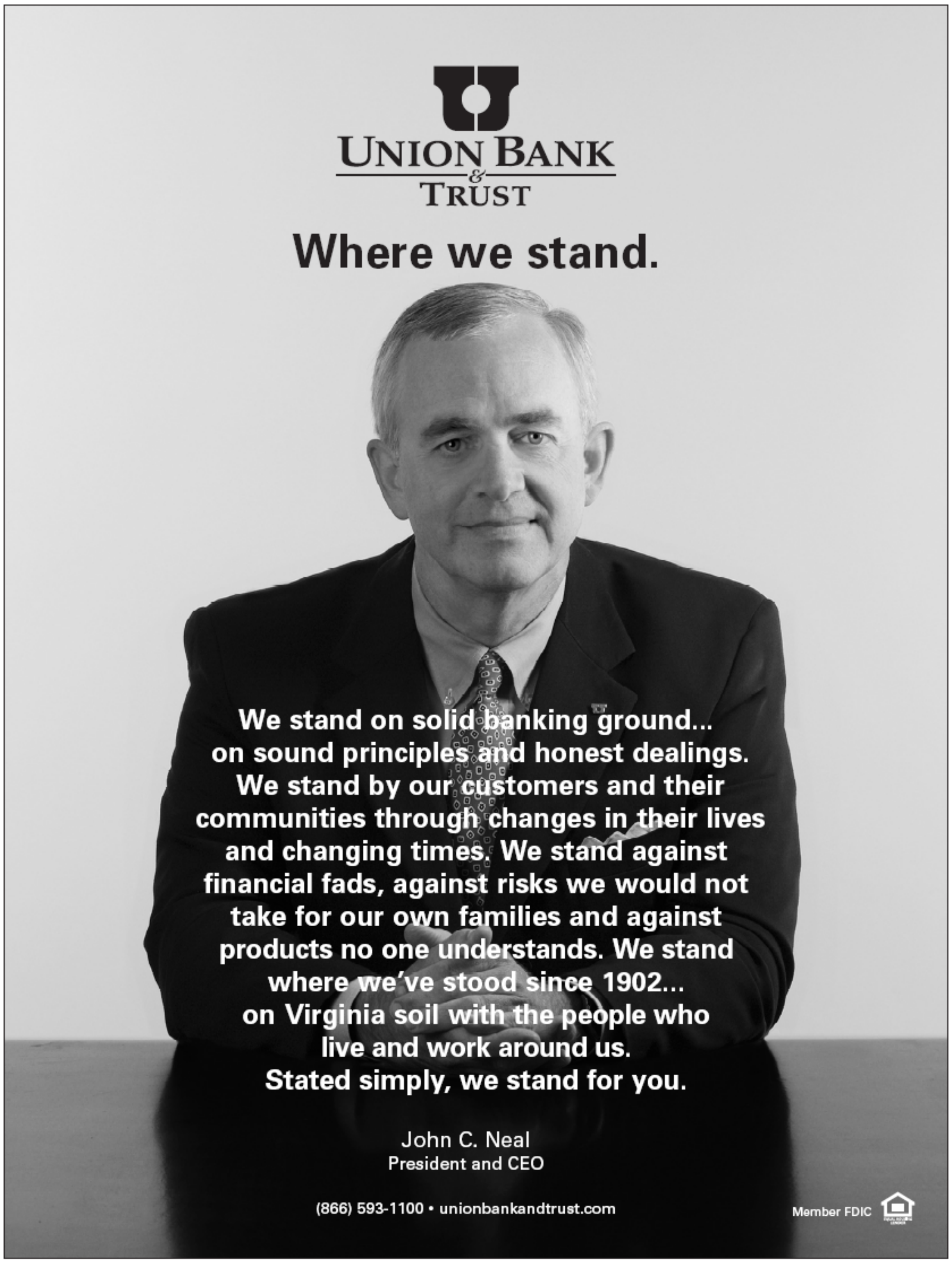
Michael T. Leake
President and CEO
Rappahannock National Bank

Robert L. Bailey
President and CEO
Bay Community Bank

“Where we stand.”

Union Bank & Trust Newspaper Advertising

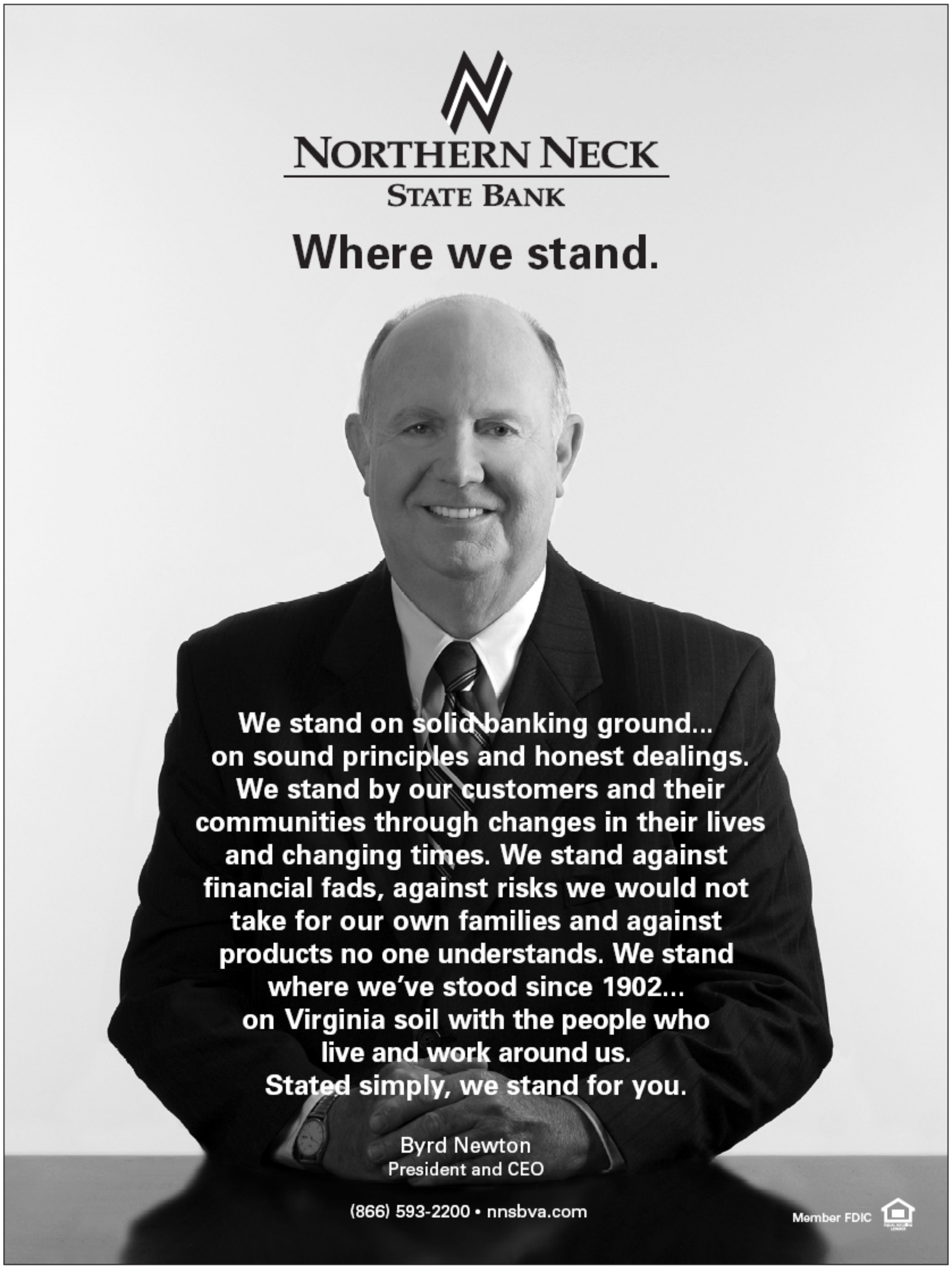
- Placed in Richmond Times-Dispatch, Fredericksburg Free-Lance Star, Charlottesville Daily Progress, Newport News Daily Press, Fairfax County Times, Virginia Gazette
- October - December 2008



“Where we stand.”

Northern Neck State Bank Newspaper Advertising

- Placed in Rappahannock Record, Westmoreland News, The Northumberland Echo, The Northern Neck News, The Rappahannock Times
- October - November 2008



“Where we stand.”

Rappahannock National Bank Newspaper Advertising

- Placed in Fauquier Times-Democrat, Winchester Star, Culpeper Star-Exponent
- October 2008

Capital Purchase Program Press Release

- December 15, 2008

Contact: D. Anthony Peay - (804) 632-2112
Executive Vice President/ Chief Financial Officer

Distribute to: Virginia State/Local News lines, NY Times, AP, Reuters, S&P, Moody's, Dow Jones, Investor Relations Service

December 15, 2008 **Traded: NASDAQ** **Symbol: UBSH**

UNION BANKSHARES CORPORATION RECEIVES PRELIMINARY APPROVAL UNDER TREASURY CAPITAL PURCHASE PROGRAM

FOR IMMEDIATE RELEASE (Bowling Green, Virginia) --- Union Bankshares Corporation (the "Company") (NASDAQ: UBSH - News), the parent company of Union Bank and Trust Company, Northern Neck State Bank, and Rappahannock National Bank, today announced it has received preliminary approval for a $59 million investment from the U. S. Treasury under the Treasury Capital Purchase Program. The program was designed to attract broad participation by healthy financial institutions to expand the flow of credit to consumers and businesses and promote the sustained growth and vitality of the U. S. economy.

Under the program, the Company would issue to the U. S. Treasury up to $59 million of preferred stock and warrants to purchase. The preferred shares would be non-voting and will pay a dividend of 5% annually for the first five years after issuance and 9% annually thereafter, unless redeemed. Additionally, the Treasury will receive warrants, with a term of 10 years, on approximately $9 million of the Company's common stock. The Treasury's term sheet with additional detail about the Capital Purchase Program is available on the Treasury's website at www.treas.gov/initiatives/eesa. Although the Company currently intends to participate in the program and expects closing to occur prior to December 31, 2008, it will continue to monitor and evaluate any additional governmental requirements that may diminish the value of, or unduly burden, participation in the program.

"We are pleased to participate in this program, which has been intentionally designed to stabilize our financial markets and provide an additional margin of strength to institutions that are best positioned to overcome the current economic climate. While each of our banks is well capitalized above regulatory guidelines, this additional capital will further strengthen our already strong position. It will allow us to provide much needed credit to consumers and businesses in our markets, as well as the flexibility to evaluate future opportunities that may arise," said G. William Beale, President and Chief Executive Officer of Union Bankshares Corporation. *"We fully intend to use this additional capital in a manner that best serves the communities and financial markets we serve."*

The final approval of the Treasury and closing of the transaction is subject to the Treasury's standard terms, closing conditions and documentation.

* * * * * * *

Capital Purchase Program Letter

- Mailed December 16, 2008
- Delivered to all customers and stockholders

UNION BANKSHARES
CORPORATION

December 16, 2008

Dear Customers and Shareholders:

Union Bankshares Corporation has received notification of preliminary approval from the United States Treasury that it intends to make a preferred stock investment in Union Bankshares through the U.S. Treasury's Capital Purchase Program for healthy banks. Under the plan, the U.S. Treasury would invest $59 million in Union Bankshares preferred stock on which it would receive a dividend of 5% annually. The plan would also provide the U.S. Treasury with warrants to purchase approximately $9.0 million in common stock. It is our intention to participate in the Capital Purchase Program and we expect to close this transaction prior to year end 2008.

We would like to be clear about two very important points. First, for banking organizations the size of Union Bankshares this is not a "bailout" – a term you may have heard used by the media and many others. The U.S. Treasury has stated that the Capital Purchase Program is only for healthy banks. The program is intended to provide capital to qualified banks to expand the flow of credit to consumers and businesses to promote the sustained growth and vitality of the economy. Secondly, we view this capital investment by the U.S. Treasury to be a temporary bridge until the capital markets become healthy and stable, which will permit Union Bankshares to make a follow-on or secondary public offering of its common stock.

We want you to know that for more than a year, as part of its normal capital management process, Union Bankshares has been exploring various avenues to raise additional common equity through the capital markets to support opportunities that we anticipate could bring both organic and acquisition growth. The volatility of the capital markets, when combined with the deep discounts to current market prices required by investors, would have resulted in a dilution of our current shareholders' interests and a decrease in earnings per share. Management concluded such results would be unacceptable, especially since we believe the pricing shown by the capital markets for follow-on offerings over the last year has been more reflective of the problem banks, which have needed capital, not a healthy banking organization such as Union Bankshares.

The capital investment from the U.S. Treasury will allow Union Bankshares to take advantage of opportunities to grow organically through loans to well-qualified individuals and businesses in our marketplace, consistent with the intent of the U.S. Treasury.

Union Bankshares fully expects to complete a follow-on offering of common stock to repurchase the U.S. Treasury investment as soon as the capital markets return to a more healthy state.

Union Bankshares and its subsidiaries are healthy, well-capitalized and have been committed to supporting the prosperity of our markets for over 100 years. We look forward to continuing to serve your financial needs now and in the future.

Sincerely,

G. William Beale
President and CEO
Union Bankshares Corporation

A UNION OF COMMUNITY BANKS

P.O. Box 446 • Bowling Green, Virginia 22427-0446 • (888) 554-5031 • www.ubsh.com

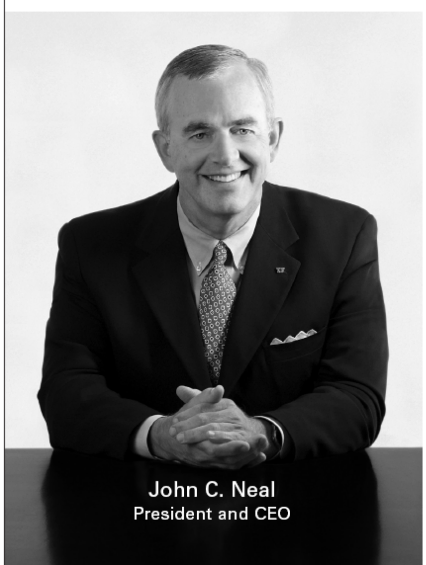
“Where we stand on lending.”

Union Bank & Trust Newspaper Advertising

- Placed in Richmond Times-Dispatch, Fredericksburg Free-Lance Star, Charlottesville Daily Progress, Newport News Daily Press, Fairfax County Times, Virginia Gazette, Chesterfield Observer
- January - February 2009

Where we stand on lending.

You hear on the news that banks aren’t lending. Those stories aren’t about us. Yes, these are tough times, and many banks are ultra cautious. But Union Bank & Trust went into this economic crisis healthy, and we remain so. We continue to do what we’ve always done… help our customers get on with the business of living. Buying a car, sending kids to college, owning a home and running a business are worthy goals that need not be put on hold. For more than 100 years, we’ve been able to help people in good times and bad.



What can we do to help you right now?

UNION BANK & TRUST

(866) 593-1100 • unionbankandtrust.com
Member FDIC

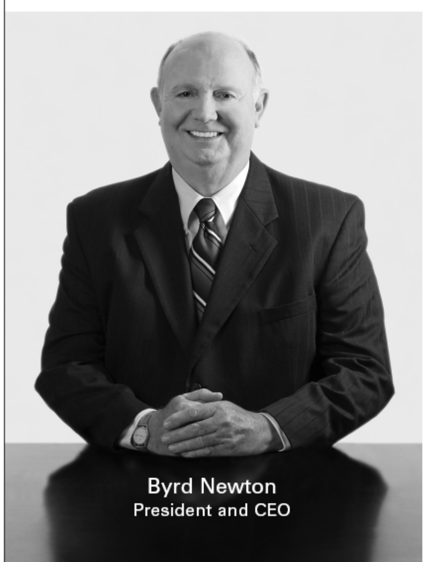
“Where we stand on lending.”

Northern Neck State Bank Newspaper Advertising

- Placed in Rappahannock Record, Westmoreland News, The Northumberland Echo, The Northern Neck News, The Rappahannock Times
- January - February 2009

Where we stand on lending.

You hear on the news that banks aren’t lending. Those stories aren’t about us. Yes, these are tough times, and many banks are ultra cautious. But Northern Neck State Bank went into this economic crisis healthy, and we remain so. We continue to do what we’ve always done…help our customers get on with the business of living. Buying a car, sending kids to college, owning a home and running a business are worthy goals that need not be put on hold. For more than 100 years, we’ve been able to help people in good times and bad.



Byrd Newton
President and CEO

What can we do to help you right now?

NORTHERN NECK
STATE BANK
(866) 593-2200 • nnsbva.com
Member FDIC

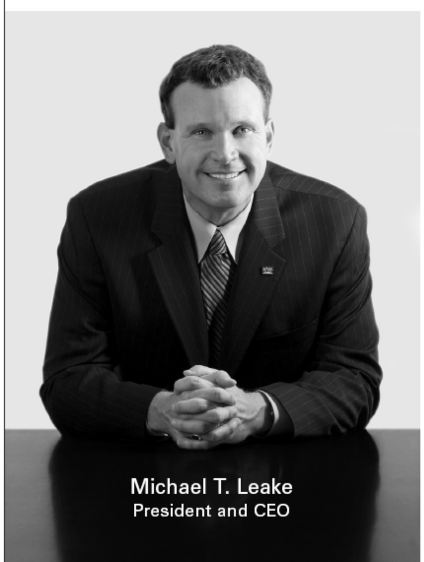
“Where we stand on lending.”

Rappahannock National Bank Newspaper Advertising

- Placed in Fauquier Times-Democrat
- January - February 2009

Where we stand on lending.

You hear on the news that banks aren’t lending. Those stories aren’t about us. Yes, these are tough times, and many banks are ultra cautious. But Rappahannock National Bank went into this economic crisis healthy, and we remain so. We continue to do what we’ve always done… help our customers get on with the business of living. Buying a car, sending kids to college, owning a home and running a business are worthy goals that need not be put on hold. For more than 100 years, we’ve been able to help people in good times and bad.



What can we do to help you right now?

RNB
RAPPAHANNOCK
NATIONAL BANK
(866) 593-4400 • rappahannockbank.com
Member FDIC

Medical Financing

Union Bank & Trust Newspaper Advertising

- Placed in Richmond Times-Dispatch Metro Business
- January 2009

Small Business Loans

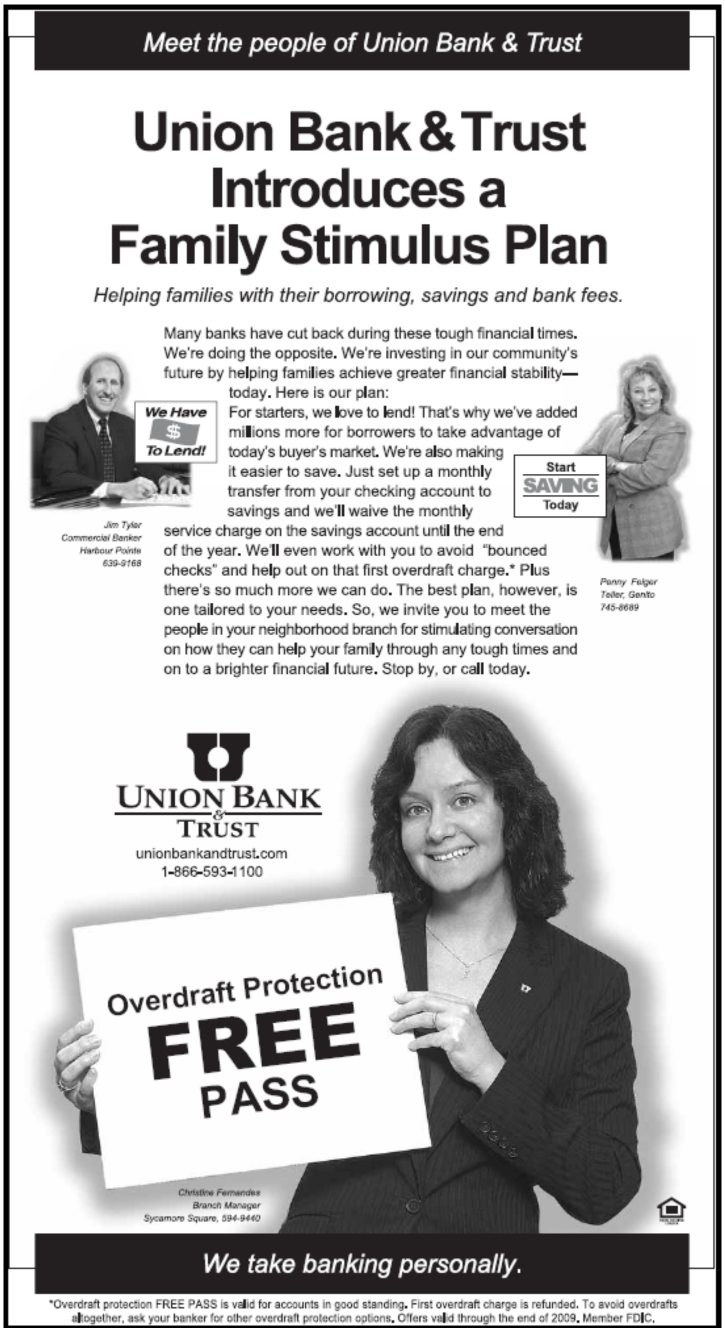
Union Bank & Trust Newspaper Advertising

- Placed in Richmond Times-Dispatch Metro Business
- January 2009

“Family Stimulus Plan”

Union Bank & Trust Newspaper Advertising

- Scheduled in Richmond Times-Dispatch, Fredericksburg Free-Lance Star, Charlottesville Daily Progress, Newport News Daily Press, Fairfax County Times, Virginia Gazette, Chesterfield Observer, Nelson County Times, Fluvanna Review, Caroline Progress, Mechanicsville Local, King George Journal, Country Courier
- March - April 2009



“Challenge Us!”

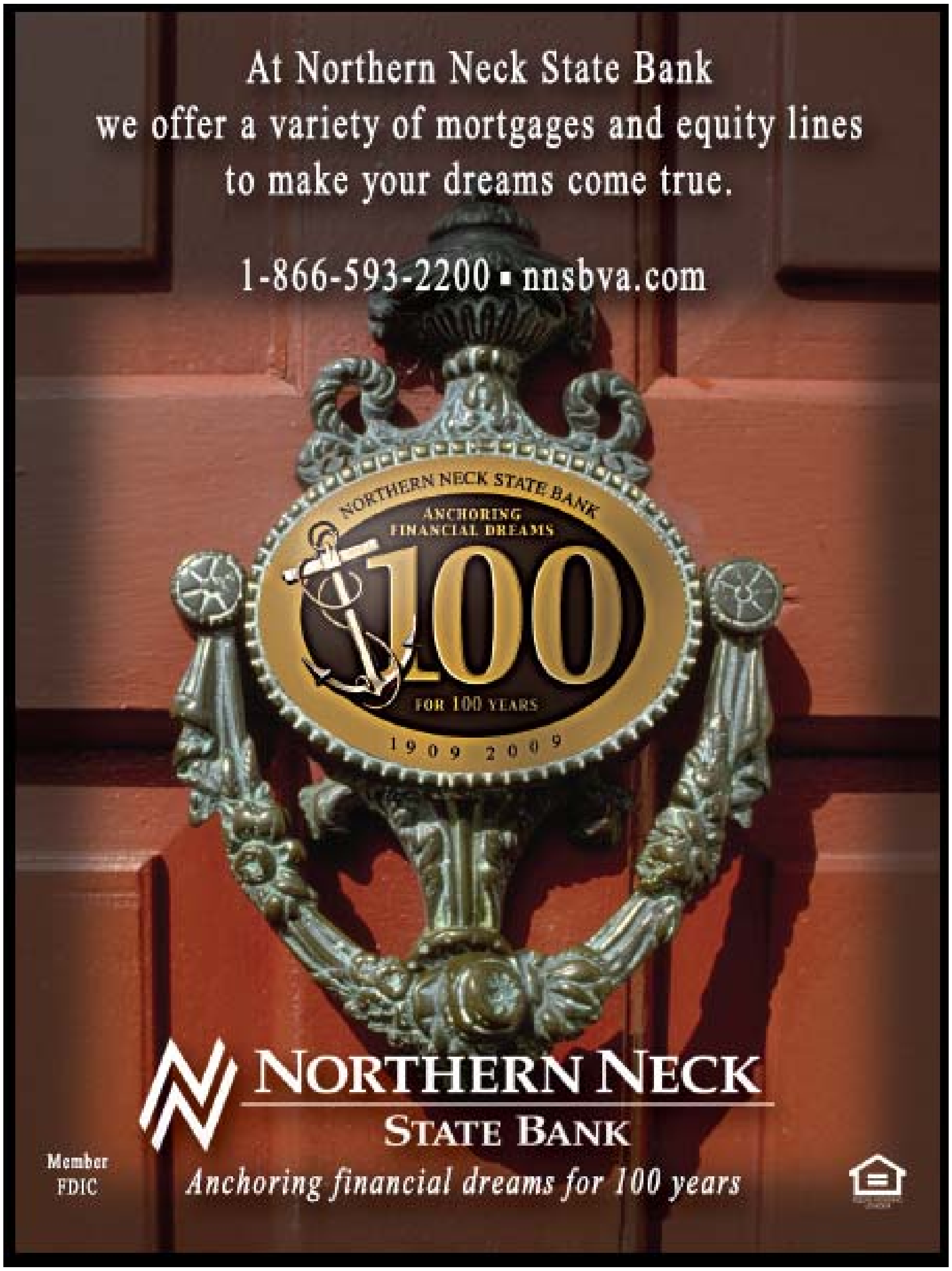
Union Bank & Trust Advertising

- Scheduled in Greater Springfield Chamber of Commerce Image Magazine
- March-April 2008 issue.

Mortgage and Equity Lines

Northern Neck State Bank Advertising

- Scheduled in House and Home Magazine
- Spring 2009 issue



Press Coverage

Richmond-Times Dispatch

- Article published February 8, 2009

Subject: Safe and secure?
Date: February 8, 2009
Source: Richmond Times-Dispatch (VA)
Word Count: 1367

Feb. 8--Most banks are safe and sound. They want to get that message out.

"Live solid, bank solid" is a marketing campaign kicked off in mid-November by Atlanta-based SunTrust Banks Inc., the fourth-largest bank in the Richmond area based on deposits.

"Still strong. Still lending" is a slogan used by BB&T Corp. of Winston-Salem, N.C., the area's third-largest bank.

The messages come as the U.S. banking system remains under siege from years of lenders and borrowers taking on huge risks.

Many banks that got into trouble were over-leveraged, lending too much money to people who couldn't afford to pay back loans.

But experts say the system will emerge strong from this crisis.

Banks need to get back to business basics, making good loans to people who can afford to pay them back.

Financial institutions also need to get the bad assets off their books. One plan calls for the government to step in to absorb bad assets that brought down national players, such as Washington Mutual and Wachovia Corp.

Not all banks have bad assets on their books, so they are assuring customers through advertisements and mailings that they are safe and sound.

"One of the best messages you can get across in an environment where people are clearly uncertain is that their financial institution is solid and secure," said David J. Urban, a marketing professor at Virginia Commonwealth University.

"If people want a safe place to put their money, banks are as safe as it gets, especially since insurance on deposits was raised [last fall] from $100,000 to $250,000," Urban said. The insurance is on one depositor's account at one institution.

"The difficulties at some large banks cast a negative halo on the industry," Urban said. "Banks in good shape have to combat the negative publicity."

Some banks are quick to distance themselves from the turmoil. They say they never strayed from sound business principles.

But they, too, are dealing with the economic downturn, the fallout from the credit freeze and bad mortgage-backed securities that are still making their way through the system.

Mortgage-backed securities were jumbled together -- good mortgages along with bad ones -- and then sliced, repackaged and resold on Wall Street.

"The economy is struggling, and we are impacted along with everyone else," said Gail Letts, president and chief executive officer of SunTrust in central Virginia.

"But our strategy will get us, our clients, and our associates through this."

The emphasis is on making good loans for the right reasons -- "the same as it's always been," she said.

She said she sees no reason to dramatically change strategy. "We have never been a flashy institution."

The bank's "live solid, bank solid" marketing push is based on the notion that consumers are embracing frugality, while seeking financial partners that give them confidence, the bank said in announcing the slogan.

Union Bankshares Corp. in Bowling Green, the area's seventh-largest bank, is honing in on its longevity as a 100-year-old bank to reassure customers and shareholders, said Anthony

Peay, executive vice president and chief financial officer.

"The recent turmoil in investment banking circles seemed far away from community banking as we know it," Union Bankshares' executives wrote in a letter to customers.

They told customers they were disappointed by the business practices at some financial institutions.

"We stand where we've stood since 1902 -- on Virginia soil with the people who live and work around us," they wrote.

"This approach has worked for customers of our banks through ups and downs of the economy from the Great Depression to smaller, more recent disruptions."

Banks have little appetite for risk, as more people lose jobs and consumers cut back on spending. Even good loans made for the right reasons to people with good credit offer no guarantees.

"I am concerned about borrowers' ability to make loan payments if they are making widgets and no one is buying widgets," said Thomas W. Winfree, president and chief executive officer of Village Bank and Trust Financial Corp. in Midlothian, the area's eighth-largest bank.

Still, small banks should not be painted with the same brush strokes as big banks, Winfree said. For the most part, they are well-capitalized and profitable.

"Trustworthiness is not an issue for us, but I'm not going to speak for the big Wall Street firms or the megabanks."

The balance sheets of most small banks are free of poorly valued investments such as mortgage-backed securities that are worth less than the loan amounts, he said.

"We did not participate in the subprime origination of home loans and for the most part we are not in need of being bailed out."

Small banks will survive, Winfree said. "And they will not be a burden on the taxpayers of our country. . . . Our country will not become stable again without the help of community banks."

J. Alfred Broaddus Jr., former president of the Federal Reserve Bank of Richmond, said small banks are part of the solution, since they are making loans in the communities where they serve. However, they do not have the financial heft of large institutions providing banking needs of large corporations.

What's needed is the removal of bad assets from bank balance sheets, he said.

Giant banks weren't the only ones hurt by exotic, mortgage-backed securities. Many mid-size banks were involved.

And small banks that invested in Fannie Mae and Freddie Mac, at the encouragement of regulators, were blindsided as well. Those mortgage giants were taken over by the federal government after their exposure to bad mortgage loans came to light.

Banks will continue to write down these losses, he said, or the bad assets will be pooled into a government-run bank.

Either way, a stable banking system is critical to the health of the U.S. economy, Broaddus said.

What happens to the banking system is the most important story about the economy, he said.

"Once lending confidence in the credit market is restored, especially in banking, that will be the beginning of the upturn."

Banks need capital to make loans, and the government is providing plenty through the Troubled Assets Relief Program. But private investors need to pony up as well, Broaddus said.

Yet, investors remain leery, as bad assets continue to make their way through the system. Even the brightest minds in banking can't get a handle on the extent of the damage.

"I would like to think that a lot is behind us, but no one knows how much is left," Broaddus said. Nor does anyone know how to value the assets.

The government will need to assist in relief efforts, possibly to a significant degree, he said. The Treasury Department had invested $195.3 billion in 359 institutions in 45 states and

Puerto Rico as of Jan. 30.

The financial system suffered a crisis of confidence last fall and it has yet to recover, said Derek Ferber, a research analyst with SNL Financial in Charlottesville.

"These are very strange times indeed," Ferber said. "The government is doing everything it can to stabilize the credit markets and these banks." Kent Engelke, chief economic strategist at Capitol Securities Management, an investment firm in Richmond, said he thinks the worst is over.

"Overall bank lending will increase in the next 100 days," he said. "Bank reserves are at an all-time high, and they are going to lend money out."

Plus, "esoteric structured finance vehicles [mortgage-backed securities] will be off the balance sheet or they will be priced higher," so financial institutions can take less of a hit on their financial statements, Engelke said.

Instead of being valued at 1 cent on $1, for example, the securities will be worth 40 cents on $1, he said.

"The government is doing a good job of keeping confidence in the system," Engelke said. "In 100 days, things will look considerably different than they do today."

Contact Carol Hazard at (804) 775-8023 or chazard@timesdispatch.com.

The Washington Post

Despite Federal Aid, Many Banks Fail to Revive Lending

By Binyamin Appelbaum
Washington Post Staff Writer, Tuesday, February 3, 2009; A01

The federal government has invested almost $200 billion in U.S. banks over the last three months to spark new lending to consumers and businesses.

So far, it hasn't worked. Lending has declined, and banks that got government money on average have reduced lending more sharply than banks that didn't.

Consider the case of Bethesda's EagleBank, which received $38.2 million from the Treasury Department in early December.

The company, which focuses on lending to local businesses, was delighted to get the money, executives said. Its nine-member board convened an impromptu conference call during the week of Thanksgiving to approve the deal.

But EagleBank used roughly half the money to digest the acquisition of Fidelity & Trust Bank, a Bethesda rival with financial problems.

And it has struggled to use the rest to increase lending.

The government investment boosted EagleBank's capital, a cash reserve that regulators require banks to hold as a cushion against losses. More capital meant EagleBank could make more loans, but the company has not been able to take advantage. Lending also requires deposits, the money that banks give to borrowers, and EagleBank's deposit base shrank over the past three months.

"You look around and everyone is saying, 'Banks are not lending,' " said Ronald Paul, EagleBank's chairman. "Well, we'd like to. I could grow my loan base considerably if I just had the deposits."

EagleBank's struggles are part of a broader national pattern and illustrate the complexity of the government's attempt to prop up the economy. Rather than investing in the banks best equipped to increase lending, the government invested disproportionately in banks that needed money to solve problems. Those banks often were ill-equipped to increase lending because of financial limitations such as a lack of deposits.

Senior administration officials have said, though, that they are largely satisfied with the results of the first round of investments. They say the true achievement is something that did not happen: The banking system did not collapse.

But the volume of loans outstanding from U.S. banks fell about 1 percent during the last three months of the year, according to Federal Reserve data. The decline was more than twice as large among banks that accepted taxpayer funds, according to an analysis of fourth-quarter financial reports from 115 companies. The Fed reported yesterday that most banks have continued tightening lending standards.

Some of the first banks to get funding, such as Citigroup and J.P. Morgan Chase, have reported the sharpest drops in lending. In the face of public pressure to use the money, Citigroup plans to announce today that it will spend $36.5 billion on increased lending because of the government's investment in the company.

"You can't just snap your fingers and make this happen," said William Beale, chief executive of Virginia-based Union Bankshares, which got $59 million from the government in mid-December after trying to raise private capital for more than a year. "It's going to take some time for us to raise deposits," Beale said, "and then we can deploy some loans."

Several recipient banks in the Washington area are digesting acquisitions. Bank of Essex, a subsidiary of Community Bankers Trust of Glen Allen, Va., for example, has bought two failed banks from regulators, including a deal announced Friday for Suburban Federal Savings Bank of Crofton.

Others are dealing with problems of their own making. Recipients of government investments in Virginia and Maryland -- no District bank has received money -- on average had lower capital levels than banks that have not received money. Community Financial of Staunton, Va., said the government's money restored its status as a "well-capitalized" bank.

The local pattern is a miniature of the national. Taxpayer money made possible the mergers of Merrill Lynch into Bank of America and National City into PNC Bank, among others. Citigroup was sick enough to need a second helping, and, without taxpayers, Wells Fargo would not be "well-capitalized."

The Obama administration is preparing to deploy the second half of the $700 billion rescue plan. Treasury Secretary Timothy F. Geithner is expected to detail those plans in a speech early next week.

Members of Congress from both parties and several agencies appointed to oversee the program have argued that the government should force increased lending, in part by tracking how banks use the money they get.

Rep. Barney Frank (D-Mass.) said on ABC's "This Week" on Sunday that he expected the Obama administration to push banks harder to increase lending. He said the initial government bailout should have come with a tighter condition that they do so. Frank, who chairs the House Financial Services Committee, plans to hold hearings on the subject today.

But some banking regulators and administration officials continue to oppose such measures, saying that banks could be forced into risky lending and that the government should not run banks. Regulators have not instructed banks on how to use the money, local executives said.

"They have not given us any guidelines on how the money should be used," said Thomas Bevivino, chief financial officer at Severn Bancorp. The Maryland company got $25 million from the government, then raised an additional $7.5 million from investors to further bolster its capital reserves. The company said its lending has remained basically flat.

The Capital Purchase Program was announced in October after then-Treasury Secretary Henry M. Paulson Jr. forced nine of the nation's largest banks to accept $125 billion in capital. Paulson said that the rest of the nation's 8,300 banks could apply for a portion of the remaining $125 billion. More than 300 have since received investments.

From the start, Treasury officials took pains to describe the program as focused on "healthy, viable banks" and to proclaim the stated purpose repeatedly: "Increasing the flow of financing available to small businesses and consumers."

Even during a recession, local banks say that loan demand remains strong. And deposits are flowing into the banking system, a pattern that financial analysts attribute to a flight from riskier investments. Federal Reserve data show that deposits in U.S. banks rose strongly in the fourth quarter.

But in the Washington area, the banks that got federal investments mostly were not those that reaped the deposits.

The deposits flowed disproportionately to the strongest banks and the weakest. The strongest banks, which tended not to apply for government money, attracted customers seeking safety, and customers seeking loans, by demanding that borrowers also become depositors. The weakest banks attracted customers by offering eye-catching interest rates. National companies called deposit brokers funnel money to the banks that offer the highest rates, and executives say competition in recent months has been fierce.

"It's a war out there right now," said W. Moorhead Vermilye, chief executive of Shore Bancshares in Easton, Md., which expanded its deposits by less than 1 percent. "It's very, very difficult, but what we're doing is insisting that borrowers bring all their deposits to the bank. If you're going to bank with us, you need to bank with us."

Companies such as EagleBank were caught in between, neither strong nor weak enough. The bank held about $1.1 billion in deposits at the end of September and slightly less at the end of December. About a third of banks nationwide that received a government investment in the fourth quarter also reported a decline in deposits.

Paul, EagleBank's chairman, said he regularly hears from board members who know someone who wants a loan. Increasingly, the conversations don't end productively. The supplicants facing the longest odds are residential and commercial developers and landlords, bank executives said.

Debbie Shumaker, EagleBank's director of business development, said the bank's sales force keeps lists of clients they can't help right now. They send keep-in-touch notes and plan to circle back once the bank has more money to lend. But she acknowledged that it's hard to build a relationship from a rejection.

"It's very frustrating," Shumaker said. "Someday banks are going to go back to these clients, and they're not going to forget these hard days."

Richmond Times-Dispatch

Richmond banks aided by feds show only modest increases in loans

By DAVID RESS Published: March 1, 2009

Billions of dollars flooded into banks' coffers as the credit crunch gripped the U.S. economy last year, but only a fraction of that stimulus money is going back into the community as loans, regulatory records show.

Richmond-area banks that received taxpayer money meant to kickstart lending show only modest increases in loans on their books, a Richmond Times-Dispatch review of hundreds of pages of filings found.

Filings with the Federal Financial Institutions Examination Council and the U.S. Treasury covering last year's fourth quarter also showed:

- The amount of new loans made was less than a quarter of the billions of dollars of new deposits banks received, as jittery consumers pulled funds out of the stock market and placed them in banks for safety.
- New loans generally were less than the amount of taxpayer money, when those sums were intended to fuel many times more loans.
- Loan totals generally rose far less than banks' holdings of securities -- even themortgage-backed securities that were at the center of last year's financial mess.
- Area banks' loans to executives and directors generally rose faster than consumer loans and mortgages. "What the federal government was trying was to get loan money into the economy," said John F. Boschen, an economics professor at the College of William and Mary.

"But the banks had a lot of bad loans; they couldn't employ a dollar of equity and get a dollar of lending because they were concerned about bad loans."

And nobody really sees a bottom yet.

"When we go into recession, banks are always more cautious in their lending, so lending gets tighter," said Christine Chmura, chief economist and president of Richmond-based Chmura Economics and Analytics.

So credit available -- such as total home-equity lines or borrowing limits on credit credits -- shrank, even among banks that received federal money, the Times-Dispatch review found.

. . .

Consumer and commercial loans grew at some and shrank at others, as banks preferred to park their money by buying bonds and other securities, the review found.

Big banks received the first injections of funds, and they reported a decline in mortgage loans outstanding. But smaller, Richmond-area-based banks that got federal money very late in the quarter remained active mortgage lenders, the review found.

Loans to executives and directors, however, increased an average of 6 percent, or by $69 million during the quarter, the Times-Dispatch review found. While the loans account for a tiny portion of banks' totals, federal regulators require that the amount be reported. The banks do not disclose who borrowed or on what terms they did on these regulatory reports.

"We're in a fairly deep recession," said C. Barry Pfitzner, an economist at Randolph-Macon College. "Banks are, and should be, more circumspect in loan approvals on any type of loan."

Net purchases of securities -- mainly bonds -- which are seen as safer than lending grew the most. Mortgage-backed and asset-backed securities, bonds that are repaid with payments from pools of mortgages or consumer loans, rose. Some of these type of securities proved troublesome to many banks last year because they contained so-called "toxic" loans.

"If they're purchasing new MBS, I only hope they've done their homework," Pfitzner said.

Capital One Chairman and Chief Executive Officer Rich D. Fairbank said last month that he saw "compelling investment opportunities" in mortgageand asset-backed securities because of the wide gap between what they are paying and what other alternatives yield.

SunTrust spokesman Michael McCoy said SunTrust believes its purchase of $5.4 billion of mortgage-based securities during the quarter is helping lower mortgage rates, while the bank has expanded its efforts to help borrowers avoid foreclosure.

. . .

While banks are cautious these days, businesses are too.

They're cutting back where they can and that means their need to borrow is down, Chmura said, pointing to the drop of more than 2 percent in business and software sales nationwide during the last three months as a key example.

"It's a chicken-and-egg thing," Chmura said. "It's a recession, so banks are cautious; it's a recession, and businesses don't want to borrow. Which comes first?"

In its first report on how banks used their federal money, the U.S. Treasury blamed the slow economy for what it called a modest decline in lending. The report, released in mid-February, focused on the biggest recipients of the federal aid.

In the Richmond area, one of the smaller recipients, Union Bank & Trust, which got its federal money just two weeks before the quarter's end, posted the biggest increase in lending. Its parent, Union Bankshares, received $59 million in federal money.

"We're working hard to get money out onto the street," said bank President John C. Neal.

He said lending rose in January from its December and November levels, with mortgage loans up about 25 percent, to reach $50 million.

It's not easy to drum up demand, and the new capital doesn't give a license to loosen lending standards, he said.

But it does allow the bank to be a little more flexible -- for instance, by exploring whether a five-year loan rather than a three-year loan might allow someone to qualify who otherwise wouldn't.

The federal money comes with a price, however. Banks must pay a 5 percent annual dividend back to Washington for the use of taxpayer money.

"We make a lot of loans at the prime rate, that's 3.25 percent, and I've got to get that money out there working," Neal said.

He said, roughly speaking, a dollar of capital translates to being able to lend four dollars.

Neal said the biggest demand for loans he's seeing is for mortgages -- but much of that is people moving to take advantage of low rates by refinancing existing debt.

Randolph-Macon's Pfitzner thinks it will take some time before lending rises, in part because demand is soft and in part because banking needs to stabilize. He thinks the need for general stability makes the capital infusions a good idea.

"You see households trying to get their balance sheets in better shape, by paying down credit cards or refinancing mortgages and what's going on at banks is the same thing, said William and Mary's Boschen.

"They're trying to get their balance sheets in order,"

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