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Business Week

August 11, 2003**SECTION:** PEOPLE; Executive Suite; Number 3845; Pg. 48**LENGTH:** 1638 words**HEADLINE:** IS THIS **BANKER TOO BRAZEN?****BYLINE:** By Amy Barrett in Cherry Hill, N.J.**HIGHLIGHT:**

Commerce Bancorp's Vernon Hill has led a rapid expansion, but his style is raising a few eyebrows

BODY:

If there's one thing to know about how Vernon W. Hill II, the founder, chairman, and president of fast-growing Commerce Bancorp Inc., does business, it's this: He gives his managers \$ 5,000 if they shut down a rival branch. It also can't hurt to know that he calls his competitors' practices "stupid" and their brands "rotten." Or that even the mere mention of another bank often elicits a response. When a woman at a July meeting for new Commerce executives tells Hill that she used to work at First Union Corp., he replies with a snicker: "Or F.U., as we call it around here."

It pretty much goes without saying that Hill's confrontational manner does not exactly endear him to other bankers. And that's putting it mildly. "Vernon likes rubbing his competitors' noses in Commerce's success," says Thomas K. Brown, chief executive officer of Second Curve Capital, a hedge fund that holds Commerce shares. Hill puts it this way: "I don't get invited to a lot of banking conventions."

What makes the 57-year-old Hill so sure of himself is that he has actually built a bank with \$ 20 billion in deposits from scratch. He was only 27 when he opened the first branch in New Jersey in 1973. After working for years to make a name for himself there, as well as in Pennsylvania and Delaware, Hill has deemed the bank ready to venture into the crowded New York market. In the past two years, Commerce has opened 27 branches in New York City and Long Island, nearly half in Manhattan. In all, the bank now has 245 branches, 95 of which didn't exist in 1999 and most of which were financed through a debt offering and the company's own earnings. By the end of 2007, Hill expects to move north to Boston or south to Washington, creating a network of more than 500 branches with \$ 50 billion in assets. Commerce's recent rapid growth has so far had the desired effect: Between 1998 and 2002, the bank's net income has grown an average of 31% annually to \$ 145 million. This year, the bank's deposits increased 44% in the second quarter, compared with last year. And since the beginning of 1998, Commerce's stock has risen 130%.

What makes Hill so disdainful of other bankers is what he says is their stubborn belief in the status quo. For the past decade, Hill has willfully ignored the conventions of the banking world. He throws block parties when he opens a new branch and hosts lunchtime or weekend concerts at many of them. He keeps branches open until 8 p.m. during the week and has Saturday and Sunday hours, too; every branch has a coin-counting machine that anybody can use. Drive-through tellers hand out dog biscuits to customers who travel with their pooches. In short, Hill has brought some retail smarts to retail banking.

No doubt about it, Hill relishes his role as the banking industry's cheekiest maverick. He's less thrilled about his reputation as one of the most controversial banking executives around. That's because the rep is for all the wrong

reasons. While no one argues the bank isn't sound, analysts and critics are starting to ask questions about the risks of Commerce's aggressive expansion, about some personal business deals between Hill's family and the bank, and about Commerce's political influence in its home state.

Hill was just a few years out of the University of Pennsylvania's Wharton School, where he received a B.A. in economics, when he persuaded a group of local New Jersey businesspeople to put up \$ 1.5 million to start Commerce. Hill, who grew up in Virginia, had helped put himself through college working in a New Jersey bank. But he was absolutely uninterested in signing on with one of the giants. "It was obvious I wasn't going to get rich working for a bank," he says. And that has always seemed to be the point. When Hill started Commerce, he already had a real estate site location business going; in the mid-1980s he decided to invest in dozens of Burger Kings. Today, he still has stakes in both those enterprises, and he and his family own about 5% of Commerce's shares, which are worth some \$ 140 million, according to the company's 2002 proxy.

Despite the bank's rapid expansion, Hill still controls almost every facet of its operations. Commerce opens some 40 new branches a year, and Hill personally approves each location. When the bank reviews a loan of more than \$ 7.5 million (and it considers about five a week), it's Hill who looks it over. He behaves as if every issue is urgent: His e-mails are written IN ALL CAPS. For Hill, Commerce is not just a business, it's a way of life. "You are all cult members," he tells his executives. "And if you can't buy in, this isn't the place for you."

But for all his talk, and for that matter all his accomplishments, analysts and critics are asking if Commerce is heading for trouble. Among the chief concerns is the bank's investment portfolio, which now makes up more than half of its assets. Because Commerce's deposits have grown more quickly than it could loan the money out, it has invested the cash, mostly in mortgage-backed securities. If interest rates rise, which is highly possible in the next year or so, the value of Commerce's portfolio would fall. That in turn could erode the bank's capital levels and its ability to continue expanding, warns Keefe, Bruyette & Woods Inc. analyst Thomas J. Monaco.

At the same time, there are concerns about Hill's strategy of growth at any cost. Commerce's so-called efficiency ratio, which measures how much a bank spends to generate \$ 1 in revenue, is 70.7%, according to Robert J. Lacoursiere, an analyst at Lehman Brothers Inc. The industry average is far leaner, at about 50%. And Commerce's return on assets is less than 1%, well below that of other banks. "His growth is not as profitable as that of his peers," says Lacoursiere. As such concerns have spread, the stock has lost about 8% of its value this year.

Hill gives such critics about a minute of his time. He acknowledges the bank's return on assets is lower than its competitors', but argues that return on equity is a better measure of performance -- and there, Lacoursiere says, Commerce is in line with the rest of the industry. As for the large securities portfolio, Hill says a rise in interest rates would in no way compromise the bank's continued growth. And he believes that it's better to invest the money flowing in from deposits in securities than rush to make loans that could go bad. "We aren't going to compromise credit quality," he says.

Commerce's potential business pitfalls aren't the only issues dogging Hill. The cozy ties among him, the company, and its board are also coming under scrutiny. The bank has built 17 New Jersey branches on land it leases from Hill's family trust or limited partnerships in which he has an interest, paying \$ 1.1 million in rent in 2002. Commerce also paid \$ 451,000 last year to use facilities at Galloway National Golf Club, a private golf course outside Atlantic City in which Hill is a principal investor. In addition, a design firm owned by Hill's wife, Shirley, received \$ 8.1 million last year for architectural design and project management services provided to the bank. And one son, Vernon Hill III, is a real estate broker whose firm does business with Commerce. Hill says that relationship doesn't have to be disclosed because his son is not paid by the bank. In fact, excluding Hill himself, 8 of the board's 11 directors are either insiders or individuals who now have or have had some sort of business relationship (either directly or through their firms) with Commerce or its top executives. "For public companies these days, these types of relationships raise eyebrows," says Charles M. Elson, director of the Weinberg Center for Corporate Governance at the University of Delaware.

Critics also contend that Commerce's political ties and generous contributions in New Jersey have helped the bank nab lucrative municipal underwriting business. Hill says all Commerce's political activities have been proper. But he announced earlier this year that the bank would halt all political action committee contributions in New Jersey until the rules become clearer.

Hill also says that last summer he decided he would no longer engage in any new real estate deals with the bank. And Commerce has now cut back on the business it does with his wife, but won't stop altogether because "she does an unbelievable job." The bank will continue to use the golf course because it's a "great" place to entertain guests. As for the board, Hill says, "they have produced unbelievable shareholder returns." He argues that a majority of the directors are independent under New York Stock Exchange rules, but says the board will "evolve." Jack R. Bershad, a director, says they are discussing bringing new people in.

In the meantime, Hill is enjoying his success. Last fall, he and his wife moved into a nearly 46,000-square-foot mansion they built near Commerce's headquarters in Cherry Hill, N.J. The estate, called Villa Collina, boasts some

eight reflecting pools on the grounds. And, maybe best of all, it gives Hill something else to rub his competitors' noses in.

RESUME: Vernon W. Hill II

BORN

Aug. 18, 1945, San Francisco.

EDUCATION

B.A., economics, University of Pennsylvania's Wharton School, 1967.

CURRENT POSITION

Runs \$20 billion Commerce Bancorp, which he founded at age 27.

CREDO

'We deliver [service] the way the great retailers deliver, not the way the stupid banks deliver.'

PUBLICITY STUNT

Got golfing buddy Donald Trump to make a \$5 million deposit at the bank's first NYC branch.

FAMILY

Married to his second wife, Shirley, for 30 years; four kids from both marriages.

URL: <http://www.businessweek.com/index.html>

GRAPHIC: Photograph: CHAIRMAN AND PRESIDENT HILL AT A COMMERCE BRANCH IN CHERRY HILL, N.J.
PHOTOGRAPH BY PETER MURPHY

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