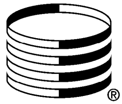

IOWA BANKERS ASSOCIATION
8800 NW 62nd Avenue
PO Box 6200
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December 16, 2008 Via electronic delivery

Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, DC 20429
Comments@FDIC.gov

Re: **FDIC** (RIN 3064-AD35); **Assessments – Establishment of FDIC Restoration Plan – Proposed Rule**; 73 Federal Register 61560; October 16, 2008.

Dear Mr. Feldman:

The Iowa Bankers Association (IBA) appreciates the opportunity to comment on the proposal of the Federal Deposit Insurance Corporation (FDIC) to raise premium assessment rates for 2009 in order to recapitalize the insurance fund and to change the risk-based premiums classification system. The Iowa Bankers Association (IBA) is the largest trade association representing the banking industry in Iowa, with roughly 400 members statewide. This represents approximately 94% of the banks and thrifts located in the state of Iowa.

The IBA realizes a strong FDIC insurance fund is important to maintaining depositor confidence and the IBA supports changes to the premium calculation that truly reflect the risk of loss to the FDIC. Due to the current economic climate, the industry expects that the assessment schedule will rise in the short run to pay for bank failures, provide reserves in the future, and rebuild the fund's reserve ratio. Our main points on the proposal, categorized in separate headings are as follows:

- **General comments regarding the proposed increases in assessment rates.**

- **Comments related to categorization of Certificate of Deposit Account Registry Service (CDARS) deposits.**

- **Comments regarding risk-based assessments beginning in the second quarter of 2009.**

General Comments Regarding the Proposed Increases in Assessment Rates.

The proposal would significantly raise premium assessments to aggressively recapitalize the insurance fund in five years to over 1.25 percent of insured deposits. Yet the Federal Deposit Insurance Reform Act requires the FDIC to rebuild the fund to 1.15 percent in five years and to take longer when there are "extraordinary circumstances." There is no question that these are extraordinary circumstances, and Congress has also given the FDIC flexibility to take into account economic conditions affecting depository institutions when setting rates. Therefore the IBA feels the FDIC plan for proposed rate hikes are too high in the early stages and does not strike the proper balance between rebuilding the fund and assuring credit is readily available in banks' communities – as excessively high premiums reduces the resources Iowa banks will have to lend in their local communities. It is also counter to other efforts by Congress and the Treasury to stimulate lending.

The proposed average premium assessment increase represents a very large increase – more than doubling current premiums. This will have a significant negative impact on bank earnings and will adversely affect the ability of healthy banks to make loans in their communities. Paying excess in premiums seems to counteract the goal of the TARP program that provides extra capital for healthy banks to encourage greater lending.

Thus, rather than more than doubling premiums as proposed, it would be more reasonable to raise the assessment schedule by two to three basis points over a six to seven year period (7-9 basis points or 8-10 basis points for the strongest, Category I rated banks). Raising rates by two or three basis points, instead of the proposed seven basis points, will keep $6 ½ billion in banks nationwide which could support up to $45 billion in lending.

At the very least, the FDIC should consider phasing in increases in the assessment schedule, given the current economic recession and forecast for next year. Such a phase-in would also be consistent with proposals for rates under a revised risk-based assessment formula for the second quarter of 2009 and beyond. Furthermore, the IBA recommends the FDIC recapitalization plan should require premiums to be adjusted downward should the reserve ratio rise faster than expected under the plan. Correspondingly, the recapitalization plan can flexibly raise rates should there be greater losses than expected and the rebuilding pace slower than expected. This flexibility should support a more limited increase in rates since the FDIC can make adjustments later as needed.

Comments Related to Categorization of Certificate of Deposit Account Registry Service (CDARS) Deposits.

With nearly 100 IBA member banks who offer the Certificate of Deposit Account Registry Service (CDARS) reciprocal deposits to their customers, the IBA believes that the FDIC proposal should remove the Certificate of Deposit Account Registry Service (CDARS) from inclusion in the brokered deposits ratio – as these institutions rely on CDARS deposits as a stable source of core funding.

CDARS reciprocal is a deposit placement service that allows banks to place customers' funds in FDIC-insured certificates of deposits at other banks and, at the same time, receive an equal sum of funds from the customers of other banks in the CDARS Network.

Many IBA members have expressed deep concern regarding how CDARS reciprocal deposits would be treated under the deposit insurance assessment proposal. This is a very important issue for them, as well as for the industry as a whole. After analyzing the proposal, the IBA has concluded that CDARS reciprocal deposits should not be included in the FDIC's definition of a "brokered deposit" for purposes of the Notice's assessment rule.

Were the proposal to go into effect as written, CDARS reciprocal CDs would be treated as brokered deposits and would be subject to surcharges under certain conditions. The FDIC's justification for an additional premium for brokered deposits states: "Significant reliance on brokered deposits tends to increase an institution's risk profile, particularly as the institution's financial condition weakens."

The key question, then, is whether the use of CDARS reciprocal does in fact increase an institution's risk profile.

CDARS reciprocal deposits share three characteristics that define core deposits. One, CDARS CDs have a high reinvestment rate. This year, the average reinvestment rate for CDARS deposits across the network has exceeded 83 percent. Two, CDARS deposits are overwhelmingly gathered within a bank's geographic footprint through established customer relationships. Eighty percent of CDARS placements are made by customers within 25 miles of a branch location of the relationship institution. Three, banks set their own rates on CDARS deposits, rates that reflect a bank's funding needs and local market. As a result, depending on maturity, CDARS deposits are gathered at a significant discount to the cost of traditional brokered deposits.

Because CDARS deposits are built on established local customer relationships, demonstrate a high degree of "stickiness" and are insulated from the rate volatility in the national certificate of deposit market, they are the functional equivalent of a core deposit, the most stable form of deposit, and do not increase an institution's risk profile beyond what any core deposit would.

Therefore, a broad-brush approach to defining CDARS reciprocal deposits as brokered deposits under the assessment proposal would unfairly penalize banks that offer the service.

It would also unfairly stigmatize the CDARS service. The stated purpose of the proposal is to more accurately match the perceived risk to the deposit insurance fund of certain banking practices with a premium that better reflects that perceived risk. Clearly, the FDIC perceives brokered deposits, at least in some circumstances, to be of greater risk than core deposits, and is thus trying to discourage any significant reliance on brokered deposits. Bankers, of course, understand the FDIC's intent. By defining CDARS

reciprocal deposits as brokered deposits, the proposal would discourage bankers from using the service.

Penalizing and stigmatizing the use of a service like CDARS seems to run contrary to the many efforts by the Administration, Congress and banking agencies to restore stability and liquidity to the financial system. Financial institutions relying on core deposits and the functional equivalent of core deposits such as CDARS reciprocal deposits are in the best position to weather difficulty.

Comments Regarding Risk-Based Assessments Beginning in the Second Quarter of 2009.

Furthermore, the IBA believes the proposal is potentially very punitive to banks using Federal Home Loan Bank advances. FHLB advances are stable source of funding for many banks that is often at lower cost than local deposits. In addition, FHLB advances can be used to match-fund longer term loans, mitigating interest rate risk. This type of funding is not available elsewhere.

FHLB advances serve as a consistent, reliable source of liquidity for many IBA members. The availability of FHLB advances as a means of wholesale funding is especially important to the community banks that represent a large majority of the FHLB Des Moines' 1,200 members. These smaller institutions do not have reliable access to other sources of cost-effective funding and rely on the availability of FHLB advances as a critical tool for managing their balance sheets and implementing their business plans. In fact, in 2007, FHLB Des Moines advances increased 83.2% to over $40 billion, and increased further to over $60 billion during the third quarter of 2008 – indicating the FHLB Des Moines is playing a vital role in alleviating the current shortage of liquidity in the mortgage markets. Penalizing the use of FHLB funding is contrary to the current efforts by the Administration, Congress and the Federal Reserve to restore liquidity and bolster confidence in the financial system.

If the FDIC proceeds with this rulemaking and its new approach to risk-based premiums, then the final rule should treat FHLB advances differently than other forms of secured lending. Advances are more reliable, flexible, and better priced than other sources of funding. As unique providers of secured funding, the FHLBs are cooperatives that serve their member/customers and price advances with very narrow spreads over the FHLBs' cost of funds. In addition, the use of advances serves to strengthen depository institutions since income earned by the FHLBs is largely paid to members in the form of dividends. In 2007, 83% of FHLB Des Moines net income was paid out as dividends; the comparable ratio through the first half of 2008 was 66%. The reduced payout of dividends in 2008 allowed the FHLB Des Moines to strengthen its capital base allowing the Bank to remain a strong partner and source of liquidity for its members.

The FDIC should not inhibit good, stable sources of funding. Rather, the focus should be on the risk of the assets that the bank has funded, regardless of the source of funds and any concerns should be raised as part of the examination process – which is included in

the premium calculation. It is patently unfair to penalize banks that use these stable sources of funding.

If the FDIC contemplates changes to this Proposed Rule, the IBA strongly urges them to thoughtfully consider the above comments. If you have any questions about these comments, please call the undersigned at 800-532-1423.

Sincerely,

Robert L. Hartwig
Legal Counsel