One Mission. Community Banks.

November 20, 2024

Mr. James P. Sheesley
Assistant Executive Secretary
Attention: Comments—RIN 3064-AF99
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

RE: Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions [RIN 3064-AF99]

Dear Mr. Sheesley:

The Community Bankers of Michigan, and on behalf of all banks in the state of Michigan, strongly opposes the FDIC's Notice of Proposed Rulemaking concerning Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions ("the Proposal" or "the Proposed Rule"). Simply stated, there is no need for this proposal as bank regulators already have the appropriate tools and regulatory authority to supervise any potential liquidity risks to individual banks. Bank regulators rate banks under the CAMELS system and the "L" is for liquidity risk. Regulators have all the tools they need today to step in if they see a bank taking excessive liquidity risk. In fact, it has been one of the top areas of regulatory focus for the last two years in bank examinations across the country and in Michigan.

Michigan Banks have done an exceptional job managing liquidity through a period of historically rapid rate increases by the Federal Reserve. The Federal Reserve was woefully late addressing rapid and excessive inflation, calling it "Transitory" even when it was apparent to everyone in the country that it was anything but transitory. The banking industry was whipsawed by flawed government policy on over stimulative spending causing rampant inflation, and by the Federal Reserve rate increases in an effort to catch up on their slow response to excessive inflation.

Banks as a whole did an outstanding job navigating through the various missteps by the federal government that put generational pressure on their balance sheets and liquidity. While the industry has performed admirably and showed incredible resilience – especially Michigan banks – there were a few casualties like Silvergate Bank, Silicon Valley Bank, and First Republic Bank. These banks had high risk business models, poor risk management practices, ineffective management and, one could argue, were not properly supervised. The bad actors have been removed from the banking system and there is no reason to negatively impact the vast majority of the nation's banks who diligently and properly managed risk through a very volatile period in our nation's financial history.

The recommended changes to the current brokered deposit rules are a knee jerk reaction to the failure of less than a handful of poorly run banks who do not reflect the management practices or business

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models of nearly all of our nation's banks. Regulators were guilty of poor management oversight as were the management teams of these banks – their excessive growth, their excessive reliance on uninsured deposits, and their poor risk management practices should have set off alarms long before they faced a crisis. These banks do not in any way resemble the vast majority of our nation's banks. Here in the Midwest, we have outstanding and productive relationships with our bank regulators. We meet regularly to discuss critical issues in the banking industry and discuss key risk areas where our banks should focus. These candid, focused discussions help both our banks, and our regulators, manage risk in the system. We would suggest similar processes be put in place across the country to get regulators and industry leaders focused on jointly managing critical risks. One area that should be the focus of more intense regulatory scrutiny, and it now is, is excessive levels of uninsured deposits at financial institutions. It was this issue that impacted the handful of failed banks with customer withdrawals at lightning speed using modern funds transfer technology that should rightfully be a regulatory area of emphasis and concern. Levels of uninsured deposits are very low at community banks across the country, but they are higher at some of the super-regional banks and both the banks and regulators have addressed the issue and moved these levels lower.

Under the Proposal, more core deposits will be considered brokered deposits. Among the deposits that the FDIC proposes to reclassify as "brokered" are deposits that do not pose "hot money" risks but are stable, sticky, and subject to contractual terms for maturity that protect against deposit flight. As a result, this misguided Proposal will negatively impact every community bank when it comes to preparing Call Report data, calculating FDIC assessments, managing liquidity, and adjusting contingency funding plans. This is especially troubling and frankly, puzzling, because the FDIC has not identified any specific problems with brokered deposits at community banks since the 2020 rule was finalized. Many of these deposits are sourced from investment firms and trusted fintechs the banks have established relationships with so they are known entities.

Banks already have a responsibility to do third party due diligence. This does not only apply to technology partners for banks, it applies to all third-party vendor relationships. Deposit brokers should be evaluated for risk by banks and the process should be reviewed by their regulators, and it is a part of existing regulatory exams. Again, the processes for risk management and mitigation already exist at banks and with their regulators and when properly conducted should address any potential liquidity risk with the deposit brokers. We want to stress again the risk management tools to make sure brokered deposit relationships are properly managed and accounted for already exist within the banks and with the regulatory review process. The FDIC can use the existing tools to limit brokered deposit risk where necessary. They already can restrict the use of brokered deposits at banks that are less than well capitalized.

There are a number of reasons the FDIC should withdraw this Proposal, including that the it will: (1) unnecessarily constrain community bank liquidity and funding sources; (2) penalize and disrupt some third-party relationships that community banks rely on to provide valued online banking and deposit services to their customers; (3) needlessly force community banks to incur additional costs and business disruptions to reapply for primary purpose exceptions ("PPEs") that the agency previously approved, and (4) the FDIC does not have the capacity to approve deposit broker relationships in a timely manner. The FDIC has a poor record in the past four years with regard to responsiveness on any banking approval issues. For example, new bank applications take excessively long periods for review and approval and it is a big reason the number of new bank applications has been so low versus historical levels for the last few years. The same is true on bank merger applications where the FDIC has an abysmal track record – painfully slow responsiveness to applications and always the last regulatory agency to get around to

making a decision on a deal. They are often months behind approvals by other regulatory agencies. It begs the question, why should bankers or the country have any faith that the FDIC could get through a new approval process for all currently approved third parties on brokered deposits in a timely manner?

The proposal as currently written would require all brokered deposit arrangements to be preapproved by the FDIC and they have provided no plan and no demonstrated capability to handle this in a timely and efficient manner. This has the potential to be another government debacle as badly needed liquidity would be taken out of the banking system and could not be replaced until the approval process took place, which might take years. This provision must be struck even if the FDIC moves forward with the proposed brokered deposit rules. Previously approved deposit broker arrangements must be grandfathered for 1-2 years to allow for a reasonable approval process to take place.

The FDIC is also proposing transferring the burden of getting an approval to the banks versus the third-party vendors who can get approvals now. This is a totally inefficient process and puts undue burden on banks, especially community banks, who face way too much regulatory burden already. Third party vendors that work with multiple banks in different regions of the country should be able to get all of their relationships approved at one time, making it a much more efficient and appropriate process for the whole system.

Michigan community banks use brokered deposits as one of several diverse sources of liquidity. The overwhelming majority of community banks do not have high concentrations of brokered deposits or rely on brokered deposits for rapid growth. The median level of brokered deposits for Michigan banks is .15% and the average is 5.55%. There are less than a handful of banks that have any significant level of brokered deposits in our state and they are very well run, well managed banks with unique business models tied to the residential mortgage or commercial finance business. When managed prudently, brokered deposits are an important funding source for community banks to meet the borrowing needs of their communities. For example, brokered deposits help community banks manage seasonal agricultural lending needs, or short term, often cyclical, instances when loan demand exceeds the ability to generate new core deposits. But requiring community banks to reclassify higher percentages of core deposits as brokered imposes serious costs and restrictions on community banks, including higher deposit insurance premiums, possibly lower CAMELS ratings, and additional regulatory scrutiny. More concerning, these reclassifications and restrictions on brokered deposits can operate in tandem to constrain community banks' access to liquidity when they need it most. Community banks should not be forced to reclassify core deposits as brokered – doing so may have the unintended consequences of forcing community banks to shed stable deposits to reduce brokered deposits exposure, thus reducing access to necessary and stable liquidity sources. This takes liquidity out of the banking system and constrains lending in local communities.

In summary, the federal government has had a flawed record on the policy front for the last four years and there is no need to make another flagrant policy miscalculation by changing the current rules on brokered deposits – regulators should not make another unforced error. The proposed changes to the brokered deposit statutes are not necessary and will have negative consequences for our nation's economy and its banking system. Any deposit restrictions that take money out of the banking system by definition restricts lending as banks will lose a stable source of funds for loans. Our nation faces a critical shortage of low to moderate income housing and taking money out of the banking system removes critical funding that can be used to help fix our severe housing shortages. The banking industry in Michigan and across the country is focused on doing its part to help our state and our nation fix the critical shortage of affordable housing. This should be the nations and our regulators' priority too so we

all work together to address this critical need in our state and our nation. Removing any sources of liquidity, which is the funding for loans, is not in the public's interest and does not align with our nation's current priorities. The attack on the Federal Home Loan Bank System and the liquidity it provides for lending and the proposed changes to the brokered deposit rules do not align with our national priority to help fix the housing crisis that so many American families and individuals are dealing with today. We respectfully ask that this proposal be withdrawn.

Sincerely,

James R. North
President and CEO