



June 19, 2020

**MEMORANDUM TO:** The Board of Directors

**FROM:**

Diane Ellis  
Director, Division of Insurance and Research

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DIANE ELLIS  
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**SUBJECT:**

Final Rule Re: Mitigating the Deposit Insurance Assessment Effect of Participation in the Paycheck Protection Program (PPP), the PPP Liquidity Facility, and the Money Market Mutual Fund Liquidity Facility

## SUMMARY

Staff are presenting for the approval of the Federal Deposit Insurance Corporation (FDIC) Board of Directors (the Board) a request to publish the attached final rule that mitigates the deposit insurance assessment effects of participating in the Paycheck Protection Program (PPP) established by the Small Business Administration (SBA), and the Paycheck Protection Program Liquidity Facility (PPPLF), and Money Market Mutual Fund Liquidity Facility (MMLF) established by the Board of Governors of the Federal Reserve System (Board of Governors).

The final rule: 1) removes the effect of participation in the PPP and borrowings under the PPPLF on various risk measures used to calculate an insured depository institution's (IDI) assessment rate, 2) removes the effect of participation in the PPP and MMLF on certain adjustments to an IDI's assessment rate, 3) provides an offset to an IDI's assessment for the increase to its assessment base attributable to participation in the PPP and MMLF, and 4) removes the effect of participation in the PPP and MMLF when classifying IDIs as small, large, or highly complex for assessment purposes.

## RECOMMENDATION

FDIC staff request that the FDIC Board approve this final rule and authorize its publication in the *Federal Register*. The final rule would take effect immediately upon publication in the *Federal Register*, with an application date of April 1, 2020, to enable the FDIC to provide the relief contemplated in this rulemaking as soon as practicable, starting with the second quarter of 2020, and to provide certainty to IDIs regarding the assessment effects of

**Concur:**

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participating in the PPP, PPPLF, or MMLF for the second quarter of 2020, which is the first assessment quarter in which the assessments will be affected.

## **BACKGROUND**

On March 18, 2020, the Board of Governors, with the approval of the Secretary of the Treasury, authorized the Federal Reserve Bank of Boston (FRBB) to establish the MMLF, pursuant to section 13(3) of the Federal Reserve Act.<sup>1</sup> Under the MMLF, the FRBB is extending non-recourse loans to eligible borrowers to purchase assets from money market mutual funds (MMFs). Assets purchased from MMFs are posted as collateral to the FRBB. Eligible borrowers under the MMLF include IDIs. Eligible collateral under the MMLF includes U.S. Treasuries and fully guaranteed agency securities, securities issued by government-sponsored enterprises, and certain types of commercial paper. The MMLF is scheduled to terminate on September 30, 2020, unless extended by the Board of Governors.

As part of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) and in recognition of the exigent circumstances faced by small businesses, Congress created the PPP.<sup>2</sup> PPP loans are fully guaranteed as to principal and accrued interest by the Small Business Administration (SBA), the amount of each being determined at the time the guarantee is exercised.<sup>3</sup>

In order to provide liquidity to small business lenders and the broader credit markets, and to help stabilize the financial system, on April 8, 2020, the Board of Governors, with approval of the Secretary of the Treasury, authorized each of the Federal Reserve Banks to extend credit under the PPPLF, pursuant to section 13(3) of the Federal Reserve Act.<sup>4</sup> Under the PPPLF, Federal Reserve Banks are extending non-recourse loans to institutions that are eligible to make PPP loans, including IDIs. Under the PPPLF, only PPP loans that are guaranteed by the SBA with respect to both principal and interest and that are originated by an eligible institution may be pledged as collateral to the Federal Reserve Banks (loans pledged to the PPPLF).

Pursuant to Section 7 of the Federal Deposit Insurance Act (FDI Act), the FDIC has established a risk-based assessment system through which it charges all IDIs an assessment amount for deposit insurance.<sup>5</sup> Under the FDIC's regulations, an IDI's assessment is equal to its assessment base multiplied by its risk-based assessment rate.<sup>6</sup> An IDI's assessment base and assessment rate are determined each quarter based on supervisory ratings and information

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<sup>1</sup> 12 U.S.C. 343(3).

<sup>2</sup> Pub. L. 116-136 (Mar. 27, 2020).

<sup>3</sup> On June 5, 2020, the President signed into law the Paycheck Protection Program Flexibility Act of 2020 (PPP Flexibility Act), Pub. L. 116-142, which amends key provisions of the CARES Act, including provisions related to loan maturity, deferral of loan payments, and loan forgiveness.

<sup>4</sup> 12 U.S.C. 343(3). On April 30, 2020, the facility was renamed the Paycheck Protection Program Liquidity Facility, from Paycheck Protection Program Lending Facility. *See* Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act May 15, 2020, Board of Governors of the Federal Reserve System, available at: <https://www.federalreserve.gov/publications/files/mlf-msnlf-mself-and-ppplf-5-15-20.pdf>.

<sup>5</sup> *See* 12 U.S.C. 1817(b).

<sup>6</sup> *See* 12 CFR 327.3(b)(1).

collected on the Consolidated Reports of Condition and Income (Call Report) or the Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks (FFIEC 002), as appropriate. Generally, an IDI's assessment base equals its average consolidated total assets minus its average tangible equity.<sup>7</sup> An IDI's assessment rate is calculated using different methods based on whether the IDI is a small, large, or highly complex institution.<sup>8</sup> All institutions are subject to adjustments to their assessment rates for certain liabilities that can increase or reduce loss to the DIF in the event the bank fails.<sup>9</sup>

Absent a change to the assessment rules, an IDI that participates in the PPP, PPPLF, or MMLF programs could be subject to increased deposit insurance assessments. For example, an institution that holds PPP loans, including loans pledged to the PPPLF, would increase its total loan portfolio, all else equal, which may increase its assessment rate. An IDI that receives funding under the PPPLF would increase the total assets on its balance sheet (equal to the amount of PPP loans pledged to the Federal Reserve Banks), and increase its total liabilities by the same amount, which would increase the IDI's assessment base and also may increase its assessment rate. An IDI that obtains additional funding, such as additional deposits or secured borrowings, to make PPP loans would increase its total liabilities and total assets by that amount of funding, which would increase its assessment base and also may increase its assessment rate. An IDI that relies on existing funding, including deposits already at the institution, to make PPP loans would not increase its total liabilities or total assets, which would not increase its assessment base.

## **THE PROPOSED RULE**

On May 20, 2020, the FDIC published in the *Federal Register* a notice of proposed rulemaking (the proposed rule, or proposal)<sup>10</sup> that would mitigate the deposit insurance assessment effects of an IDI's participation in the PPP, PPPLF, and MMLF programs. To remove the effect of these programs on various risk measures used to determine the deposit insurance assessment rate for each IDI, the FDIC proposed to exclude PPP loans, which include loans pledged to the PPPLF, from an institution's loan portfolio; exclude loans pledged to the PPPLF from an institution's total assets; and, for institutions subject to the large or highly complex bank scorecard, exclude amounts borrowed from the Federal Reserve Banks under the PPPLF from an institution's liabilities. In addition, because participation in the PPPLF and MMLF programs will have the effect of expanding an IDI's balance sheet (and, by extension, its assessment base), the FDIC proposed to exclude loans pledged to the PPPLF and assets purchased under the MMLF in the calculation of certain adjustments to an IDI's assessment rate, and to provide an offset to an IDI's total assessment amount for the increase to its assessment base attributable to participation in the PPPLF and MMLF. Finally, in classifying IDIs as small,

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<sup>7</sup> See 12 CFR 327.5.

<sup>8</sup> For assessment purposes, a small institution is generally defined as an institution with less than \$10 billion in total assets, a large institution is generally defined as an institution with \$10 billion or more in total assets, and a highly complex institution is generally defined as an institution that has \$50 billion or more in total assets and is controlled by a parent holding company that has \$500 billion or more in total assets, or is a processing bank or trust company. See generally 12 CFR 327.8.

<sup>9</sup> See 12 CFR 327.16(e).

<sup>10</sup> 85 FR 30649 (May 20, 2020).

large, or highly complex for assessment purposes, the FDIC proposed to exclude from an IDI's total assets the amount of loans pledged to the PPPLF and assets purchased under the MMLF.

In response to the proposal, the FDIC received 41 comment letters from depository institutions, depository institution holding companies, trade associations, and other interested parties.<sup>11</sup> Commenters generally supported the FDIC's efforts to mitigate the deposit insurance effects of an IDI's participation in the PPP, PPPLF, and MMLF programs, but expressed concerns with certain aspects of the proposal. Most commenters stated that the proposed modifications would not completely offset the PPP lending on assessments and requested that the FDIC exclude all PPP loans in determining an IDI's deposit insurance assessment.

## **DISCUSSION OF THE FINAL RULE**

### **Summary**

Staff recommends that the FDIC Board, under its general rulemaking authority in Section 9 of the FDI Act,<sup>12</sup> and its specific authority under Section 7 of the FDI Act to establish a risk-based assessment system and set assessments, adopt this final rule to mitigate the deposit insurance assessment effects of participating in the PPP, PPPLF, and MMLF.

Under the final rule, staff recommends that the FDIC (1) remove the effect of participation in the PPP and borrowings under the PPPLF on various risk measures used to calculate an IDI's assessment rate, (2) remove the effect of participation in the PPP and MMLF program on certain adjustments to an IDI's assessment rate, (3) provide an offset to an IDI's assessment for the increase to its assessment base attributable to participation in the PPP and MMLF; (4) and remove the effect of participation in the PPP and MMLF when classifying insured depository institutions as small, large, or highly complex for assessment purposes.

#### **1. Exclusion of All PPP Loans**

Most of the comments the FDIC received in response to the proposed rule stated that the proposed modifications would not completely offset the impact of PPP lending on assessments. Many of these commenters requested that the FDIC exclude all PPP loans, whether funded under the PPPLF or through other sources of liquidity, including deposits or Federal Home Loan Bank (FHLB) advances, from the calculation of an IDI's assessment rate, assessment base, or both, so that the bank's assessment would be mitigated accordingly, rather than excluding only loans pledged to the PPPLF.

After considering comments received, and in recognition of the important role IDIs play in providing liquidity to small businesses and helping to stabilize the broader economy in the midst of the economic disruption caused by COVID-19, as well as in recognition that some banks have funded PPP loans through liabilities other than borrowings under the PPPLF, staff recommends that the FDIC exclude the quarter-end outstanding balance of all PPP loans from an

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<sup>11</sup> See comments on the proposal, available at <https://www.fdic.gov/regulations/laws/federal/2020/2020-assessments-ppp-3064-af53.html>.

<sup>12</sup> See 12 U.S.C. 1817, 1819 (Tenth).

IDI's total assets in calculating an IDI's assessment rate and the offset to an IDI's assessment amount due to the inclusion of PPP loans in its assessment base.

As described below, the final rule excludes the quarter-end outstanding balance of all PPP loans from an IDI's total assets in the applicable risk measures used to determine an IDI's assessment rate. In addition, because participation in the MMLF program will have the effect of expanding an IDI's balance sheet and because PPP lending funded by additional liabilities could have the effect of expanding an IDI's balance sheet (and, by extension, its assessment base), under the final rule the FDIC will provide an offset to an IDI's total assessment amount for the increase to its assessment base attributable to PPP lending and participation in the MMLF. The offset will be calculated by summing an IDI's quarter-end outstanding balance of PPP loans and the quarterly average amount of assets purchased under the MMLF. The FDIC also will exclude the outstanding balance of PPP loans and assets purchased under the MMLF in the calculation of certain adjustments to an IDI's assessment rate.

Moreover, in classifying IDIs as small, large, or highly complex for assessment purposes, under the final rule the FDIC also will exclude from an IDI's total assets the outstanding balance of PPP loans and assets purchased under the MMLF.

To minimize additional reporting burden, and in consideration of comments requesting that the FDIC exclude the quarter-end balance of outstanding PPP loans, staff recommends that under the final rule the FDIC exclude the quarter-end outstanding balance of PPP loans in mitigating the effect of PPP participation on an IDI's deposit insurance assessment, both for risk measures that are calculated using amounts reported as of quarter-end and for calculations that use amounts reported on an average basis.

## 2. Tier 1 Leverage Ratio

Some commenters also suggested that the leverage ratio, as applied in the calculation of an IDI's assessment rate, should be reduced by the quarter-end outstanding balances of all PPP loans. In accordance with the agencies' April 13, 2020, regulatory capital interim final rule, banking organizations are required to neutralize the regulatory capital effects of assets pledged to the PPPLF on leverage capital ratios.<sup>13</sup> This requirement is due to the non-recourse nature of the Federal Reserve's extension of credit to the banking organization, a protection that does not exist if the banking organization funds PPP loans using other sources of liquidity.

To remain consistent with the regulatory capital interim final rule, and consistent with the proposed rule, staff recommends that the FDIC not modify its deposit insurance assessment pricing system with respect to the Tier 1 leverage ratio, which is one of the measures used to determine the assessment rate for small, large, and highly complex IDIs. The neutralization of effects of participation in the PPPLF will be automatically reflected in an IDI's assessment because the FDIC's risk-based assessment system incorporates an IDI's regulatory capital reporting of its Tier 1 leverage ratio.

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<sup>13</sup> See 85 FR 20387 (April 13, 2020).

## *B. Mitigating the Effects of PPP Loans on an IDI's Assessment Rate*

Under the final rule, to mitigate the assessment effect of PPP loans, staff recommends that the FDIC exclude the outstanding amount of PPP loans held by an IDI and borrowings under the PPPLF, from various risk measures used in the calculation of an IDI's deposit insurance assessment rate, as described in more detail below.

### 1. Established Small Institutions

#### a. Exclusion of PPP Loans from Total Assets in Various Risk Measures

Under the final rule, staff recommends that the FDIC exclude the outstanding balance of all PPP loans from total assets in risk measures used to determine an established small institution's assessment rate: the net income before taxes to total assets ratio, the nonperforming loans and leases to gross assets ratio, the other real estate owned to gross assets ratio, the brokered deposit ratio, the one-year asset growth measure, and the loan mix index (LMI).

#### b. Exclusion of PPP Loans from the Loan Portfolio in the LMI

The LMI is a measure of the extent to which an IDI's total assets include higher-risk categories of loans. Consistent with the proposed rule, under the final rule, staff recommends that the FDIC exclude PPP loans, which include loans pledged to the PPPLF, from an institution's loan portfolio in calculating the LMI, based on a waterfall approach.<sup>14</sup> Under the final rule, the FDIC will first exclude the outstanding balance of PPP loans from the balance of C&I Loans in the calculation of the LMI. In the unlikely event that the outstanding balance of PPP loans exceeds the balance of C&I Loans, the FDIC will exclude any remaining balance of these loans from the balance of Agricultural Loans, up to the total amount of Agricultural Loans, in the calculation of the LMI.<sup>15</sup>

### 2. Large or Highly Complex Institutions

Under the final rule, staff recommends that the FDIC remove the outstanding balance of PPP loans from a large or highly complex bank's loan portfolio and its total assets in calculating its assessment rate. As proposed, under the final rule the FDIC also will exclude amounts

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<sup>14</sup> Based on data from the SBA and on the terms of the PPP, the FDIC expects that most PPP loans will be categorized as Commercial and Industrial (C&I) Loans. Collateral is not required to secure the loans. Therefore, staff expects that PPP loans will not be included in other loan categories, such as those that are secured by real estate or consumer loans, in measures used to determine an IDI's deposit insurance assessment rate. See Pub. L. 116-136 (Mar. 27, 2020), Pub. L. 116-142 (June 5, 2020), 85 FR 20811 (Apr. 15, 2020), 85 FR 36308 (June 16, 2020), and Slide 8, Industry by NAICS Subsector, Paycheck Protection Program (PPP) Report: Approvals through 06/06/2020, Small Business Administration, available at: [https://www.sba.gov/sites/default/files/2020-06/PPP\\_Report\\_Public\\_200606%20FINAL\\_-508.pdf](https://www.sba.gov/sites/default/files/2020-06/PPP_Report_Public_200606%20FINAL_-508.pdf)

<sup>15</sup> All Other Loans are not included in the LMI; therefore, staff recommends that the FDIC exclude the outstanding balance of PPP loans from the balance of C&I Loans, followed by Agricultural Loans. The loan categories used in the Loan Mix Index are: Construction and Development, Commercial and Industrial, Leases, Other Consumer, Real Estate Loans Residual, Multifamily Residential, Nonfarm Nonresidential, 1-4 Family Residential, Loans to Depository Banks, Agricultural Real Estate, Agricultural Loans. 12 CFR 327.16(a)(1)(ii)(B).

borrowed from the Federal Reserve Banks under the PPPLF from a large or highly complex bank's liabilities in calculating its assessment rate.

a. Exclusion of PPP Loans from Total Assets in the Core Earnings Ratio and the Short-Term Funding Measure

Under the final rule, staff recommends that the FDIC exclude the quarter-end outstanding amount of PPP loans, whether or not they have been pledged to the PPPLF, from total assets in the core earnings ratio<sup>16</sup> and the short-term funding measure<sup>17</sup> used to determine a large or highly complex institution's assessment rate.

b. Exclusion of PPP Loans from the Loan Portfolio in Various Risk Measures

Under the final rule, staff recommends that the FDIC exclude PPP loans from an IDI's loan portfolio in risk measures used to determine a large or highly complex IDI's assessment rate, as proposed. In calculating the growth-adjusted portfolio concentration measure,<sup>18</sup> which is applicable to large IDIs, the FDIC will exclude the quarter-end outstanding balance of PPP loans from C&I Loans.<sup>19</sup> In calculating the trading asset ratio,<sup>20</sup> which is applicable to highly complex IDIs, the FDIC will reduce the balance of loans by the quarter-end outstanding balance of PPP loans.<sup>21</sup> The FDIC will exclude the quarter-end outstanding balance of PPP loans from a large or highly complex IDI's loan portfolio in calculating the loss severity measure, as described below.

A few commenters suggested that PPP loans should not be classified as "higher risk assets" in calculating the concentration measures for large or highly complex institutions. In response to these comments, staff recommends that the final rule clarify that government guaranteed loans are not considered "higher risk assets" for assessments purposes. Because PPP

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<sup>16</sup> For the core earnings ratio, the FDIC divides the four-quarter sum of merger-adjusted core earnings by the average of five quarter-end total assets (most recent and four prior quarters). See Appendix A to subpart A of 12 CFR part 327.

<sup>17</sup> For highly complex IDIs, the short-term funding ratio is calculated by dividing average short-term funding by average total assets. See Appendix A to subpart A of 12 CFR part 327.

<sup>18</sup> For large banks, the concentration measure is the higher of the ratio of higher-risk assets to Tier 1 capital and reserves, and the growth-adjusted portfolio measure. For highly complex institutions, the concentration measure is the highest of three measures: the ratio of higher risk assets to Tier 1 capital and reserves, the ratio of top 20 counterparty exposure to Tier 1 capital and reserves, and the ratio of the largest counterparty exposure to Tier 1 capital and reserves. See Appendix A to subpart A of part 327.

<sup>19</sup> All Other Loans and Agricultural Loans are not included in the growth-adjusted portfolio concentration measure; therefore, consistent with the proposal, staff recommends that the FDIC exclude the outstanding balance of PPP loans from the balance of C&I Loans under the final rule. The loan concentration categories used in the growth-adjusted portfolio concentration measure are: construction and development, other commercial real estate, first lien residential mortgages (including non-agency residential mortgage-backed securities), closed-end junior liens and home equity lines of credit, commercial and industrial loans, credit card loans, and other consumer loans. Appendix C to subpart A of 12 CFR part 327.

<sup>20</sup> See 12 CFR 327.16(b)(2)(ii)(A)(2)(vii).

<sup>21</sup> To minimize reporting burden, staff recommends that the FDIC reduce average loans in the trading asset ratio by the outstanding balance of PPP loans, as of quarter-end, rather than requiring institutions to additionally report the average balance of PPP loans.

loans are guaranteed by the SBA, they are already excluded from “higher risk assets” in calculating the concentration measures for large or highly complex institutions and no additional modification is necessary.

c. Exclusion of Borrowings Under the PPPLF from Total Liabilities in Various Risk Measures

As proposed, staff recommends that under the final rule the FDIC exclude borrowings from the Federal Reserve Banks under the PPPLF from an institution’s liabilities in the calculation of the core deposit ratio, the balance sheet liquidity ratio, and the loss severity measure used to determine a large or highly complex IDI’s assessment rate.

Under the final rule, in calculating the core deposit ratio<sup>22</sup> for large or highly complex IDIs, the FDIC will exclude from total liabilities borrowings from Federal Reserve Banks under the PPPLF.

Also as proposed, under the final rule the FDIC will exclude an IDI’s reported borrowings from the Federal Reserve Banks under the PPPLF with a remaining maturity of one year or less from liabilities included in the denominator of the balance sheet liquidity ratio.<sup>23</sup> Additionally, in calculating the balance sheet liquidity ratio under the final rule, staff recommends that the FDIC treat the quarter-end outstanding balance of PPP loans that exceed borrowings from the Federal Reserve Banks under the PPPLF as highly liquid assets, as proposed. Because PPP loans are riskless and banks with PPP loans in excess of PPPLF borrowings can access additional liquidity by pledging such loans to PPPLF, the FDIC will treat these PPP loans as highly liquid assets. To the extent that a PPP loan represents collateral for borrowings other than under the PPPLF – such as an FHLB advance – treating the loan as highly liquid will provide an assessment benefit for IDIs that may not be able to readily access additional liquidity. PPP loans can no longer be pledged as collateral to the PPPLF after September 30, 2020, the date after which no new extensions of credit will be made under the PPPLF, unless extended by the Board of Governors and the Department of Treasury. Therefore, under the final rule, the quarter-end outstanding balance of PPP loans that exceed borrowings from the Federal Reserve Banks under the PPPLF will be treated as highly liquid assets until September 30, 2020, unless the Board of Governors and the Department of Treasury extend the deadline to apply for new extensions of credit under the PPPLF.

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<sup>22</sup> The core deposit ratio is defined as total domestic deposits excluding brokered deposits and uninsured non-brokered time deposits divided by total liabilities. *See* Appendix A to subpart A of 12 CFR part 327.

<sup>23</sup> The balance sheet liquidity ratio is defined as the sum of cash and balances due from depository institutions, federal funds sold and securities purchased under agreements to resell, and the market value of available-for-sale and held-to-maturity agency securities (excludes agency mortgage-backed securities but includes all other agency securities issued by the U.S. Treasury, U.S. government agencies, and U.S. government sponsored enterprises) divided by the sum of federal funds purchased and repurchase agreements, other borrowings (including FHLB) with a remaining maturity of one year or less, 5 percent of insured domestic deposits, and 10 percent of uninsured domestic and foreign deposits. Appendix A to subpart A of 12 CFR part 327.



d. Treatment of PPP Loans and Borrowings under the PPPLF in Calculating the Loss Severity Measure

The loss severity measure estimates the relative magnitude of potential losses to the DIF in the event of a large or highly complex IDI's failure.<sup>24</sup> Under the final rule, staff recommends that the FDIC remove the effect of participation in the PPP and PPPLF, as proposed. In calculating the loss severity score under the final rule, the FDIC will remove the effect of PPP loans in an IDI's loan portfolio using a waterfall approach, as proposed. Under this approach, the FDIC first will exclude PPP loans from an IDI's balance of C&I Loans. In the unlikely event that the outstanding balance of PPP loans exceeds the balance of C&I Loans, the FDIC will exclude any remaining balance from All Other Loans, up to the total amount of All Other Loans, followed by Agricultural Loans, up to the total amount of Agricultural Loans.

To the extent that an IDI's outstanding PPP loans are not pledged to the PPPLF, such loans may be funded by a variety of liabilities, such as deposits and secured borrowings. While IDIs will report borrowings under the PPPLF that are secured by PPP loans, the FDIC will not have sufficient data to determine other sources of funding for an IDI's PPP loans. Obtaining such data would require additional reporting burden on IDIs. Because the FDIC will not have sufficient data to remove each type of non-PPPLF funding used to make PPP loans, staff recommends that under the final rule the FDIC remove PPP loans in excess of its PPPLF borrowings from a large or highly complex IDI's loan portfolio based on the waterfall approach described above and reallocate the same amount to cash. Such treatment of PPP loans is consistent with the proposal to treat PPP loans in excess of PPPLF borrowings as riskless for purposes of calculating a large or highly complex IDI's loss severity score.

To match the removal of PPP loans funded through borrowings under the PPPLF from an IDI's loan portfolio, the FDIC will remove the total amount of outstanding borrowings from the Federal Reserve Banks under the PPPLF from short- and long-term secured borrowings, as appropriate.

*C. Mitigating the Effects of PPP Loans and Assets Purchased under the MMLF on Certain Adjustments to an IDI's Assessment Rate*

Under the final rule, staff recommends that the FDIC exclude the quarter-end outstanding amount of PPP loans and the quarterly average amount of assets purchased under the MMLF from the calculation of the unsecured debt adjustment, depository institution debt adjustment, and the brokered deposit adjustment.<sup>25</sup>

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<sup>24</sup> Appendix D to subpart A of 12 CFR 327 describes the calculation of the loss severity measure.

<sup>25</sup> For certain IDIs, adjustments include the unsecured debt adjustment and the depository institution debt adjustment (DIDA). The unsecured debt adjustment decreases an IDI's total assessment rate based on the ratio of its long-term unsecured debt to its assessment base. The DIDA increases an IDI's total assessment rate if it holds long-term, unsecured debt issued by another IDI. In addition, large banks that meet certain criteria and new small banks are subject to the brokered deposit adjustment. The brokered deposit adjustment increases the total assessment rate of large IDIs that hold significant concentrations of brokered deposits and that are less than well capitalized, not CAMELS composite 1- or 2-rated, as well as new, small IDIs that are not assigned to Risk Category I. See 12 CFR 327.16 (e).

*D. Offset to Deposit Insurance Assessment Due to Increase in the Assessment Base Attributable to PPP Loans and Assets Purchased under the MMLF*

Under the final rule, staff recommends that the FDIC provide an offset to an IDI's total assessment amount due for the increase to its assessment base attributable to the quarter-end outstanding balance of PPP loans and participation in the MMLF.<sup>26</sup> Staff further recommends that the FDIC use the quarter-end outstanding amount of PPP loans rather than the quarterly average amount of assets pledged to the PPPLF in calculating the offset to an IDI's total assessment amount. To determine this offset amount, the FDIC will sum the total of the quarter-end outstanding balance of PPP loans and the quarterly average amount of assets purchased under the MMLF, multiply that amount by an IDI's total base assessment rate (after excluding the effects of participation in the PPP, MMLF, and PPPLF, consistent with the final rule), and subtract the resulting amount from an IDI's total assessment amount.<sup>27</sup>

Because the FDIC proposed to calculate the offset as the sum of the quarterly average amount of loans pledged to the PPPLF and the quarterly average of assets purchased under the MMLF, the Board of Governors is requiring that insured branches of foreign banks report only these two additional items on the FFIEC 002 starting with the report filed as of June 30, 2020. Adjustments to the calculation of the assessment rate of an insured branch of foreign banks to mitigate the effect of participation in the PPP, PPPLF, and MMLF are not necessary.<sup>28</sup> Under the final rule, the FDIC will provide an offset to the assessment of an insured branch of a foreign bank that is calculated by summing the quarterly average amount of assets purchased under the MMLF with either the quarterly average amount of loans pledged to the PPPLF, or the amount of outstanding PPP loans at the end of the quarter, based on available data.<sup>29</sup>

*E. Classification of IDIs as Small, Large, or Highly Complex for Assessment Purposes*

Under the final rule, staff recommends that the FDIC exclude the quarter-end outstanding balance of all PPP loans, rather than only those PPP loans pledged to the PPPLF, in the classification of an IDI as small, large, or highly complex for assessment purposes. As a result, the FDIC will not reclassify a small institution as large or a large institution as a highly complex

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<sup>26</sup> Under the final rule, the offset to the total assessment amount due for the increase to the assessment base attributable to the quarter-end outstanding balance of PPP loans and participation in the MMLF will apply to all IDIs, including new small institutions as defined in 12 CFR 327.8(w), and insured U.S. branches and agencies of foreign banks.

<sup>27</sup> Currently, an IDI's total assessment amount on its quarterly certified statement invoice is equal to the product of the institution's assessment base (calculated in accordance with 12 CFR 327.5) multiplied by the institution's assessment rate (calculated in accordance with 12 CFR 327.4 and 12 CFR 327.16). See 12 CFR 327.3(b)(1).

<sup>28</sup> Insured branches are assessed for deposit insurance in accordance with 12 CFR 327.16(c).

<sup>29</sup> Through the Board of Governors, the FDIC anticipates revising the reporting of the quarterly average amount of loans pledged to the PPPLF and instead requiring insured branches of foreign banks to report the outstanding balance of PPP loans at quarter-end, beginning as of September 30, 2020. For purposes of determining the deposit insurance assessment amount for an insured branch of a foreign bank as of June 30, 2020, an insured branch additionally may provide to the FDIC certified information on the amount of outstanding PPP loans at the end of the quarter.

institution solely due to participation in the PPPLF and MMLF programs, which would otherwise have the effect of expanding an IDI's balance sheet.<sup>30</sup>

#### *F. Other Conforming Amendments to the Assessment Regulations*

Under the final rule, staff recommends that the FDIC make conforming amendments to the FDIC's assessment regulations to effectuate the modifications described above. These conforming amendments ensure that the modifications to an IDI's assessment rate and the offset to an IDI's assessment amount under the final rule are properly incorporated into the assessment regulation provisions governing the calculation of an IDI's quarterly deposit insurance assessment.

### **EXPECTED EFFECTS**

Under the final rule, the FDIC will mitigate the deposit insurance assessment effects of PPP loans, amounts borrowed under the PPPLF, and assets purchased under the MMLF. Because IDIs are not yet reporting the necessary data, staff does not have sufficient data on the distribution of loans among IDIs and other non-bank financial institutions made under the PPP, the loan categories of PPP loans held, the types of liabilities used to fund PPP lending, the extent to which PPP participation resulted in an increase to an IDI's total assets and total liabilities, nor on the dollar volume of assets purchased under the MMLF by IDIs. Although this estimate is subject to considerable uncertainty, staff estimates that application of the final rule could provide quarterly assessment relief to IDIs participating in these programs totaling approximately \$150 million, based on certain assumptions.<sup>31</sup> The actual effect of these programs on deposit insurance assessments will vary depending on participation in the programs by IDIs and non-IDIs, the maturity of borrowings from the Federal Reserve Banks under these programs, the extent of reliance on existing sources of funding for PPP lending, and the types of loans held under the PPP, as described above. To the extent that some IDIs may rely on existing balance sheet liquidity to fund PPP lending, certain provisions of the final rule may reduce assessments for some institutions by more than they would have increased due to participation in PPP lending.

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<sup>30</sup> In addition, a small institution with total assets between \$5 billion and \$10 billion, excluding the amount of PPP loans and assets purchased under the MMLF, may request that the FDIC determine its assessment rate as a large institution. See 12 CFR 327.16(f).

<sup>31</sup> In estimating the deposit insurance assessment effects of participation in the PPP, PPPLF, and MMLF, staff assumed that (1) \$600 billion of PPP loans are held by IDIs, (2) the PPP loans that are held by IDIs are evenly distributed across all IDIs that have C&I loans, which results in a 33 percent increase in those loans, except where IDI-specific data are available, (3) 5.9 percent of PPP loans held by IDIs are pledged to the PPPLF, except where IDI-specific data are available, (4) 100 percent of loans pledged to the PPPLF are matched by borrowings from the Federal Reserve Banks with maturities greater than one year, (5) IDIs fund the remaining 94.1 percent of PPP loans with additional funding, including deposits or secured borrowings, and (6) large and highly complex IDIs hold approximately \$30 billion in assets pledged under the MMLF. Based on Call Report data as of March 31, 2020, SBA data as of June 6, 2020, and Federal Reserve data as of June 11, 2020. Because PPP loans must be issued by June 30, 2020, and because the FDIC expects that eligible IDIs will begin receiving PPP loan forgiveness reimbursement from the SBA, the FDIC expects that the amount of assessment relief provided under this final rule will decline in subsequent quarters.

## CONCLUSION

FDIC staff are requesting the FDIC Board to approve this final rule and authorize its publication in the *Federal Register* with an immediate effective date and an application date of April 1, 2020.

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