Massachusetts Bankers Association

December 17, 2008

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

RE: RIN 3064-AD35
Assessments

Dear Mr. Feldman:

On behalf of our 200 commercial, savings and co-operative banks, federal savings banks, and savings and loan associations throughout Massachusetts and New England, the Massachusetts Bankers Association (MBA) appreciates the opportunity to comment on the Federal Deposit Insurance Corporation's (FDIC) proposed rule revising deposit insurance assessment rates and changing the risk-based assessment system. The proposed rule would implement the FDIC's restoration plan to recapitalize the Deposit Insurance Fund (DIF).

MBA believes a strong deposit insurance fund is essential to maintaining depositor confidence, particularly given the current economic crisis. As more and more Americans engage in a "flight to quality" and move their savings into insured deposit accounts, it is imperative that these depositors have confidence in the strength of the FDIC and the deposit insurance system. The proposed rule makes a number of changes to the current assessment system designed to recapitalize the fund over the next several years.

While we support changes to the assessment formula that more accurately reflect the risk of loss to the Fund, we have a number of serious concerns with the proposal. Our member institutions, and the vast majority of banks throughout New England, are well capitalized and did not contribute to the current crisis. The FDIC's proposed rule would penalize these banks with higher premiums, even though they pose significantly lower risk to the Fund than institutions engaged in riskier lending and investment practices. In particular, we believe agency's insistence on returning the fund to a reserve ratio of 1.25 percent instead of the statutorily mandated 1.15 percent is counterproductive and will limit the ability of many banks, particularly community banks, to meet the credit needs of their local communities.

Our comments will focus on the new risk categories that the FDIC is proposing to add to the formula: secured liabilities, specifically Federal Home Loan Bank (FHLB) Advances, and brokered deposits, including the Certificate of Deposit Account Registry Service (CDARS). We believe these provisions will have the most significant impact on our member institutions.

Secured Liabilities

The proposed rule imposes an additional charge on the assessment rate for institutions that have ratios of secured liabilities to domestic deposits exceeding 15 percent. Secured liabilities include any securities sold under repurchase agreements, secured federal funds, and most importantly, FHLB advances. This additional

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charge could increase the assessment rate of a Category I bank above the proposed ceiling of 14 basis points. We believe this approach is deeply flawed and will have a number of unintended consequences.

Under the current formula, secured liabilities do not affect an institution's assessment rate; however the agency believes that this exclusion can lead to inequities in the system. Specifically, the agency states that under the current rules, substituting secured liabilities for unsecured liabilities increases the FDIC's loss in the event of a failure without providing any increased assessment revenue.

Our member banks, like institutions throughout the country, use FHLB advances for a number of reasons. Most importantly, they are a stable source of liquidity that allows them to manage the overall cost of funding. In this volatile environment, there are often competing institutions which put significant upward pressure on the cost of retail deposits in a particular region. In particular, several of the former investment banks that recently obtained federal or state bank charters are expected to aggressively pursue deposits and large, out-of-state institutions may also market their deposit products in regions where they do not have physical branches. Banks also use advances to effectively manage interest rate risk. By match-funding longer term loans, community banks can maintain safe and sound banking practices via a stable, low-cost funding source.

Without access to advances, banks would be forced to rely on higher rate deposits more heavily during these periods. Over the last six months, the availability of advances has been particularly useful as funding sources dried up due to the frozen credit markets. At a time when federal policymakers and Members of Congress are calling on banks to increase their lending activity in an effort to improve the nation's economy, increasing the cost of lending for community banks is counterproductive.

While we have a large proportion of residential lenders in Massachusetts and New England, we are operating in a state that has seen less than 1.5% annual deposit growth in the past five years. The banks that have failed or that add more risk to the Deposit Insurance Fund do not do so as a result of increased FHLB advances or brokered deposits. They fail due to the types and growth of lending that the funding supports such as alt-A and subprime mortgage lending or out-of-market construction and development loans.

For example, the FDIC often cites the resolution cost of Indy Mac as one of the prime reasons for imposing a new fee on FHLB advances. Again, we would assert that it was not the source of funds which caused IndyMac's problems, but how they were using the funds. A higher fee for advances will only serve to discourage lending by traditional lenders, not "go-go" lenders such as IndyMac.

The FDIC and the other banking regulators already have risk monitoring processes in place, Safety and Soundness Examinations and CAMELS ratings. The regulators also have the ability to curtail these riskier practices on a bank-specific basis before they become problematic and contribute to bank failures. Instead of penalizing healthy banks that are providing much-needed credit in their communities, the FDIC should be working with the other banking agencies and the FHLB system to develop more effective monitoring systems and reporting mechanisms so that potential issues can be addressed before they cause problems for the DIF.

If the FDIC decides to impose higher premiums on banks that use secured liabilities, we strongly suggest that the proposed 15 percent threshold be increased to at least 45 percent of domestic deposits. This would allow institutions to continue accessing FHLB funding, while discouraging banks from using FHLB advances to support higher-risk lending strategies.

Brokered Deposits

The proposed rule also creates a new premium adjustment for the use of brokered deposits for banks in Risk Categories II, II, and IV. Institutions with ratios of brokered deposits to domestic deposits in excess of 10

percent would be assessed based on a formula that takes the ratio of brokered deposits, minus 10 percent and multiplied by 25 basis points. The maximum adjustment under the proposed rule would be 10 basis points.

According to the FDIC, significant reliance on brokered deposits tends to increase an institution's risk profile. Some weaker insured institutions pay higher interest rates on brokered deposits in order to maintain adequate liquidity. The agency also believes that brokered deposits greatly reduce the value of a failed institution, particularly in cases where the institution has funded rapid asset growth through the use of brokered deposits.

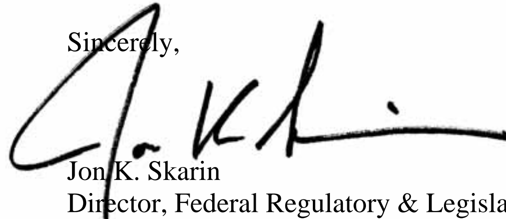
MBA is concerned with failed or troubled banks that have used brokered deposits to grow rapidly and fund risky assets. However, the proposed rule does not differentiate between types of brokered deposits. Specifically, we believe it is unfair to include CDARS deposits in the same risk category as other, more volatile forms of brokered deposits. Several of our member banks use the CDARS program to provide depositors with additional deposit insurance coverage – coverage that is even more important given the volatility in the economy. In Massachusetts, where many, but not all institutions have excess deposit insurance coverage through one of two state funds, banks without access to this extra coverage rely on the CDARS program to compete for deposits in their communities.

Placing a significant cost on maintaining CDARS places these institutions at a competitive disadvantage, and could encourage depositors to withdraw money from healthy institutions for deposit in higher-risk banks that are paying higher interest rates. MBA strongly believes that the FDIC should exclude CDARS from the calculation of brokered deposits. This method of funding is not risky and any concerns should be raised as part of the examination process – which is included in the premium calculation.

Conclusion

Thank you again for the opportunity to comment on the proposed rule. Please contact me at (617) 523-7595 or via email at jskarin@massbankers.org if you have any questions or need additional information.

Sincerely,



Jon K. Skarin
Director, Federal Regulatory & Legislative Policy

JKS