LIBERTAD Bank SSB

April 3, 2009

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

**Re: Public Comments FDIC Part 337 - Interest Rate Restrictions**

Dear Mr. Feldman,

I am writing in response to the Notice of Proposed Rulemaking - Interest Rate Restrictions on Institutions that are Less Than Well Capitalized. (Part 337- Interest Rate Restrictions) published in the Federal Register: February 3, 2009 (Volume 74, Number 21, pages 5904-5908).

While I strongly support the FDIC's efforts to bring much needed clarity and concreteness to the aforementioned limits, after reviewing the proposed rulemaking I am very concerned about the simplistic deposit interest rate analysis presented to support the proposed rule, the conclusions drawn from that analysis, and the methodology of using "a simple average of rates paid by all insured depository institutions and branches for which data are available," for calculating the proposed "national rate" as a proxy for the 'prevailing market rate'.

In its desire for simplicity and concreteness, the FDIC should not rush to adopt and implement a rule that will have significant unintended negative consequences.

**Adopting the proposed rule as written will have significant negative unintended consequences, not be consistent with the original intent of the United States Congress in enacting 12 USC 1831 - Sec. 1831(f) Brokered Deposits / Section 29 of the Federal Deposit Insurance Act, and will unnecessarily and artificially increase the risk to, and ultimate losses incurred by, the FDIC Deposit Insurance Fund.**

**Personal Background**

I am an executive of a financial institution that is currently subject to Part 337.6 rate restrictions. While the institution I work for has capital ratios that would easily classify the institution as well capitalized if measured by those ratios, the institution previously consented to a written agreement with the FDIC that included a capital maintenance provision, and it is therefore classified as 'adequately capitalized' regardless of its capital ratios, and is therefore subject to Part 337.6 rate restrictions.

As of January 31, 2009, the bank's capital ratios were:

| | Bank's Ratios | Required ratio to be 'well capitalized' |
|---|---|---|
| Core capital (leverage) ratio | 15.7% | 5.0% or greater |
| Tier 1 risk-based capital ratio | 22.3% | 6.0% or greater |
| Total risk-based capital ratio | 23.5% | 10.0% or greater |

As an institution subject to Part 337.6 rate caps I am very familiar with the difficulties and ambiguities involved in attempting to calculate and comply with the Part 337.6 rate cap regulations as derived from Section 29 of the Federal Deposit Insurance Act and the underlying 12 USC 1831 - Sec. 1831(f).

In our initial attempts at calculating a prevailing rate in our normal market area, we utilized a 'Rateline' service, but quickly realized that the service did not accurately reflect the prevailing rates offered in our normal market area. We subsequently established procedures to do a manual survey of rates at least monthly and more frequently during times of high rate volatility. Our rate methodology has been reviewed multiple times by our FDIC Regional Office. Our FDIC Regional Office took the additional step to create its own rate survey for our market area and compare it to the bank's rate survey, presumably because it apparently believed we were offering rates that might be 'substantially above the prevailing deposit rates offered in our normal market area'. In the end, after extensive time and resources were expended by both the Bank and our FDIC Regional Office, the result was that the FDIC derived rate survey differed from the bank's rate survey by only a few immaterial basis points, both higher and lower.

It is the express intent of the bank to comply with Part 337.6 and we are pleased to see the FDIC take this opportunity to openly and publicly discuss the issues related to Part 337.6 rate cap calculations in an effort to streamline and simplify both compliance and verification of compliance with the rate restrictions.

Based on my personal experience in attempting to have a bank comply with Part 337.6 Regulations and the intent of the law, I offer the following observations and recommendations on the proposed methodology and put forth several questions for consideration before the proposed rules become final.

**Definition of 'Brokered Deposits'**

The Law and FDI Act set forth clear definitions for most brokered deposits. For the most part it is a straight forward process for both a financial institution and its regulators to determine if a deposit is 'brokered'. As the Memo points out, the difficulty in complying with and verifying compliance with the Law, FDI Act, and Part 337.6 regulations (Regulations) is centered on determining a clear and easily measurable definition of "rates of interest which are significantly higher than the prevailing rates of interest on deposits offered by other insured depository institutions". To establish a clear and easily measurable metric for such rates, the FDIC has set forth its proposed methodology in the Memo. Unfortunately, the FDIC's analysis and methodology does not reflect the realities in the marketplace for deposits nor the advances in technology since the Law was originally enacted in 1989.

**Memo 'Analysis and Conclusion'**

On page 3 of the January 22, 2009 Memo to the FDIC Board of Directors, the FDIC sets forth the following analysis and conclusion:

> *"The uncertainty in the FDIC's regulation has made it difficult for banks and regulators to administer the regulation and appears to have resulted in higher rates being paid by less than well capitalized banks as compared to other banks. For example, based on the most recent information currently available, the average 1-year certificate of deposit rate paid by less than well capitalized banks was 2.87 while the average 1-year certificate of deposit rate paid by all insured banks and branches over the same period for which the FDIC had data was 2.18 percent."*

This analysis is faulty. Using "a simple average of rates paid by all insured depository institutions and branches for which data are available" to draw such a sweeping conclusion is potentially very misleading and dangerous. As I will illustrate below, **simple averages for standard maturity time deposits do not reflect the true "prevailing rates of interest" in any market**, and therefore should not be used as a proxy for the 'prevailing market rate' absent an appropriate adjustment factor.

While I can appreciate the FDIC's desire for simplicity and concreteness in deriving rate caps, further refinement and modification is necessary to the proposed rule to avoid a potentially dramatic unintended consequence of the proposed rule and the associated compounded losses to the FDIC Deposit Insurance Fund that are completely avoidable absent adoption and implementation of the proposed rule change.

**Methodology Analysis**

As with any analysis, the conclusion and methodology to derive that conclusion should be compared to current 'real-world' data to verify and confirm their veracity (and should also usually be back-tested

against historical data to augment such an analysis). Data and analysis relevant to the proposed rule is presented below.

**Odd Term Maturities**

The current regulations establish a methodology for an institution offering 'odd term' maturities. Part 337.6 states that:

> *An effective yield on a deposit with an odd maturity violates paragraphs (b)(2)(ii)(A) and (b)(3)(ii) of this section if it is more than 75 basis points higher than the yield calculated by interpolating between the yields offered by other insured depository institutions on deposits of the next longer and shorter maturities offered in the market.*

The proposed new regulations do not contemplate odd rate maturities, and if a rate was interpolated between the "national rate" standard duration maturity CD rates as proposed, it would be well below the "prevailing rates" in the market. This is a critical flaw in the proposed rate limitation calculation.

When the Law and Regulations were originally contemplated, odd rate maturities were the exception not the rule. Today most financial institutions offer below market interest rates on standard term/maturity fixed-rate time deposits, while offering much more attractive interest rates on odd-term time deposits. Financial institutions do this to match their funding to their liquidity needs and projections, but also as a marketing tactic to make it difficult to directly compare one institution's time-deposit offerings to another institution's (and in this case making it difficult, if not impossible, for both banks and the FDIC to use simple averages calculated from 'standard term maturity' time deposit data to determine prevailing market interest rates).

For example, on February 6 & 7, 2009 the following time deposit terms and rates were being offered by financial institutions in our local area:

**Wells Fargo**

| | | |
|---|---|---|
| **9 Month Standard CD** | **1.30% APY** | **$5,000 minimum balance** |
| 12 Month Standard CD | 1.10% APY | $10,000 minimum balance |
| 24 Month Standard CD | 1.25% APY | $5,000 minimum balance |
| **25 Month Standard CD** | **2.25% APY** | **$5,000 minimum balance** |

**Bank of America**

| | | |
|---|---|---|
| **7 Month Standard CD** | **1.85% APY** | **$5,000 minimum balance** |
| 12 Month Standard CD | 1.26% APY | Less than $10,000 minimum balance |
| 24 Month Standard CD | 1.50% APY | Less than $10,000 minimum balance |

**Wachovia**

| | | |
|---|---|---|
| **9 Month Standard CD** | **1.40% APY** | **$5,000 minimum balance** |
| 12 Month Standard CD | 0.85% APY | $1,000 to $9,999 balance |
| **17 Month Standard CD** | **2.00% APY** | **$5,000 minimum balance** |
| 24 Month Standard CD | 0.95% APY | $1,000 to $9,999 balance |

Using simple averages of the above three institutions' 12 and 24 month rates would provide the following:

12 month rate: 1.07% APY
24 month rate: 1.23% APY

Clearly these simple averages for standard term maturity time deposits are not indicative of the "prevailing interest rates" in the market as no rational depositor would select either of these terms and rates given the other odd-term options provided by the same institutions. For example, any rational depositor would select the 25 month 2.25% CD from Wells Fargo yielding 100bps higher than the standard term maturity 1.25% 24 month CD.

**Weighting of Sample Selection**

The FDIC states that the national average rate would be calculated by:

*"…a simple average of rates paid by all insured depository institutions and branches for which data are available."*

During the FDIC Board meeting on January 27, 2009, Mr. Bervid stated that the data source the FDIC used to calculate its simple national averages has 80,000 institutions/branches.

As illustrated in the preceding section, many banks post artificially low standard maturity term rates which are not reflective of the 'prevailing rate' being paid in the market for deposits. Does the FDIC propose to take the 'artificially low' standard maturity 12 and 24 month term rates of these financial institutions and then multiply them by the number of branches of each institution to determine an average national rate? For example, multiply Bank of America's standard term maturity rates by ~6,100 and Wells Fargo by ~6,000? Using this approach would obviously distort the "average national rate" to a rate much lower than the actual prevailing market rate being paid for deposits in any market area.

The FDIC might consider simply adding each institution's rate only once to the sample and dividing by the total number of institutions in the sample to determine a national average rate to minimize this distortion. This approach is supported by the FDIC's own assertions. On page 4 of the Memo presented to the FDIC Board of Directors, the logic is presented that the proposed approach: *"…recognizes that with the increasing prevalence of Internet deposits and Internet advertising of deposit rates, competition for deposit pricing has become more national in scope."*

Additionally, in the original memo posted to FDIC.gov for the January 27, 2009 FDIC Board meeting, the use of online deposit interest rate comparison services by consumers (e.g. Bankrate.com and similar) make the use of one rate per institution more appropriate. The original Memo stated on Page 19, *"Today, a consumer can compare interest rates around the country simply by checking certain Web sites."* A simple use of any of these services will clearly illustrate that only one rate for each institution is presented to the user, i.e. the search results screen of a simple rate search does not return 6,000+ Bank of America or Wells Fargo rates, it returns one rate for the desired size deposit and maturity. Accordingly, multiplying an artificially low rate by the number of branches of an institution inappropriately biases the calculation of a simple national average.

Another way to consider this same issue is that consumer rate selection is a binary choice. If Bank A offers 3% and Bank B offers 2.75% on similar deposit products, according to the rationale being used to support a national rate, it does not make a material difference to the consumer if Bank A has 1 branch and Bank B has 20,000 branches. The consumer evaluating rates on the internet is choosing only between 3% or 2.75%, not between 3% and 20,000 individual 2.75% rates.

**Differing Delivery Channels (Technology)**

Comparing similar duration time deposits today is not as straight-forward as it may seem. For example, Bank of America offers the following:

**Bank of America**

| | | |
|---|---|---|
| 12 Month Standard CD | 1.26% APY | Less than $10,000 minimum balance |
| **12 Month 'High Yield' CD** | **2.01% APY** | **$5,000 minimum balance** |

The Bank of America 'High Yield' CD must be opened via the Internet. Which interest rate would the FDIC use in determining its 'national average'? Again, a rational depositor would always opt for the higher interest rate on the same duration CD from the same institution and given the ubiquitous nature of Internet accessibility today, would it not be most logical to select the higher rate for the average national interest rate sample?

**Time Deposit Attributes (Technology)**

To further complicate the use of simple averages, is the introduction of time-deposits with complex attributes, which include; 'variable rate', 'callable', 'liquid', 'step-rate', and 'ready access' time deposits. These time deposits may or may not have lower rates than 'traditional fixed rate' CDs of similar size and duration, and may provide other benefits such as, no penalties for early withdrawal, rates that can adjust up later (but not down), etc.

Again using Bank of America as just one example of this issue, it offers the following:

**Bank of America**

| | | |
|---|---|---|
| 9 Month Standard CD | 1.00% APY | Less than $10,000 minimum balance |
| **9 Month 'Risk Free' CD** | **1.75% APY*** | **$5,000 minimum balance** |

* Rate is increased by 0.25% APY if $10,000 is added to deposit from a source outside of Bank of America. No penalty for early withdrawal.

Would the 'standard' CD rate be used to determine a national average, or would the highest rate offered for a particular size and maturity be used to determine the actual prevailing rates in the market? What if the rate can be adjusted upward after origination, how would this be accounted for in the rate determination? If a 12 month time deposit has no penalty for early withdrawal, is it really a 12 month time deposit, or is it a non-maturity deposit since it can be readily withdrawn at any time without penalty?

**Size of Deposit**

The Memo indicates that a national rate would be established for each size and maturity set forth in the national rate table. **The selection of the rate tiers for these "national rates" would be a critical element.** For example, defining a deposit size tier of $75,000 to $100,000 might generate an "average national rate" materially different from a tier of $50,000 to $95,000 or $90,000 to $99,000. What would be the rate tiers for the proposed national rates and caps? What would be the FDIC's methodology to handle the fact that in the deposit market the institutions it surveys to determine the "national rate" will not have rate tiers that align exactly with the rate tiers the FDIC establishes? Will the FDIC always choose the highest rate to avoid downward bias on the "national rate"?

**Exclusion of Credit Unions**

Currently as an institution subject to Part 337.6 we have been instructed by the FDIC to exclude local Credit Unions in determining a prevailing average interest rate in our market. Credit Unions today have expanded both their scope of product offerings and their fields of membership. Clearly banks compete against Credit Unions with large geographic based fields of membership for deposits and the rates these Credit Unions offer affect the prevailing rates that are offered for deposits by banks.

Part 337.6 states:

> *(4) For purposes of the restriction contained in paragraphs (b)(2)(ii)(A) and (b)(3)(ii) of this section, the effective yields in the relevant markets are the average of **effective yields offered by other insured depository institutions** in the market area in which deposits are being solicited. …. A market area is any readily defined geographical area in which the rates **offered by any one insured depository institution soliciting deposits in that area may affect the rates offered by other insured depository institutions** operating in the same area*

From NCUA.gov

> *The National Credit Union Administration (NCUA) is the federal agency that administers the National Credit Union Share Insurance Fund (NCUSIF). The NCUSIF, like the FDIC's Deposit Insurance Fund, is a federal insurance fund backed by the full faith and credit of the U.S. Government.*
>
> *The NCUSIF insures member savings in federally insured credit unions, which account for approximately 98 percent of all credit unions. All federal credit unions and the vast majority of state-chartered credit unions are covered by NCUSIF insurance protection.*

Based on the Law, Act, and Regulations, a Credit Union with an open or large geographic field of membership would appear to meet both the definition of an *"insured depository institution"* and the interest rates offered by such Credit Unions clearly *"may affect the rates offered by other insured depository institutions".* The case for including Credit Unions is further strengthened because the text "having the same type of charter" was stricken from the original Law in 1994.

If the purpose of the “national rate” is to determine the prevailing interest rates offered in the market by insured depository institutions and the deposit rates Credit Unions offer affects the rates offered by other depository institutions, why are Credit Unions excluded from the current and proposed determination of the “prevailing rates paid on deposits”?

**Non-Maturity Products**

As stated earlier, the purpose of Section 29 of the Federal Deposit Insurance Act is to limit or prohibit institutions that are classified as less than well capitalized from accepting ***Brokered*** deposits, not to prohibit them from accepting ***ANY or ALL*** deposits. Brokered deposits are defined in the Act and include rates offered by financial institutions themselves that *“are significantly higher than the prevailing rates of interest on deposits offered by other insured depository institutions in such depository institution's normal market area.”*

The proposed rule makes no differentiation between account types for non-maturity deposit products. **This is a critical issue, as this rate cap methodology would essentially eliminate the ability of a financial institution subject to part 337.6 to obtain or retain savings, money market, NOW, or interest-bearing non-maturity deposits.**

By lumping together all non-maturity transaction accounts into one category, the posted “average national rate” and “rate cap” would effectively prevent a bank subject to Part 337.6 from offering an average market rate, much less a prevailing market rate for certain categories of deposit bearing non-maturity deposit accounts. For the purpose of determining prevailing market rates, deposit products such as savings accounts, online savings accounts, money market accounts, online money market accounts, and rewards checking accounts should be grouped according to accounts with similar attributes and restrictions to determine a prevailing market rate or “average national rate” and a rate cap should be applied to each group based on size of the deposit relationship.

This point is best illustrated through a ‘real-world’ example.

## Example: IndyMac FSB (under FDIC Conservatorship)

As an example of the potential impact of the proposed rule, let's examine IndyMac FSB under conservatorship of the FDIC ('FDIC IndyMac').

First let me explicitly state that the purpose of this empirical example is not to raise the question as to whether the deposit rates IndyMac Bank under the conservatorship of the FDIC was offering in January of 2009 were in excess of rate caps as calculated under Part 337.6 of the FDIC Rules and Regulations. Rather it is to use the rates being offered by an institution under FDIC conservatorship as a barometer of the prevailing market rates and then compare them to the proposed methodology as a measurement of how accurately the proposed 'average national rate' rate calculation reflects true prevailing market rates.

For this analysis, I will assume the following to be true:

1. The FDIC as Conservator of IndyMac Bank would not offer interest rates on deposits substantially above the prevailing market rates
2. The deposit rates offered by the FDIC in January 2009 as Conservator of IndyMac Bank would be indicative of prevailing market rates at that time

These assumptions are supported by articles generally reported in the media, for example:

> *"…almost immediately after the agency took over IndyMac last July, it sent over two of its top officials, chief operating officer John Bovenzi and Dallas-based assistant director Rick Hoffman, to Pasadena, Calif., to run the bank. Bovenzi became IndyMac's CEO. Hoffman took on the role of president. For Bovenzi and Hoffman, cost-cutting was high on their agenda. They slashed the rate the bank was paying on certificates of deposit..."*
>
> Source: Time Magazine, Time.com, Nationalized Banks: Why They Might Work
> By Stephen Gandel Friday, March 6, 2009

Additionally, the FDIC has stated that while it did continue to offer 'above market rates' to existing IndyMac depositors at the time it became Conservator of IndyMac Bank to retain the bank's franchise value, the FDIC has also stated that those rates were only offered to existing customers to retain them, and that new customers were offered rates more in line with prevailing market rates. As such, the rates used in this analysis include only those rates publicly available to new customers in January of 2009 (6 months after the FDIC became conservator of IndyMac FSB). So it is reasonable to assume the interest rates being offered by FDIC IndyMac in January of 2009 are reflective of prevailing market rates and not significantly above prevailing market rates.

In addition to these assumptions, it appears that IndyMac Bank is a financial institution that is both less than well capitalized and an institution that has been under the conservatorship of the FDIC for over 90 days, therefore it may not accept, renew or rollover any brokered deposit. Accordingly the interest rates it offered in January of 2009 must be within the restrictions of Part 337.6 of the regulations.

On July 11, 2008, IndyMac Bank, F.S.B., Pasadena, CA was closed by the Office of Thrift Supervision (OTS) and the FDIC was named Conservator.

Per part 337.6 (Regulations based on the Law and FDI Act)

> *(d) Exclusion for institutions in FDIC conservatorship. No insured depository institution for which the FDIC has been appointed conservator shall be subject to the prohibition on the acceptance, renewal or rollover of brokered deposits contained in the § 337.6 or section 29 of the Federal Deposit Insurance Act for 90 days after the date on which the institution was placed in conservatorship. <u>During this 90-day period, the institution shall, nevertheless, be subject to the restriction on the payment of interest contained in paragraph (b)(2)(ii) of the section. After such 90-day period, the institution may not accept, renew or roll over any brokered deposit</u>.*

Per the FDIC.gov website, on December 31, 2008 FDIC IndyMac Bank had the following capital ratios:

| | FDIC IndyMac | Required ratio to be 'well capitalized' |
|---|---|---|
| Core capital (leverage) ratio | -23.83% | 5.0% or greater |
| Tier 1 risk-based capital ratio | -58.49% | 6.0% or greater |
| Total risk-based capital ratio | -58.49% | 10.0% or greater |

**FDIC IndyMac Time Deposits**

On January 5, 2009 FDIC IndyMac was offering a 12 month CD with a 2.90% APY. Logically, the FDIC would not be offering interest rates that *"are significantly higher than the prevailing rates of interest on deposits offered by other insured depository institutions"* or accepting 'brokered deposits' as defined by the Part 337.6 interest rate caps, yet the rate FDIC IndyMac was offering on its 12 month CD was 95 bps point higher than the "national average rate" on January 4, 2009 as presented in the Memo and 20 bps higher than the proposed rate cap.

**This is a clear indicator that the prevailing market rate for deposits is higher than what the proposed average "national rate" and "rate cap" methodology would indicate.**

This is also true for the 6 month certificate of deposit offered by FDIC IndyMac at 2.55% APY on January 5, 2009. The 2.55% APY rate offered by FDIC IndyMac on 6 month time deposits was 100 bps higher than the "national average" rate of 1.55% shown in the Memo, and 25 bps higher than the proposed rate cap.

**Memo 'Analysis and Conclusion': FDIC IndyMac**

As stated earlier in this comment, on page 3 of the January 22, 2009 Memo to the FDIC Board of Directors, the FDIC sets forth the following analysis and conclusion:

> *"The uncertainty in the FDIC's regulation has made it difficult for banks and regulators to administer the regulation* ***and appears to have resulted in higher rates being paid by less than well capitalized banks as compared to other banks. For example, based on the most recent information currently available, the average 1-year certificate of deposit rate paid by less than well capitalized banks was 2.87 while the average 1-year certificate of deposit rate paid by all insured banks and branches over the same period for which the FDIC had data was 2.18 percent.****"*

To further support the assertion, that **simple averages for standard maturity time deposits do not reflect the true "prevailing rates of interest" in any market**, please review the table below. Assuming that FDIC IndyMac is paying 'prevailing rates' of interest on deposits and not paying rates of interest on deposits 'substantially higher than prevailing rates', FDIC IndyMac's rate should be a reasonable approximation of 'true' prevailing rates in the market. While it is evident the data used to draw the FDIC conclusion presented above was from a time when 'average rates' were higher than the January 4, 2009 calculated rates presented in the rate cap table in the Memo, the 1 -year CD offered by FDIC IndyMac on January 5, 2009 still far exceeded the 'average national rate' and was also higher than the average rate paid by Less Than Well Capitalized banks.

| 1-Year CD Rates | Rate | Source |
|---|---|---|
| FDIC IndyMac Rate | 2.90 | January 5, 2009 imb.com |
| Ave. Rate Paid by 'Less than Well Capitalized' FI | 2.87 | Memo: Analysis & Conclusion, date not incld |
| 'National Ave. Rate' | 2.18 | Memo: Analysis & Conclusion, date not incld |
| 'National Ave. Rate' | 1.95 | Memo: January 4, 2009 |

While I can appreciate the FDIC's desire for simplicity and concreteness as a Regulator, clearly the 'average national rate' calculated as proposed in the Memo is not a good proxy for 'prevailing market rates' as it far underestimates 'true' prevailing market rates.

**FDIC IndyMac Non-Maturity Deposits**

A survey of FDIC IndyMac's posted rates for non-maturity deposit products on January 29, 2009 reveals the following as compared to the proposed Part 337.6 national rate caps (see **APPENDIX A** for complete rate information):

| Non-Maturity Product | APY Cap or Top Rate | In Compliance with Proposed Part 337.6 Cap? |
|---|---|---|
| National Average as Calculated for Memo | 0.60% | |
| **Proposed Rate Cap** | **1.35%** | |
| FDIC IndyMac Starter Savings | 1.75% | **NO** |
| FDIC IndyMac Super Savings | 1.75% | **NO** |
| FDIC IndyMac Money Market | 1.75% | **NO** |
| FDIC IndyMac E Money Market | 2.25% | **NO** |
| FDIC IndyMac Premium Checking | 1.25% | YES |
| FDIC IndyMac Ultimate Checking | 1.50% | **NO** |
| FDIC IndyMac Online Retirement Money Market | 1.75% | **NO** |
| FDIC IndyMac Online Retirement Top Tier MM | 1.75% | **NO** |
| FDIC IndyMac Online Retirement Super Savings | 1.75% | **NO** |

Note: Under the proposed methodology set forth in the Memo, the rate cap for all non-maturity products on January 4, 2009 would have been 1.35%. For the table above, FDIC IndyMac rates from January 29, 2009 are compared to the limits included in the Memo as of January 4, 2009. As illustrated in the Federal Reserve Board Certificate of Deposit rate information below, deposit interest rates declined between January 4, 2009 and January 29, 2009, so the level of Part 337.6 non-compliance would likely increase if the proposed 'National Rate' and 'Rate cap' as calculated for the Memo were updated to January 29, 2009.

| Date | Average Interest Rate |
|---|---|
| Jan 2, 2009 | 1.74% |
| Jan 30, 2009 | 1.56% |

Source: Federal Reserve Board: Data on 6 month certificate of deposit rates

A review of the rates offered by FDIC IndyMac on the above non-maturity deposits products illustrates that almost every non-maturity interest bearing deposit product offered by FDIC IndyMac would be above the non-maturity product rate cap under the proposed methodology (8 out of 9 accounts) and substantially above the "national average" for non-maturity deposit accounts as calculated using the methodology proposed in the Memo. Clearly FDIC IndyMac, even under the conservatorship of the FDIC and the FDIC's associated implicit guaranty of all deposits in the bank, would see significant deposit outflows and have extreme difficulty in attracting core deposits and maintaining liquidity if it had to set its non-maturity deposit rates in accordance with the proposed rate cap methodology as this would effectively eliminate its ability to compete for these low cost core deposits at prevailing market rates.

Implementing the proposed rule as written would raise both the risk and ultimate cost to the FDIC Deposit Insurance Fund as it would likely push otherwise stable financial institutions towards liquidity failure or liquidity crisis events by putting unwarranted restrictions on their ability to pay a prevailing market rate on specific categories of non-maturity deposits to attract and retain adequate liquidity in the form of low-cost relationship core deposit accounts.

This rate survey also highlights that the difficulties in determining prevailing market rates for non-maturity deposits have many similarities to the difficulties in determining the prevailing market rates for time deposits. For example, a FDIC IndyMac E-Money Market account offers a 2.25% APY, while a FDIC IndyMac 'standard' money market account offers only 1.75% APY.

**‘Rewards Checking’**

Rewards checking accounts are a technology enabled non-maturity account type that has been actively used for several years by banks and credit unions. Currently there are over 500 federally insured financial institutions offering rewards checking accounts. Rewards checking accounts ‘reward’ accountholders with a favorable interest rate on their deposits when they meet specific criteria each statement cycle. They also provide additional benefits such as free online banking and Bill Payment, ATM transaction fee refunds, etc. to these depositors.

An example of the specific account criteria to qualify for the ‘Rewards’ interest rate might include:

1) The accountholder must elect to receive electronic statements
2) The account holder must have one direct deposit or one ach withdrawal from the account each statement cycle
3) The account holder must make 10 debit card transactions per statement cycle

For each account cycle the accountholder meets the criteria, their Rewards checking account might pay the following interest rates:

- 3.50% APY on balances up to and including $25,000
- 1.00% APY on balances over $25,000

If they did not meet all the criteria in a statement cycle, their account might pay the following rate:

- 0.50% APY

While the top tier of interest rate earned on such an account might be 3.50% on a portion of a bank’s deposits, the average interest rate paid on an institutions total portfolio of Rewards Checking accounts would typically be closer to 1.0% to 1.5% in this scenario based on the ratio of qualifying accounts to non-qualifying accounts and average balances held in accounts each statement cycle. These accounts are mutually beneficial to both the depositor and the bank as they provide the depositor with a favorable interest rate and additional benefits in statement cycles they qualify and beneficial to banks in that they provide stable, low-cost, relationship based deposits, reduce expenses (e.g. E-Statements) and increase revenues (e.g. interchange revenues).

In applying Part 337 restrictions to this type of account it has been our bank’s approach to compare the interest rate tiers and qualifying criteria that are being offered by other insured institutions in the bank’s normal market area to our own Rewards Checking account. Thus determining the ‘prevailing market rate’ for this type of account and calculating a rate cap for each tier accordingly.

Recently the FDIC has indicated that it may consider the bank’s ‘Rewards Checking’ accounts as brokered deposits, even though the rates at every tier offered by the bank are within the rate caps as calculated in comparison to the average rates offered by other insured depository institutions offering Rewards Checking in the bank’s normal market area (the prevailing rates for this type of non-maturity depository product).

This is an example of the Regulations not keeping pace with technology, as clearly when taken as a whole, these are low-cost relationship core deposits and not brokered deposits and it was not Congress’ intent to restrict these types of deposits.

Is it the FDIC’s official position to pronounce that all Reward Checking accounts are brokered deposits, even those Reward Checking accounts with rates and terms similar to or below the prevailing rates and terms offered by other institutions for similar or substantially the same Rewards Checking accounts in an institutions normal market area? If yes, why?

## Questions and Responses

1. **Should the FDIC amend its definition of a "market area"? Should the FDIC add a definition of "normal market area"? If so, what should be the definition of an insured depository institution's "normal market area"?**

   Yes. The FDIC should allow for three different definitions for normal market area: 1) National, 2) State, 3) Metropolitan Statistical Area (MSA). These are three readily identifiable and measureable market areas. In the event a bank is not located partially or wholly within a MSA, it could define a local market area and provide its rationale to the FDIC. A bank would be allowed to select its market area/normal market area from these three sets of rates when accepting deposits subject to 337.6.

2. **Should the FDIC create a presumption that the prevailing rate in any "market area" or "normal market area" is the national rate? If not, how should the FDIC determine the prevailing rate in a particular "market area" or "normal market area"?**

   No. As stated in the response to question 1, the FDIC should allow for three different definitions for normal market area: 1) National, 2) State, 3) Metropolitan Statistical Area (MSA). These are three readily identifiable and measureable market areas. In the event a bank is not located partially or wholly within a MSA, it could define a local market area and provide its rationale to the FDIC. A bank would be allowed to select its market area/normal market area from these three sets of rates when accepting deposits subject to 337.6.

3. **Should the FDIC, in addition to publishing a "national rate" that can be used as a proxy for the "normal market area" rate, also provide a schedule that lists prevailing rates for maturities by state for those institutions soliciting deposits only in those states?**

   Yes. As stated in the response to question 1, the FDIC should allow for three different definitions for normal market area: 1) National, 2) State, 3) Metropolitan Statistical Area (MSA). These are three readily identifiable and measureable market areas. In the event a bank is not located partially or wholly within a MSA, it could define a local market area and provide its rationale to the FDIC. A bank would be allowed to select its market area/normal market area from these three sets of rates when accepting deposits subject to 337.6.

4. **Should the FDIC redefine the "national rate"? If so, should the FDIC define the "national rate" as "a simple average of rates paid by all insured depository institutions and branches for which data are available"? If not, how should the FDIC define the "national rate"?**

   Yes the FDIC should redefine the 'national rate'.

   No the FDIC should not define the 'national rate' as "a simple average of rates paid by all insured depository institutions and branches for which data is available." As illustrated above, this methodology generates a 'national rate' that is not reflective of the 'prevailing rates' offered in any market, which is the objective of the rule.

   This is the most difficult, yet most critical issue for the FDIC to resolve. Unfortunately there is no simple answer. I can only offer the following recommendations:

   - The FDIC should determine the highest interest rate offered at each maturity term for each institution regardless of channel of offering and include that rate in its survey (as any logical depositor would select the highest rate for the same maturity time deposit).

   - If an institution offers both an 'in branch' and 'online' rate for the same size and maturity deposit, the FDIC should use the higher of the two rates in its sample (as a logical depositor would choose the higher rate and therefore the higher rate is more indicative of the 'prevailing market rate').

- The FDIC should include the highest rate for each size and maturity regardless of the time deposit type (i.e. standard 'fixed-rate', 'variable rate', 'callable', 'liquid', 'step-rate', 'ready access', or other time deposit variations) and the FDIC should use the maximum attainable rate for its sample.

- The FDIC should use only one rate per institution per measured category (and specifically not use one rate per branch to prevent a distortion of the national average rate by institutions with large branch networks that price 'standard' maturity CDs much lower than prevailing market deposit rates while actively promoting 'odd maturity' time deposits).

- The FDIC should segment non-maturity deposits into the following categories with similar attributes (or other categories as appropriate) and measure the average national rate based on size of the deposit relationship for its rate survey
    - Savings accounts
    - Money market accounts
    - Interest bearing checking accounts
    - E-Accounts (whether savings or money market)
    - Rewards checking accounts

- The FDIC should include the rates offered by Credit Unions with large geographic fields of membership in its rate survey.

- I do not have a firm recommendation on how to address the 'odd-term' time deposit issues at this time, perhaps allowing banks to at least match any public odd term time deposit being offered or an FDIC statement of policy that it will not criticize an institution for matching odd-term maturity rate and terms being offered in the market?

  Alternatively, using a subset of the total population or sample set data could reduce the undue influence of odd-term maturity pricing on the calculated 'national average rate' as contemplated in the response to question 9 below.

**5. Should the definition of the "national rate" be made more flexible? For example, in the event of changes in market conditions, should the FDIC possess the discretion to add or remove a multiplier to the "national rate" (so that the "national rate" might be the "average of rates times 1.20" or some other multiplier)?**

No. Changing the multiplier, and hence changing the 'rules of the game', could have critical ramifications on an institution's liquidity and liquidity planning if they were using one set of regulations to plan by and then those regulations were changed after action had already been taken based on the current multiplier.

It should be noted that changing the multiplier or modifying the rate cap based on the sample size of data used to calculate the 'national average rate' essentially have the same effect. It is my opinion that using a subset of the rate data to calculate the 'national average rate' would lead to a 'national average rate' more reflective of the 'prevailing market rate' and therefore I propose that approach vs. an approach that would modify the multiplier. Please see my response to Question 9.

If the FDIC determines it would prefer to use the 'multiplier' approach, it should change the multiplier only with advanced public notice or comment. For example, if the FDIC was required to provide 6 or 12 months advanced notice, a public comment period, or something of that nature.

**6. Should the FDIC set forth a specific procedure for determining average or prevailing rates? For example, should the FDIC specify that data may be obtained from one or more private companies as to the rates paid by insured depository institutions?**

Yes. This part of setting rate caps is critical. It may be OK to use a data service that provides rate data that generates a 'national average rate' that the FDIC acknowledges is below prevailing market

rates if it is simple to calculate and administer, but, then the FDIC should take the step contemplated in Question 9 and increase the rate cap accordingly (or adjust the 'national rate' with a multiplier as proposed in Question 5). In reality, this may be the best and simplest solution for both the FDIC and financial institutions.

For example, if 'Data Source A' provides an efficient and cost effective means for the FDIC to gather standard term maturity time deposit information, but it is recognized that these rates when aggregated and averaged reflect an average rate that is below prevailing market rates paid on deposits for all the reasons mentioned earlier in this comment, it may be appropriate to use Data Source A, but to increase the rate cap accordingly. An alternative to this approach would be to use a modification of the methodology put forth by the Conference of State Bank Supervisors as detailed in the December 17, 2009 letter to Chairman Bair from Neil Milner, President and CEO of the Conference of State Bank Supervisors RE: Brokered Deposit Rule, Part 337.6 (excerpt below and attached as **Appendix B**)

> *"Second, institutions need greater latitude in the pricing of deposits from the local market. The current rule sets an upper limit of 75 basis points above the average of other banks operating in the area. We recommend the limitation be the average of the top five ratepayers of all firms soliciting in the market area. Banks not seeking deposits for a given maturity will have artificially low pricing, pulling down the average. This makes it very difficult for a bank to price deposits competitively. The average should also include national companies which may not have a physical presence in the market but actively solicit deposits. Limiting the calculation to other local institutions does not fully capture the competitive landscape in a given market."*

The recommendation to select only the top 5 rate payers in any given market was put forth before the FDIC publicly contemplated using a national rate; however the concept behind this recommendation is valid for use with the proposed national rate methodology and will be illustrated in the response to Question 9.

7. **Should the FDIC establish a procedure for disseminating information about average rates or rate caps? For example, should the FDIC post such information on its Web site for use by insured depository institutions and examiners?**

   Yes. The FDIC should post the rates weekly on FDIC Connect.

8. **Should the FDIC establish a procedure through which an insured depository institution could present evidence about the prevailing or average rates in a particular market?**

   Yes.

**9. Under the FDIC's regulations, a rate of interest "significantly exceeds" another rate, or is "significantly higher" than another rate, if the first rate exceeds the second rate by more than 75 basis points. Should the FDIC change this standard?**

Possibly. If as contemplated in the answer presented to Question 6 above, it is determined that the simplest solution for both financial institutions and the FDIC to comply with and measure compliance with the Law and FDI Act is to use data that is readily available, but that both the FDIC and financial institutions acknowledge the proposed methodology generates an 'average national rate' that is substantially below prevailing market rates, it would be appropriate to increase the adjustment rate accordingly (or add a multiplier as contemplated in Question 5 above). Alternatively, using only a subset of the sample data may make it appropriate to leave the rate cap as is or decrease it. For example:

| Simple Average of Deposit Rates | Rate Cap Adjustment |
|---|---|
| All Financial Institutions x branches | + 125 bps |
| All Financial Institutions | + 100 bps |
| Top 75% FI Rates | + 75 bps |
| Top 50% FI Rates | + 50 bps |
| Top 25% FI Rates | + 25 bps |

Using a subset of the depository institutions offering a rate for any given standard rate maturity time deposit should theoretically serve to eliminate downward bias on the sample average from financial institutions that offer artificially low standard maturity deposit rates because they offer odd-term maturities as their regular practice. This would provide an average rate much closer to the true prevailing market rate, accordingly, as lower rate institutions in the sample are removed, the average rate generated by the sample would be more reflective of the true prevailing market rate and accordingly the cap limit over that rate could be decreased to prevent less than well capitalized institutions from offering rates 'substantially higher than prevailing market rates'. The sample composition and rate caps above are presented as an example only, and any final determination should compare the final proposed rate caps to actual market conditions to ensure they reflect the reality of the market and the rate caps should be back-tested against historical data to ensure that the proposed methodology will stand the test of time.

**10. Should the FDIC adopt restrictions in addition to the current restrictions based on a depository institution's capital category?**

No. Today the FDIC can place an institution under Part 337.6 restrictions simply by entering into a written agreement with an institution regardless of the institution's capitalization or risk based capital ratios.

**Additional thoughts:**

The FDIC should consider a less restrictive set of regulations for institutions that would otherwise be considered well-capitalized, minus a written agreement with a capital maintenance provision. For example, an automatic waiver for the acceptance of Reciprocal deposits unless the FDIC shows good cause why the acceptance of such deposits would be an unsafe and unsound banking practice (essentially reversing the burden of proof from the institution to the FDIC for these low-cost relationship based deposits that are 'brokered' in technical definition only). As an example, my institution recently had to decline accepting a $1,000,000 12-month CD at 1.55% APY from a long-time relationship customer because they wished to place the funds through the CDARS reciprocal deposit program (the prevailing market rate for a similar size and maturity deposit in our market was ~2.50% and the rate being offered by FDIC IndyMac was 2.90% at the time). While the bank could apply for a waiver for this transaction, doing so is impractical because the nature of a reciprocal deposit is relationship based. Our Bank has been advised that submitting a brokered deposit waiver could take up to 60 days to process. It is an impossibility to ask a relationship based customer to wait up to 60 days for the bank to provide a response on whether or not it can accept such a deposit and the rate it can pay. This impediment to accepting these low-cost relationship deposits is contrary to both Banks' and the FDIC's best interests.

Thank you for taking the time to review and consider these comments.

Sincerely,

Erik Beguin
CEO
Libertad Bank SSB

# Appendix A

FDIC IndyMac Bank deposit interest rates as listed on www.imb.com on January 29, 2009 for non-maturity deposit accounts. Rates above the proposed rate cap are shaded in Red. These rates would not be in compliance with the rate caps under the proposed new methodology.

**Starter Savings**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1 - 999 | 0.75 | 0.75 |
| 1,000 - 9,999 | 0.75 | 0.75 |
| 10,000 - 24,999 | 1.00 | 1.00 |
| 25,000 - 49,999 | 1.24 | 1.25 |
| 50,000 - 74,999 | 1.49 | 1.50 |
| 75,000 - 99,999 | 1.49 | 1.50 |
| 100,000 - 249,999 | 1.73 | 1.75 |
| 250,000 + | 1.73 | 1.75 |

**Super Savings**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1 - 999 | 0.75 | 0.75 |
| 1,000 - 9,999 | 0.75 | 0.75 |
| 10,000 - 24,999 | 1.00 | 1.00 |
| 25,000 - 49,999 | 1.24 | 1.25 |
| 50,000 - 74,999 | 1.49 | 1.50 |
| 75,000 - 99,999 | 1.49 | 1.50 |
| 100,000 - 249,999 | 1.73 | 1.75 |
| 250,000 + | 1.73 | 1.75 |

**Money Market Savings**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1,000 - 9,999 | 0.75 | 0.75 |
| 10,000 - 24,999 | 1.00 | 1.00 |
| 25,000 - 49,999 | 1.24 | 1.25 |
| 50,000 - 74,999 | 1.49 | 1.50 |
| 75,000 - 99,999 | 1.49 | 1.50 |
| 100,000 - 249,999 | 1.73 | 1.75 |
| 250,000 + | 1.73 | 1.75 |

**E-Money Market**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1,000 - 9,999 | 2.23 | 2.25 |
| 10,000 - 24,999 | 2.23 | 2.25 |
| 25,000 - 49,999 | 2.23 | 2.25 |
| 50,000 - 74,999 | 2.23 | 2.25 |
| 75,000 - 99,000 | 2.23 | 2.25 |
| 100,000 - 249,999 | 2.23 | 2.25 |
| 250,000 + | 2.23 | 2.25 |

**Premium Checking**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1,000 – 4,999 | 0.50 | 0.50 |
| 5,000 – 9,999 | 0.75 | 0.75 |
| 10,000 – 24,999 | 1.00 | 1.00 |
| 25,000+ | 1.24 | 1.25 |

**Ultimate Checking**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1,000 – 9,999 | 0.50 | 0.50 |
| 10,000 – 24,999 | 0.75 | 0.75 |
| 25,000+ | 1.49 | 1.50 |

**Online Retirement Money Market Rates**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1,000 - 9,999 | 0.75 | 0.75 |
| 10,000 - 24,999 | 1.00 | 1.00 |
| 25,000 - 49,999 | 1.24 | 1.25 |
| 50,000 - 74,999 | 1.49 | 1.50 |
| 75,000 - 99,999 | 1.49 | 1.50 |
| 100,000+ | 1.73 | 1.75 |

**Online Retirement Top Tier Money Market Rates**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1,000 - 9,999 | 0.75 | 0.75 |
| 10,000 - 24,999 | 1.00 | 1.00 |
| 25,000 - 49,999 | 1.24 | 1.25 |
| 50,000 - 74,999 | 1.49 | 1.50 |

| | | |
|---|---|---|
| 75,000 - 99,999 | 1.49 | 1.50 |
| 100,000+ | 1.73 | 1.75 |

**Online Retirement Super Savings Rates**

| Balance ($) | Interest Rate (%) | APY (%) |
|---|---|---|
| 1,000 - 9,999 | 0.75 | 0.75 |
| 10,000 - 24,999 | 1.00 | 1.00 |
| 25,000 - 49,999 | 1.24 | 1.25 |
| 50,000 - 74,999 | 1.49 | 1.50 |
| 75,000 - 99,999 | 1.49 | 1.50 |
| 100,000 - 249,999 | 1.73 | 1.75 |
| 250,000 + | 1.73 | 1.75 |

## Appendix B

December 17, 2008

Sheila C. Bair
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

RE: Brokered Deposit Rule, Part 337.6

Dear Chairman Bair:

Over the last several months, state bank regulators have been concerned with the stringent provisions of Part 337.6 of the FDIC's Rules and Regulations as it pertains to brokered deposits. We understand the FDIC has a legal mandate to apply restrictions on the acceptance of brokered deposits when a bank drops below well capitalized. However, we believe the FDIC can make changes to its current rule which will meet the legal requirement while lowering the bank's risk profile in a more orderly manner.

First, we believe institutions falling below well capitalized should be allowed time to reduce their dependence on brokered funds. Absent a waiver from the FDIC, institutions are required to totally stop accepting or renewing brokered deposits. This unnecessarily creates a liquidity problem for the institution and deters management's focus from other safety and soundness issues which may need to be addressed. We recommend banks be given 12 months to unwind the positions, reducing the balances each month by 1/12 of the amount as of the determination date. This will allow the bank to reduce its dependence on brokered deposits over time, helping to ensure adequate liquidity as the bank works to enhance capital and reduce its risk profile.

Second, institutions need greater latitude in the pricing of deposits from the local market. The current rule sets an upper limit of 75 basis points above the average of other banks operating in the area. We recommend the limitation be the average of the top five rate-payers of all firms soliciting in the market area. Banks not seeking deposits for a given maturity will have artificially low pricing, pulling down the average. This makes it very difficult for a bank to price deposits competitively. The average should also include national companies which may not have a physical presence in the market but actively solicit deposits. Limiting the calculation to other local institutions does not fully capture the competitive landscape in a given market.

We believe these changes will give institutions an opportunity to gradually and safely reduce their use of brokered deposits, while allowing the FDIC to meet your statutory requirements and supervisory needs.

CONFERENCE OF STATE BANK SUPERVISORS
1155 Connecticut Ave., NW, 5th Floor • Washington DC 20036-4306 • (202) 296-2840 • Fax: (202) 296-1928

Thank you for your time and consideration. Please feel free to contact me if you would like to discuss this further.

Best personal regards,

Neil Milner
President and CEO