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Financing America's Economy

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January 3, 2011

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

Re: **Assessments, Assessment Base and Rates, and Large Bank Pricing**

File Numbers: FR Docs. 2010-29137, 2010-29138

Ladies and Gentlemen:

The Financial Services Roundtable (the "Roundtable[1]") appreciates the opportunity to provide the Federal Deposit Insurance Corporation (the "FDIC") with its comments regarding implementation of the new assessment base and assessment rates applicable to insured depository institutions ("IDIs"), as set forth in the FDIC's Notices of Proposed Rulemaking published in the Federal Register on November 24, 2010 (the "Proposed Assessment Rule"[2] and the "Proposed Large Bank Pricing Rule" [3]).

The Roundtable is composed of large, integrated financial services companies that finance most of the nation's economy and are critical to its sustained growth. The Roundtable is the premier executive forum for the leaders of the financial services industry, leads in industry best practices, and provides a positive industry perspective on legislative and regulatory policy. The Roundtable believes the competitive marketplace should largely govern the delivery of products and services, and that regulation should mitigate the risk and enhance the stability of the banking system.

The Roundtable once again expresses its appreciation for the FDIC's decision to forego the uniform 3 basis point increase in assessment rates previously scheduled to go

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1 The Financial Services Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Roundtable member companies provide fuel for America's economic engine, accounting directly for $74.7 trillion in managed assets, $1.1 trillion in revenue, and 2.3 million jobs.

2 75 Fed. Reg. 72582 (November 24, 2010).

3 75 Fed. Reg. 64173 (November 24, 2010).

into effect on January 1, 2011.[4] The Roundtable further appreciates the opportunity to comment on the proposed assessment base and rates applicable to IDIs, issues of great importance to both IDIs themselves and the economy as a whole. In this letter, the Roundtable offers comments on both the Proposed Assessment Rule and the Proposed Large Bank Pricing Rule.

Background and Proposals

Section 331(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act")[5] requires the FDIC to amend its regulations to redefine the insurance assessment base for IDIs, ending the previous practice of basing assessments on an IDI's domestic deposit base. The Proposed Assessment Rule is intended to implement this required statutory change in the assessment base. Under Section 331(b), the FDIC is required to define the assessment base applicable to IDIs as the average consolidated total assets of the IDI minus the average tangible equity of the IDI during the assessment period.[6] Section 331(b) also provides that the FDIC should make an adjustment to the assessment base for custodial banks and banker's banks. The Proposed Assessment Rule provides for an adjustment for custodial banks and banker's banks. Under the Proposed Assessment Rule, a banker's bank would be able to exclude from its assessment base (i) the daily average reserve balances passed through to the Federal Reserve, (ii) the daily average reserve balances held at the Federal Reserve for its own account, and (iii) the daily average amount of its Federal funds sold. A custodial bank would be able to exclude highly liquid, short-term assets from its assessment base. In designing the Proposed Assessment Rule, the FDIC has stated that it intends it to be revenue neutral as compared to the October Notice of Proposed Rulemaking on Assessment Dividends, Assessment Rates, and the Designated Reserve Ratio.[7]

Concurrently, the Proposed Large Bank Pricing Rule eliminates the existing system of risk categories for IDIs with assets of $10 billion or more ("large IDIs") which was established in 2006 to calculate assessment rates. The FDIC instead proposes to use a new "scorecard" method to calculate assessment rates for large IDIs, while retaining the risk category system for calculating assessment rates for small institutions. The large IDI scorecard uses risk measures to produce two scores, a performance score and a loss severity score, which are ultimately combined into a total score. Under the Proposed Large Bank Pricing Rule, the FDIC would have the discretion to adjust the total score up or down by a maximum of 15 points, based upon significant risk factors not adequately captured in the

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4 *See* Letter from Richard Whiting, Executive Director and General Counsel, The Financial Services Roundtable, to Robert Feldman, Executive Secretary, Federal Deposit Insurance Corporation (November 26, 2010) (available at http://www.fdic.gov/regulations/laws/federal/2010/10c05AD63.PDF).

5 Pub L. No. 111-203, § 331(b), 124 Stat. 1376 (2010).

6 Section 331(b) of the Dodd-Frank Act does not define the term "average consolidated total assets" or the term "average tangible equity." The Proposed Assessment Rule provides a methodology for calculating "average consolidated total assets" and "average tangible equity." It also provides a definition of the term "tangible equity" as Tier 1 Capital.

7 75 Fed. Reg. 66272 (October 27, 2010).

scorecard. Based on the results of the scorecard analysis, a large IDI would be subject to a minimum base assessment rate of between 5 and 35 basis points. The large IDI base assessment rate would be subject to further adjustment based on an IDI's unsecured debt, brokered deposits, and holdings of debt issued by another IDI.

Our specific comments regarding the proposed rules on assessments and large bank pricing follow.

Effect on Large IDIs

The Roundtable believes that the FDIC must consider the different parts of its assessments regulations and changes together. The changed assessment base and the new scorecard approach to large IDIs would significantly shift the overall burden of assessments to larger institutions (those with over $10 billion in assets), and these changes must also be considered in light of the "offset" provided for in the Dodd-Frank Act,[8] which the FDIC has suggested will shift the overall burden of assessments to larger institutions even more.

The Roundtable believes that the FDIC's statement that large IDIs "would pay assessments at least 5 percent higher than currently" likely underestimates the effect on large IDIs. We believe that implementation of the Proposed Large Bank Pricing Rule as currently formulated would likely lead to increases in assessments much greater than 5% for large IDIs, with some large IDIs experiencing *significantly* greater increases in assessments. The Roundtable believes it is of great importance that the FDIC understand the effect that significantly increased assessment payments will have on capital availability in the overall economy, especially when the large IDIs subject to the increased assessments account for much of the lending activity in the overall economy. Excessive assessments could remove billions of dollars in capital from the most significant engines of economic recovery available to the country.

While Section 331(b) of the Dodd-Frank Act directs the FDIC to change its assessment base from a domestic deposit base to a total asset base, the Dodd-Frank Act does not nullify the requirement in Section 7(b)(1)(A) of the Federal Deposit Insurance Act that there must be a "risk-based assessment system" or the requirement in Section 7(b)(1)9C) that the system for calculating an IDI's assessment must be based, *inter alia*, on the probability that the deposit insurance system (the "DIF") will incur a loss "with respect to the institution."[9] If the assessment system simply shifts the burden of assessments to larger IDIs, rather than assessing all IDIs based on the risk they pose to the DIF, the assessment system would not be consistent with this statutory mandate. The Roundtable believes a more rigorous showing must be made as to how the FDIC's final rules on assessments and large bank pricing, as well as future rules on assessments (including the "offset" provided for in the Dodd-Frank Act), appropriately assess large IDIs based on the risk they pose to the DIF.

[8] Section 334(e) of the Dodd-Frank Act.
[9] 12 U.S.C. § 1817(b)(1)(A)(C).

A holistic analysis of the proposed rules indicates that under the new proposed assessment base large IDIs will be subject to a significantly higher assessment burden, both quantitatively and qualitatively. In quantitative terms, the FDIC explicitly states that the proposed rules will lower assessments for IDIs with less than $10 billion in assets and increase assessments for IDIs with more than $10 billion in assets.[10] From a qualitative perspective, the new assessment scorecard places large IDIs in an entirely separate assessment category, a category that subjects these institutions to assessment rates that do not, on a relative basis, match the risk of loss that these IDIs pose to the DIF. For example, the proposed assessment schedule would assess large IDIs at a maximum possible rate higher than those applicable to any other category of IDI, with the exception of Risk Category IV IDIs. The FDIC characterizes Risk Category IV IDIs as small institutions that are "Undercapitalized." It is incongruous that under the proposed rules a healthy, well-capitalized large IDI could be assessed at the same maximum possible rate as an IDI that failed to meet the minimum Tier 1 risk-based capital ratio.

The FDIC states that the proposed assessment base and revised rates will yield outcomes that are "revenue neutral" relative to the assessment system proposed in October.[11] Given that the October NPR stands as the empirical basis of the FDIC's assertions about revenue neutrality, the Roundtable questions the ability to determine that the *new* proposed assessment system for large IDIs, one based on significantly different data than the old one, will yield the same revenue outcomes as would have been the case under the October NPR.

<u>The New Assessment Base and the Large IDI Scorecard</u>

The Roundtable believes that several elements of the new assessment base definition and large IDI scorecard deserve specific comment.

<u>First</u>, the Roundtable urges the FDIC to either exclude goodwill from the assets making up the assessment base, or provide for a goodwill-based adjustment that allows IDIs to reduce their assessment rate based on the amount of goodwill in their asset base. Providing for a goodwill-based elimination or adjustment would avoid penalizing IDIs for assets that pose no additional risk of loss to the DIF, and would also be consistent with the FDIC's statutory mandate to conduct risk-based assessments.

Section 331(b) of the Dodd-Frank Act defines the new assessment base to be consolidated total assets minus tangible equity, both tangible and intangible assets (such as

[10] 75 Fed. Reg. at 72589 ("[O]verall, the proposed rates and proposed assessment base should have no effect on the capital and earnings of the banking industry, although the proposed rates would affect the earnings and capital of individual institutions. The great majority of institutions of all sizes would pay assessments at least 5 percent lower than currently and would thus have higher earnings and capital. However, about 36 percent of large institutions (those with greater than $10 billion in assets *would pay assessments at least 5 percent higher than currently*") (emphasis added).

[11] Id. at 72588 ("the proposed rate schedules are intended to be revenue neutral *in that they anticipate collecting approximately the same amount of assessment revenue over the same period as the rate schedules presented in the October NPR*") (emphasis added).

goodwill) will be part of the assessment base. Unlike the case with other assets, a loss in value or write-off of goodwill poses no additional risk of loss to the FDIC in the event of a failure of an insured institution. Goodwill is not an asset for which the FDIC as receiver could have any expectation of recovery. For these and other reasons, goodwill is deducted when calculating regulatory capital. Goodwill is also deducted from the total asset base when calculating regulatory capital.[12] This treatment ensures a fair and symmetrical approach to goodwill. We believe that a similar symmetrical approach should be taken in the Proposed Assessment Rule. The Roundtable also asks the FDIC to consider the possible unintended consequences of including goodwill as part of the assessment base, specifically the potential result that inclusion would violate the general requirement that the assessment system be risk-based. For example, the asset base of two IDIs that plan to merge pose the same risk as the merged IDIs, yet any goodwill created by the merger would increase the IDI's assessment base, and consequently the premium it pays. In addition, IDIs that write off their goodwill through an impairment charge, possibly because they are riskier and their earnings cannot support the goodwill, would have lower assessments and pay less premiums than IDIs that are stronger and can support their goodwill. Another unintended consequence of the Proposed Assessment Rule would be to create a disincentive to IDIs considering acquisitions, including acquisitions of distressed banks.

The Roundtable also urges the FDIC to consider whether an exclusion for inter-company lending between sister banks is warranted, as assessing assets related to such transactions effectively amounts to double-counting of assets for assessment purposes. Although the FDIC has stated that it will continue to conduct assessment analysis on an individual IDI basis, continuing to do so in this context will result in double-counting because of the new assessment base.

Second, we have concerns with the proposed adjustments for banker's banks and custodial banks. With respect to the banker's bank adjustment, the adjustment may make it prohibitively costly for banks that are assessed on the amount of Federal funds sold to compete with banks that are not, leading to concerns that the Federal funds market will no longer have sufficient participants to meet existing demand. With respect to the custodial bank adjustment, although the Roundtable is supportive of the FDIC's approach of excluding highly liquid assets from the assessment base for purposes of the adjustment, the Roundtable is concerned with the standard of "a stated maturity of 30 days or less" constituting the dividing line between highly liquid and non-highly liquid assets. Because the maturity of an asset is not the only indicator of the asset's liquidity, the FDIC should broaden the definition of "highly liquid assets" so that the definition looks to a variety of asset characteristics, including asset maturity, for purposes of the liquidity determination.

Third, the large IDI scorecard fails to properly account for the changed risk characteristics of the new assessment base *vs.* the deposit-based assessment base. Because

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[12] 12 C.F.R. Appendix A to Part 325 n. 6.

the large IDI scorecard encompasses much of the methodology of the April NPR[13] on large banks (which assumed that the amount of assessments would be arrived at by multiplying the base assessment rate by domestic deposits), in order to properly encapsulate the change in risk associated with the new assessment base, the methodology to arrive at the new base assessment rate should have changed as well. However, the methodology in the large IDI scorecard is substantially similar to that in the April NPR, raising the question as to how the new assessment methodology can be "risk-based" if it has not changed significantly despite the new assessment base.

Fourth, assessments under the large IDI scorecard bear little quantitative or methodological connection to an IDI's deposit base, making it possible that a large IDI could pay assessment premiums *greater* than the amount of its total deposit base. For example, a banker's bank with $5 billion in assets (but only $.5 million in deposits) could, if assessed at a rate of 5 basis points, pay $2.5 million in assessments, an amount greater than its deposit base. To avoid such incongruous results, a large IDI's assessment premium should be capped at a percentage of the IDI's deposit base. Barring a cap, the assessment base should be recalibrated to define a specific proportional relationship between an IDI's assessment premium and its deposit base, so that assessment calculations are more closely tied to actual insured deposits, and hence to the FDIC's actual risk of loss in the event of an IDI's failure.

Fifth, although the scorecard clearly seeks to assess a large IDI at a higher rate based on the perceived risk level of its asset base, the scorecard calculations fail to provide any significant countervailing adjustments for risk mitigating elements that enhance the quality of underlying assets, such as hedging arrangements, collateralization, insurance, asset underwriting standards, or the quality of IDI mortgage originating processes. The scorecard thus fails to accurately capture the risk associated with an IDI's asset base. Indeed, this failure to include asset quality in the assessment calculation is at odds with other regulatory approaches to bank capital regulation. The Basel Committee, Federal Reserve, and the Office of the Comptroller of the Currency all subscribe to risk-weighted assessments (rather than notional determinations) of asset quality. The Roundtable thus proposes that the FDIC integrate an adjustment into the scorecard that encompasses existing risk mitigants in an IDI's asset base. Such adjustments will allow the FDIC to better implement its statutorily required approach of accurate risk-based assessment of large IDIs.

Sixth, the Roundtable believes that elements of both the Performance Score and Loss Severity Score require recalibration and revision. For example, key elements of the Performance Score are based on a subjective, rather than objective analysis of risk of failure, and thus key weights assigned to the various sub-factors in the Performance Score need more careful calibration based on actual experiences associated with large IDIs. In addition, the Loss Severity Score must be calibrated relative to the loss to the DIF,

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[13] 75 Fed. Reg. 23516 (May 3, 2010).

assuming that the IDI fails. The Roundtable believes that the Loss Severity Score (i) should be based exclusively on the amount by which the assets, after proper haircuts, fail to cover deposits, and (ii) should be expanded in its range, so that the Loss Severity Score accurately captures situations where an IDI poses little or no risk to the DIF. In this vein, the Roundtable believes that there is little objective basis for placing a 25% weight on an extraneous factor, the ratio of noncore funding to total liabilities. Indeed, the first element of the Loss Severity Score, the loss severity measure, contains all the information necessary to determine loss given default. Thus, the Roundtable believes that the ratio of noncore funding to total liabilities should be eliminated from the Loss Severity Score entirely.

Seventh, the Roundtable is troubled that the proposed rules retain the proposal from the April NPR to allow the FDIC to make discretionary adjustments of up to 15 points "based upon significant risk factors that are not adequately captured in the appropriate scorecard."[14] As was the case with the April NPR, such wide latitude for such a large discretionary adjustment is "too large, too subjective, and not transparent."[15] Significant discretion for adjustment makes IDIs unable to plan their operations, as billions of dollars in capital may be diverted away from bank balance sheets as a result of the discretionary adjustment.

Eighth, the Roundtable believes that the complexity of the scorecard makes it extremely difficult for IDIs, as well as the FDIC, to predict what level of assessments will actually be paid into the DIF. This complexity reduces needed certainty in the banking industry, makes the assessment system significantly more costly to administer, and actually detracts from, rather than enhances, the ability of the FDIC to assess IDIs based on risk.

Finally, the Roundtable believes that further clarity is needed on numerous elements of the scorecard, including (i) whether the definition of "nontraditional mortgage loan" for purposes of the concentration measure calculation will include mortgages that have long been integral elements of the mortgage market, such as adjustable rate ("ARM") or limited period interest-only mortgages, (ii) whether the use of FICO scores for purposes of the subprime consumer loan element of the concentration measure will reflect changes in FICO score calculation over time, and (iii) what "idiosyncratic or other relevant risk factors not included in the scorecard" the FDIC will look to when determining the 15 point discretionary adjustment to an IDI's total score. In addition to providing IDIs with certainty essential to structuring operations in light of the new assessment base, further clarity as to scorecard components will reduce the potential for inequitable and unpredictable assessments across large IDIs, hence reducing the risk and enhancing the safety and soundness of the banking system.

The Large IDI Scorecard: Performance Score

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[14] 75 Fed. Reg. at 72641.
[15] *See* 75 Fed. Reg. at 72623.

The Roundtable believes that the performance score component of the large IDI scorecard suffers from several theoretical and methodological flaws.

With respect to the concentration measure component of the ability to withstand asset-related stress measure, the FDIC's creation of the four risk that which make up the concentration measure (construction and land development loans, leveraged loans, nontraditional mortgage loans, and subprime consumer loans) is inconsistent with current assessment practice. Besides the fact that calculations of exposures in these four risk areas are not regularly incorporated into Call Report data, application of these measures across IDIs with highly divergent product lines and loan portfolios likely will lead to inconsistent assessments. Given the potential for inconsistency introduced by the concentration measure, the Roundtable believes that it should be removed from the scorecard.

If the FDIC nevertheless intends to retain the concentration measure as an element of the performance score, the Roundtable recommends that (i) the FDIC reduce the 35% weight assigned to the concentration measure in the ability to withstand asset-related stress calculation, (ii) the FDIC average, rather than take the greater of, the criticized and classified items and underperforming assets scores that compose the numerator of the credit quality measure, and (iii) the growth-adjusted portfolio concentrations element of the concentration measure exclude the impact of FAS 166/167 asset consolidation, as this consolidation was simply the result of a one-time accounting rule change, and including the impact of these accounting changes would lead to the false conclusion that the overall rate of growth in certain portfolios or business activities is far higher than it actually is. In addition, the Roundtable notes that some of the elements of the concentration measure are not adequately risk-based. For example, the mere fact that a mortgage secures a consumer or commercial construction loan or is "interest-only" does not indicate the mortgage's risk or potential for default.

With respect to the balance sheet liquidity ratio component of the ability to withstand funding-related stress measure, the Roundtable believes that, in addition to the listed assets that make up the ratio, IDIs should also receive credit for holding agency-backed available-for-sale residential mortgage securities, as markets for these assets are highly liquid. In this regard, it should be noted that the Basel Committee on Banking Supervision includes such securities for purposes of liquidity ratio calculations. Further, the Roundtable believes that bank deposit accounts owned by the bank's parent entity should not be treated like other deposits. Because these accounts typically reflect cash raised in the form of long-term unsecured debt, they should not be subject to high runoff rates.

Finally, the Roundtable notes that the methodology utilized to create the performance score is based on the FDIC's recent experience and judgment, as opposed to empirical validation of sound statistical relationships. Because nearly all of the failure data that the FDIC has relied on to set the relationships in the performance score calculation are derived from IDIs with assets of less than $10 billion, it is difficult to understand how the analysis underlying the performance score can reflect or provide predictive insight into failures of large IDIs. Indeed, only 29 IDIs failed between 2000 and 2004, and none failed in 2005 and 2006. Because (i) the FDIC's "recent experience" covers the 2005-2009 period, (ii) the FDIC's analysis consists of forced ranking of IDIs based on subjective assessments of risk, and (iii) the dependent variables against which the performance score factors are selected are whether the IDI failed before year-end 2009 or was "deemed to have failed"[16], the IDI assessment process is not properly based on a methodology with robust statistical support.

The Large IDI Scorecard: Loss Severity Score

The Roundtable also believes that the loss severity score component of the large IDI scorecard suffers from theoretical and methodological flaws.

First, the Roundtable believes that the methodology utilized by the FDIC to arrive at the loss severity score is not supported by sufficient data. Because the Loss Severity Score represents a "quantitative" valuation of loss at default, it is curious that there is (i) no empirical data given in support of the assumed asset loss and runoff rates that compose the loss severity measure, (ii) no data to support the use of a ratio of non-core funding to total liabilities as part of the loss severity score, other than the blanket assertion that "heavy reliance on secured liabilities or other types of noncore funding reduce an IDI's potential franchise value,"[17] and (iii) no robust statistical analysis, benchmarking, or back testing underlying the derivation of the loss severity score.

Given the lack of statistical analysis underlying the loss severity score, the Roundtable recommends that the loss severity score be calculated in a different manner, such that it is truly calibrated relative to the loss to the DIF, assuming that the IDI fails. Specifically, the minimum range of the loss severity score range should be expanded, such that the score remains close to zero where no risk to the DIF can be found, but more importantly, the loss severity score should be based *exclusively* on the amount by which assets (after factoring in proper haircuts) would fail to cover deposits. Thus, because there is no data to support the use of a ratio of non-core funding to total liabilities as part of the loss severity score, the Roundtable believes that the ratio of noncore funding to total liabilities should be eliminated from the score. In addition, (i) the FDIC's assumption of a 32 percent growth in insured deposits prior to IDI failure is unrealistic for a large IDI, (ii) the assumption of *pro rata* growth in every asset category funded by deposit growth is also unrealistic, as a troubled IDI would more likely, allocate deposit growth to short-term securities, securities that would have a much lower loss rate, (iii) the "Revolving Home Equity Loans" category in the asset loss rate assumptions table fails to adequately differentiate between first and second lien positions, and should be adjusted so that revolving home equity first liens are assigned a 19.4 percent loss rate and junior liens are

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16 The analysis supporting the Proposed Large Bank Pricing Rule treats banks that received significant government support as "failed" institutions. This methodology does not comport with the requirement for an assessment system that is based on loss or probability of loss to the DIF.

17 75 Fed. Reg. at 72618.

assigned a 41 percent loss rate (similar to the "1-4 Family Closed-End" categories), (iv) the "All Other Loans" category in the asset loss rate assumptions table should be adjusted so that specific categories of non-domestic loans (such as revolving home equity and residential loans) can be assigned specific risk weights, just as with the domestic loans in the same table, and (v) the "Other Assets" category in the asset loss rate assumptions table is insufficiently granular, in that it assumes a single universal 75 percent loss factor for many different categories of loans. Many IDIs have assets, such as bank-owned life insurance, which carry loss rates of between 0 and 15 percent, and yet such assets would be assigned a loss rate of 75 percent under the proposed rules.

Proposed Adjustments to Base Assessment Rates

The Roundtable notes that distinguishing between short and long-term debt by looking to the debt instrument's time until maturity, the unsecured debt adjustment actually disincentivizes IDIs from issuing long-term unsecured debt. In order to maintain an IDI's incentive to issue long-term unsecured debt, the Roundtable recommends that the definition of "long-term unsecured debt" be changed to focus on the instrument's *original* maturity (such as a maturity of greater than two years), rather than have an IDI lose the benefit of the unsecured debt adjustment once the instrument has a remaining maturity of less than a year. If the FDIC continues to delineate between short and long-term debt based on remaining maturity, the Roundtable recommends that the original adjustment be increased to compensate for the definition's incentive-reducing effects.

With respect to the proposed depository institution debt adjustment, the Roundtable questions the FDIC's assumption that "Although issuance of unsecured debt by an IDI lessens the potential loss to the DIF in the event of an IDI's failure, when this debt is held by other IDIs, the overall risk to the DIF is not reduced."[18] To the contrary, modern portfolio theory recognizes that if a firm's debt is held by multiple investors, the effect of the firm's default on any individual investor's portfolio will be mitigated if the investor holds the debt as part of a diversified portfolio of assets.[19] The Roundtable proposes that the baseline depository institution debt adjustment therefore be reduced from 50 basis points to reflect the portfolio-based risk reduction that comes from multiple IDIs holding the debt of an individual IDI. In addition, the Roundtable requests clarification as to whether or not the depository institution debt adjustment will include term certificates of deposit and Federal funds sold.

With respect to the brokered deposit adjustment, the Roundtable questions why the brokered deposit adjustment would not apply to small Risk Category I IDIs, and yet would still be applicable to large IDIs. The FDIC provides no justification for imposing the brokered deposit adjustment on large IDIs, but not on Risk Category I IDIs. Although the FDIC perhaps contemplates the exemption for small Risk Category I IDIs as a continuance of the previous approach, this approach no longer makes sense in light of the changes to the

[18] 75 Fed. Reg. at 72586.

[19] See William B. Bratton, Corporate Finance: Cases and Materials 91-94 (6th ed. 2008).

way the assessment base is calculated. The Roundtable therefore proposes that the exclusion for small Risk Category I institutions be eliminated, and that an empirical basis be shown for the FDIC's decision to implement the brokered deposit adjustment when brokered deposits exceed ten percent of an IDI's assessment base.

The proposed language of the brokered deposit adjustment seems a carryover from previous FDIC engagements with the issue, and thus clarity is particularly important in this context. IDI utilization of (i) brokered deposits from affiliate relationships, (ii) brokered deposits facilitated through exclusive agents or affinity arrangements, and (iii) brokered deposits subject to risk-mitigating contractual commitments are merely three examples where brokered deposits can actually mitigate the risk of an IDI. Indeed, special-purpose banks, such as credit card banks, utilize brokered deposits as an alternative to building special branch networks, rather than as a means of rapid growth. The Roundtable therefore requests clarification and a more precise definition of brokered deposits, one that provides additional guidance on brokered deposits and recognizes the risk mitigating, rather than risk enhancing, characteristics of certain categories of brokered deposits. Indeed, because the FDIC will further study the distinction between core and brokered deposits, it seems inappropriate to penalize all brokered deposits before the FDIC has studied the issue sufficiently.

The Offset Requirement and the Impact of the New Assessment Base

Section 334 of the Dodd-Frank Act requires that in setting assessments, the FDIC offset the effect of increasing the DIF minimum reserve ratio to 1.35 percent on insured depository institutions with total consolidated assets of less than $10 billion. The FDIC plans to "postpone[] until 2011 rulemaking regarding the method that will be used to effectuate the offset."[20] Because large IDIs will pay 80 percent of total assessments under the new assessment system compared with 70 percent of total assessments under the deposit-based assessment system, the net effect of the proposed rules will be to shift the assessment burden to large IDIs. Although the new assessment base is required by the Dodd-Frank Act, the Dodd-Frank Act does not permit the FDIC simply to shift the burden of payments under the new assessment system to large IDIs, unless such shifts are due to an increased risk of loss that large IDIs pose to the DIF. The Roundtable believes that the FDIC has not adequately demonstrated that the additional shift of assessment payments to large IDIs is based on increased risk of loss to the DIF. Hence, at a minimum, any increases in large IDI assessments resulting from implementation of the proposed rules should be deemed to constitute the FDIC's implementation of the Section 334 offset requirement.

Conclusion

The Roundtable believes that considering together all the proposed changes to the assessment rules (and the future implementation of the "offset") would result in an

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[20] 75 Fed. Reg. 66272, 66273 (October 27, 2010).

extraordinary shift in the burden of assessments to larger institutions – a shift that has not been shown to be consistent with the statutory requirement that the assessments be risk-based. To be properly risk-based, the assessments rules should be based on robust statistical data, and reflect the true risk of loss that individual IDIs, both large and small, pose to the DIF. We have made many recommendations in this letter to more clearly and equitably achieve this mandate, and urge the FDIC to accord them serious consideration. Again, the Roundtable reiterates its appreciation to the FDIC for the opportunity to comment on the proposed rules on assessments and large bank pricing. If you have any questions, please feel free to contact me or Brian Tate at (202) 289-4322.

Sincerely,

Richard M. Whiting

Richard Whiting
Executive Director and General Counsel