May 31, 2011

Via Electronic Delivery

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Attention: Comments

Re: Proposed Assessment Rate Adjustment Guidelines for Large and Highly Complex Institutions

Dear Mr. Feldman:

The Clearing House Association L.L.C. ("*The Clearing House*"),[1] an association of major commercial banks, appreciates the opportunity to comment on the Proposed Assessment Rate Adjustment Guidelines for Large and Highly Complex Institutions[2] (the

1 Established in 1853, The Clearing House is the nation's oldest banking association and payments company. It is owned by the world's largest commercial banks, which collectively employ 1.4 million people in the United States and hold more than half of all U.S. deposits. The Clearing House Association is a nonpartisan advocacy organization representing – through regulatory comment letters, amicus briefs and white papers – the interests of its owner banks on a variety of systemically important banking issues. Its affiliate, The Clearing House Payments Company L.L.C., provides payment, clearing and settlement services to its member banks and other financial institutions, clearing almost $2 trillion daily and representing nearly half of the automated-clearing-house, funds-transfer and check-image payments made in the U.S. *See* The Clearing House's web page at www.theclearinghouse.org for additional information.

2 A ''Highly Complex Institution'' is defined as: (1) an insured depository institution (excluding a credit card bank) that has had $50 billion or more in total assets for at least four consecutive quarters and that either is controlled by a U.S. parent holding company that has had $500 billion or more in total assets for four consecutive quarters, or is controlled by one or more intermediate U.S. parent holding companies that are controlled by a U.S. holding company that has had $500 billion or more in assets for four consecutive quarters, or (2) a processing bank or trust company, whose last three years' non-lending interest income, fiduciary revenues, and investment banking fees, combined, exceed 50% of total revenues (and its last three years' fiduciary revenues are non-zero), whose total fiduciary assets total $500 billion or more, and whose total assets for at least four consecutive quarters have been $10 billion or more. A "Large Institution" is defined as an insured depository institution that: (1) had assets of $10 billion or more as of

"*Guidelines*") issued by the Federal Deposit Insurance Corporation ("*FDIC*") on April 12, 2011. 76 Fed. Reg. 21,256 (April 15, 2011). On February 7, 2011, the FDIC issued a final rule (the "*Final Rule*") adopting a new methodology for determining deposit insurance assessment rates for Large and Highly Complex Institutions (the "*New Assessment System*"). 76 Fed Reg. 10, 672 (Feb. 25, 2011). The New Assessment System introduced a scorecard method to calculate assessment rates for Large and Highly Complex Institutions, under which each institution will receive a total score that cannot be greater than 90 or less than 30.

The New Assessment System also provided the FDIC with discretionary authority to adjust a Large or Highly Complex Institution's total score by up to 15 points, either upward or downward, provided that the resultant score is not greater than 90 or less than 30. The proposed Guidelines were issued to clarify the analytical process the FDIC intends to follow to make adjustments under this discretionary authority. The Guidelines set out how the FDIC proposes to determine whether to make an adjustment, the size of any adjustment and the FDIC's procedure for notifying an institution of any proposed adjustment.

The Clearing House appreciates the effort that the FDIC has undertaken to solicit public comment on the proposed Guidelines. As we previously indicated in our comment letter on the proposal that became the Final Rule submitted to the FDIC on January 3, 2011 (the "*January 3 Comment Letter*"), however, we believe the Final Rule and the proposed Guidelines give the FDIC excessively broad discretionary authority to adjust a Large or Highly Complex Institution's total score. This creates undue uncertainty and potentially wide variations in assessments that may undermine the disciplines intended by the FDIC in the Final Rule.

We respectfully submit the following recommendations and urge the FDIC to consider these recommendations when adopting the final guidelines:

- Upward adjustments under the FDIC's discretionary adjustment authority should be made rarely and only in clearly compelling circumstances.

- The FDIC should limit the overall upward percentage change as a result of an adjustment to no more than 10% of an institution's total assessment obligation.

- The final guidelines should require concurrence by an institution's primary regulator for any upward adjustment.

December 31, 2006 (unless, by reporting assets of less than $10 billion for four consecutive quarters since then, it has become a small institution); or (2) had assets of less than $10 billion as of December 31, 2006, but has since had $10 billion or more in total assets for at least four consecutive quarters, whether or not the institution is new. *See* 76 Fed. Reg. 21,256, 21,256 (April 15, 2011).

- The FDIC should provide a definitive statement of complementary risk measures and qualitative risk considerations.

- The list of qualitative risk factors should be expanded to include certain factors relating to loss severity, and a downward adjustment should be made if a large institution[3] meets certain criteria, including, for example, a higher level of subordinated liabilities to the FDIC's claim than the norm.

- The FDIC should not make any upward adjustment for the second quarter of 2011 under the Guidelines when adopted.

I. Upward Adjustments for Large Institutions Should Be Made Only in Clearly Compelling Circumstances

The FDIC's discretionary authority to adjust an institution's total score by up to 15 points, either upward or downward, in light of the total score range of 30-90, is excessively broad and can have a very substantial impact on an institution's overall assessment obligation. As indicated in the January 3 Comment Letter, for large institutions, an increase in total score by 15 points would translate into an approximately 60% increase in the assessment fee for such institutions on average. In addition, because of the non-linear relationship between the score and the assessment rate, an adjustment to a total score has significantly more effect in raising an institution's overall assessment than in decreasing an institution's overall assessment. For example, a downward adjustment of a large institution's total score by 15 points would reduce the institution's assessment rates by six basis points on average. Conversely, an upward adjustment by 15 points would increase the institution's assessment rates by nine basis points on average. The excessively broad range of adjustment authority and substantial impact on an institution's total assessment obligation caused by the FDIC's discretionary adjustment authority creates additional uncertainty and makes it impossible for an institution to predict, monitor and manage its assessment obligation.

In addition, as discussed in the January 3 Comment Letter, the New Assessment System adopted by the Final Rule includes a pronounced bias against Highly Complex Institutions. Their assessment costs increased by approximately 50% at the same time that the vast majority of banks experienced significant reductions in such costs. Among other things, the loss severity measure is limited in its impact by the arbitrary scaling, and the loss severity score does not adequately take into account the loss absorption function of statutorily subordinated liabilities.

[3] For the purposes of this comment letter, large institutions include both Highly Complex Institutions and Large Institutions unless otherwise specified.

This existing bias could be exacerbated by any upward adjustment. Accordingly, we believe that upward adjustments should be made only in clear and compelling circumstances and that this approach should be explicitly recognized in the final guidelines.

There is one other, more general, reason that upward adjustments should be so limited. The disclosure of such an adjustment, which, as the FDIC recognizes, would be "idiosyncratic," could create investor and even funding concerns, exaggerating any problems that the depository institution may be experiencing. We recognize that the FDIC should not be deterred from an appropriate adjustment by potential market impact, but that potential should mandate a clear and convincing case for an adjustment.

II. The FDIC Should Limit the Upward Discretionary Adjustment to No More Than 10% of an Institution's Total Assessment

According to the Final Rule, as a result of the recent financial crisis, the FDIC is better able to measure and price for risks that resulted in failures and losses at large institutions.[4] Furthermore, as indicated in the proposed Guidelines, the FDIC believes that the total score produced by the scorecard under the New Assessment System would reflect an institution's overall risk relative to other large institutions in most cases.[5] Therefore, under the FDIC's own analysis, further adjustments to the total assessment for a large institution generally should be unnecessary.

Consequently, the FDIC should not use the discretionary adjustment to make substantial upward changes to a large institution's deposit insurance assessment. We believe such upward discretionary adjustments should be limited to no more than 10% of an institution's total assessment obligation for the affected period.

III. The FDIC Should Defer to an Institution's Primary Regulator for any Proposed Upward Adjustment

Because of the market, reputational and cost impact on an institution's assessment obligation caused by an upward adjustment, concurrence by (as opposed to just consultation with) an institution's primary banking regulator should be required for any upward adjustment under this authority. Given the discretionary nature of this adjustment process, it is particularly incumbent upon the FDIC to defer to the primary regulator because examination information may well provide insight and data otherwise unavailable to the FDIC necessary both to inform the assessment adjustment and limit resulting disparities among comparable insured depositories. The primary regulator has the breadth and depth of experience and

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4 *See* 76 Fed. Reg. at 10,701.

5 *See* 76 Fed. Reg. at 21,257.

knowledge to provide the most accurate evaluation of a bank's risk profile. If only consultation with the institution's primary regulator remains, the FDIC should at least commit to giving substantial deference to the views of the primary regulator.

IV. The FDIC Should Provide a Definitive Statement of Complementary Risk Measures and Qualitative Risk Considerations and the Criteria for a Downward Adjustment

The Clearing House appreciates that the FDIC clarifies in the proposed Guidelines the two types of information that it will consider in determining whether to make an adjustment and the size of the adjustment: (a) scorecard measure outliers, and (b) information not directly captured in the scorecard, including complementary risk measures and qualitative risk considerations.[6] According to the proposed Guidelines, the FDIC would use these two types of information to consider whether potential discrepancies exist between the risk ranking of institutions based on their total scores and the relative risk ranking suggested by a combination of these two types of information.[7]

The proposed Guidelines provide definitions and examples for these measures, and further provide detailed examples on the analytical process that the FDIC would follow in applying these measures. While The Clearing House appreciates the FDIC's effort to clarify these measures and process, we are concerned that, as described in the proposed Guidelines, the scope of both complementary risk measures and qualitative risk considerations is limitless and undefined, and it could change from time to time without prior notice. As a result, it will be very difficult for institutions to predict when and which factors will trigger the adjustment process. An institution's ability to identify, monitor and manage relevant factors will be limited or even eliminated.

In light of the substantial impact of an upward discretionary adjustment on an institution's assessment obligation, The Clearing House respectfully submits that the FDIC should include a definitive statement of complementary risk measures and qualitative risk considerations in the final guidelines. For new possible risk factors that arise from market or regulatory developments, the FDIC generally should provide a prior notice and seek comment before using such risk factors in any adjustment. At minimum, if the FDIC believes that it must retain residual authority to consider other risk factors that are not in the final guidelines without prior notice, we respectfully submit that the FDIC should commit that this be done very rarely.

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6 *See* 76 Fed. Reg. at 21,262-63.

7 *See* 76 Fed. Reg. at 21,263.

We also submit that it would be appropriate to list factors that could result in a downward adjustment. These would include a ratio of liabilities subordinated to FDIC's claims that is higher than the norm, including, among other subordinated liabilities, unsecured debt and foreign deposits. As discussed in detail in our January 3 Comment Letter, these are required material factors in assessing an institution's risk to the Deposit Insurance Fund. In addition, we submit that the FDIC should commit to responding promptly to submissions requesting for a downward adjustment.

The Clearing House also requests that where the FDIC considers scorecard outliers in making adjustments, the FDIC also consider fully any offsetting outliers on other scorecard measures and that the FDIC make an explicit statement to this effect in the final guidelines.

V. The FDIC Should Not Make any Upward Adjustment With Respect to the Second Quarter of 2011

As the Final Rule indicates, the New Assessment System went into effect on April 1, 2011. As a result, the FDIC's discretionary authority to adjust a Large or Highly Complex Institution's total score also went into effect on April 1, 2011. Nonetheless, we urge the FDIC not to make any upward adjustment for the second quarter of 2011.

The Final Rule stipulates that "to ensure fair treatment and accountability," "the FDIC will not adjust assessment rates until the updated guidelines are published for comment and approved by the Board." [8] The Guidelines were published on April 12, 2011 for public comment, which must be received on or before May 31, 2011. When the FDIC finalizes the proposed Guidelines after the close of the public comment period, it will be close to, or possibly after, the end of the second quarter. It would be fundamentally unfair for the FDIC to make any upward adjustment for an institution for the second quarter of 2011 because the institution could not be regarded as having received fair prior notice of the factors considered by the FDIC in making adjustments. Therefore, we urge the FDIC to commit not to make any upward adjustment for the second quarter of 2011.

VI. Other Comments

A. The FDIC Should Exclude the Impact of FAS 166/167 for any Proposed Adjustment Contributed by an Outlier on the Growth-Adjusted Portfolio Concentration Measure

The New Assessment System in the Final Rule uses the three-year merger-adjusted portfolio growth rates in the calculation of the growth-adjusted portfolio

[8] 76 Fed. Reg. 10,672, 10,699 (February 25, 2011).

concentration measure as part of the scorecard. As we noted in our January 3 Comment Letter, the Financial Accounting Standards Nos. 166 and 167 ("*FAS 166/167*") inflated the real growth rate by applying a change in accounting convention to consolidate certain securitizations and special purpose entities. Therefore, when the FDIC proposes any adjustment contributed by an outlier score on the growth-adjusted portfolio concentration measure, it should explicitly exclude the impact of FAS 166/167. This impact is simply the result of a one-time accounting rule change, and it does not represent real business growth or increase in risk. The Clearing House respectfully submits that the FDIC should make an explicit statement to this effect in the final guidelines.

B. The FDIC Should Increase its Estimate of Hours Needed to Prepare a Response to the FDIC's Request for Information in Adjustments

The New Assessment System helpfully allows an institution to make a request to the FDIC for the FDIC to apply its discretionary adjustment power and adjust the institution's total score.[9] According to the proposed Guidelines, the FDIC would consider an institution-initiated request only if the request is supported by evidence of a material risk or risk-mitigating factor that is not adequately accounted for in the scorecard.[10] An information collection by the FDIC would occur when an institution makes such a request.[11] The FDIC estimates that the average number of hours to prepare a response to the FDIC's request for information in these circumstances would be eight hours. This seems to be an odd and quite limited basis for estimation, since the scope of the FDIC's request for further information and the consequential burden of response would depend largely on the evidence submitted with the institution's initial request. In any event, and particularly if this FDIC estimate is in fact intended to measure the entire burden of responding with supporting evidence beyond the bare initial request by the institution, we believe based on the experience of our members that the burden would be a considerable multiple of that estimated by the FDIC.

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9 *See* 76 Fed. Reg. 21,258.

10 *Id*.

11 *See* 76 Fed. Reg. 21,265.

Thank you for considering the views expressed in this letter. We appreciate the opportunity to share our views and would be pleased to discuss any of them further at your convenience. If you have any questions, please contact me at (202) 649-4602 (email: eli.peterson@theclearinghouse.org) or Joseph Alexander at (212) 612-9234 (email: joe.alexander@theclearinghouse.org).

Sincerely,

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