



Farmers & Merchants Bank

April 23, 2020

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

**Re: RIN 3064-AE94 - Unsafe and Unsound Banking Practices: Brokered Deposit Restrictions**

Dear Secretary Feldman,

I would like to thank the FDIC for the opportunity to share our thoughts about its February 10, 2020 proposed rule regarding brokered deposits. I am President and CEO of Farmers & Merchants Bank which has four locations in the Southwest Dayton area and the surrounding the Miamisburg, Germantown, West Carrollton and New Lebanon communities. Farmers & Merchants Bank was founded in 1923 and is one of the last locally owned and independent banks in the area. We focus on serving residents and small businesses who are often ignored by the area's larger banks and we invest deposits back into the local community in the form of loans to individuals for homes, autos, education and to businesses for new equipment, construction, additions and other operational and strategic needs. We offer access to over 75,000 ATMs nationwide and we also offer online and mobile banking for our customers' convenience.

During this time of crisis, we are even more focused on our local small businesses. To assist our communities' recovery from the Coronavirus devastation, our bank has rapidly shifted gears to fund the federal Paycheck Protection Program (PPP) loans for our small businesses. We've even had to turn to deposit placement firms like StoneCastle to help secure deposits in order to fund loans quickly for our local business clients. We usually don't do brokered deposits (on average we have less than 2%) but with PPP loan applications, we had to increase our use of brokered deposits to serve an immediate funding need so I am concerned about changes to brokered deposits rule that will potentially cause several of the third-party service providers I use to be deemed to be a deposit broker. Such determinations would have had a significant impact on our bank especially during times like this pandemic.

We are working with local partners to help save our downtown during this crisis. We recently setup a fund for our local merchants to get \$3,000 loans with no payments for 6 months and we've done over \$20,000 in loans to date. Staying true to our founding mission, we are continuing our philosophy of serving the small businesses that operate in our communities and are typically ignored by larger financial institutions. Megabanks usually won't lend for less than \$10 million so we make sure to fill the gap for our local businesses that need \$1-2 million loans. With this strategy, we've seen loan growth of 13% year over year.



Farmers & Merchants Bank

To fund those loans we need to offer competitive deposit products. Yet, as I read the proposed rule, it appears that we will be unable to utilize outside resources to research our markets and help us establish the interest rates, terms and rewards that make us competitive with the credit unions and the regional banks – large and small – that operate in our market areas, else the deposits we gather through the use of their services would be declared to be brokered. We don't see the logic of penalizing our small institution for outsourcing activities that if we conducted ourselves would be deemed to be permissible. The consultants we use to assist us with our deposit portfolio have advanced tools and loads of data and experience that help us stay competitive in our markets. The propose rule should not be allowed to put community banks at a competitive disadvantage for merely engaging an outside resource to help us operate our businesses.

In addition to funding small businesses, we want to make sure we are serving our customers in the manner that they want to be served which is why we use third-party service providers to assist us with our mobile app, online banking services, social media marketing and other customer service activities. Online account openings have become especially important during COVID-19 since our lobbies and branches are not open and consumers are beginning to open accounts remotely via online account opening software that is provided to us by a third party.

Before providing the specific revisions that I would like to see incorporated into the FDIC's final rule, I'd like to summarize the public statements FDIC Chairman Jelena McWilliams has made since being confirmed in her role on June 5, 2018 as I believe her comments serve as an informative backdrop to my recommended revisions. In her December 4, 2019 statement before the Committee on Financial Services, U.S. House of Representatives, Chairman McWilliams articulated the following three overarching goals for the FDIC:

1. Strengthen the banking system as it continues to evolve;
2. Ensure FDIC supervised institutions can meet the needs of consumers and businesses and
3. Foster technology solutions and encouraging innovation at community banks and the FDIC

In statements, speeches and public comments she has made throughout her time at the FDIC, Chairman McWilliams has consistently communicated her desire to lay the foundation for the next chapter of banking by encouraging innovation that meets consumer demands; promoting community banking; reducing the compliance burden; and modernizing the FDIC's supervisory capabilities. This is demonstrated by her October 1, 2019 "The Future of Banking" speech at the Federal Reserve Bank of St. Louis:

*"It is my goal that the FDIC lays the foundation for the next chapter of banking by encouraging innovation that meets consumer demand, promotes community banking, reduces compliance burdens, and modernizes our supervision. This is not optional for the FDIC. We must lay this foundation because the survival of our community banks depends on it. These small banks face challenges from industry consolidation, economies of scale, and competition from their community bank peers, larger banks, credit unions, fintechs, and a plethora of other non-banks lenders. While the FDIC has limited ability to address*



Farmers & Merchants Bank

*the direct cost of developing and deploying technology at any one institution, there are things that we can do to foster innovation across all community banks and to reduce the regulatory cost of innovation. We cannot sit on that proverbial regulatory perch and observe the change from above. We have to get on the ground, roll up our sleeves, and get to work on supporting and advancing scalable technological change that works for community banks.”*

The Chairman has expressed her desire to amend the current brokered deposit rules to reflect the transformative power of new technologies, ever evolving consumer preferences, and today’s modern banking practices. Since the requirements for brokered deposits were put in place thirty years ago, the financial services industry has seen significant changes in technology, business models, products, services, delivery capabilities and industry participants and I agree, the current rules must be updated to reflect these changes.

Unfortunately, as I read the currently written proposed rule, it appears that the proposed language is NOT focused on fostering innovation within community banks or ensuring the viability of our community banking system. While I understand this might not be the FDIC’s intent, I can only opine on the written language and, as I read it, the proposed rule will restrict my institution’s ability to serve my community and support my customers in the manner in which they want to be supported.

The proposed new “facilitating” definition indicates that a person would meet the “facilitating the placement of deposits” definition of a “deposit broker” by engaging in any one, or more than one, of the following activities: the person directly or indirectly shares any third party information with the insured depository institution; or the person provides assistance or is involved in setting rates, fees, terms, or conditions for the deposit account. Therefore, the proposed rule would restrict my bank’s ability to receive any external information from any third party (and by extension, likely can’t receive any associated insights either) about our own customers and / or potential customers. This restriction negates my institution’s ability to build holistic understandings of our customers; our ability to deliver personalized messages and alerts containing next-best-actions and/or financial advice; and all but eliminates our ability to deepen our relationships by offering our customers additional products, services and capabilities from our institution.

In addition, the proposed rule restricts rather than enables community banks from using consulting and/or advisory services to assist us develop, deliver and improve retail deposit offerings. Thus, without potentially having our deposits being declared “brokered,” banks like mine will no longer be able to engage companies who provide market research; product development; price elasticity studies; profitability assessments; non-interest income; retail optimization services; behavioral and activity insights; asset liability management advice, overdraft protection services; reward and customer loyalty programs and more.

As I mentioned earlier, community banks rely on industry experts to help us with these activities and yet, the proposed rule denies community banks access to these experienced resources. Rather than providing safety and soundness protections, the proposed language is actually introducing



Farmers & Merchants Bank

safety and soundness concerns by prohibiting institutions like mine from utilizing industry experts and advanced modeling tools and analysis.

It also appears that the FDIC has not considered the negative financial impact the proposed rule will have on individual community banks. For example, our bank offers a series of free checking accounts that provide our customers with a suite of rewards and reimbursements of other institution’s ATM withdrawal fees when they utilize specific services from our institution – direct deposit, debit card, online bill pay, etc. We utilize a third party to help us manage the distribution of these rewards and to consult with us on how we can expand the direct relationships we establish with individual depositors via these attractive accounts. As currently written, the first and third prong within the proposed rule’s “facilitating the placement of deposits” definition would eliminate our ability to engage this third party and we would be left with one of two decisions – bear the brunt of these deposits being treated as brokered or withdraw the accounts and replace the corresponding deposits with other sources of fund--likely either 1 year or 5 year certificates of deposits.

As exhibited below, this would be an extremely expensive alternative for our institution as the non-interest income generated within these accounts offsets both the interest and non-interest expense of these accounts, which will not happen if these funds have to be replaced with certificates or other traditional depository products. Here is the analysis we’ve done, should we have to declare these deposits brokered and replace them with 1 or 5 year CDs:

	3 <sup>rd</sup> Party Assisted Deposits	1 Year CD	5 Year CD
Average Balance of Reclassified Funds			
Cost of Funds			
Interest Expense			
Non-Interest Expense			
Non-Interest Income			
Net Cost of Deposits			
Net Percentage Cost			
Total Savings vs CDs			

\* Source: <https://www.depositaccounts.com/cd/#rateTrend>



Farmers & Merchants Bank

Furthermore, the new rule is problematic with the process by which third parties would have to apply for a primary purpose exception from the FDIC for each of its individual lines of business; and, with the FDIC Staff's authority to review or eliminate current FDIC Advisory Opinions post final rule. If left unchanged, the proposed rule would severely interfere with substantial investments that have been made by community banks and industry participants based upon the specific assurances provided by those Advisory Opinions.

With all those issues outlined, I accordingly request the FDIC consider the following modifications to the final rule:

1. Grandfather all current FDIC Advisory Opinions so they remain in full force and effect post final rule.
2. Revise the proposed "facilitation" definition as follows: Remove the first prong of the proposed definition altogether. I fail to understand how the exchange of information has an adverse effect on the stability of an individual's deposits.

Modify the third prong of the proposed definition so that it specifically addresses third parties who control the depositor relationship. The language is currently too broad so it should be clarified so that it captures traditional brokers that own the depositor relationship and negotiate or set the rates, fees, terms or condition of the deposit account on behalf of their depositor customer.

3. Provide explicit exclusion from the "brokered deposit" definition for transaction account deposits (i.e. checking accounts) and relationship-based deposits (i.e. where a depositor uses multiple services and products from their chosen bank – savings account, loan, debit card, online bill pay, direct deposit, etc.) as these deposits are a very stable source of funds as they are associated with a tangible relationship that has been established directly between the individual depositor and the bank.

Similarly, exclude third-party service providers from the "deposit broker" definition, who do not have any contractual relationship with any depositor to place, manage or control any of the individual's deposits. Community banks rely on third-party service providers to help us develop and offer attractive products and services as we don't have the same resources, technical expertise and budgets that our larger banking counterparts have. We should be able to use external resources to build direct relationships with individuals who live, work and play in the communities we serve.



Farmers & Merchants Bank

4. Streamline the proposed primary purpose exception application and determination process. As currently worded, the proposed rule is so broadly written that it traps a wide range of industry participants. As written, all of those industry participants would be required to apply for a primary purpose exception from the brokered deposit rule. This is a cumbersome and time-consuming process that will effectively put all third-party innovation "on hold" as each industry participant would have to apply for an exception for each line of business, they are engaged in. In light of the COVID-19 crisis, think of where many community banks would be if they had to wait four months to deploy new online account opening software as their chosen vendor had to wade through the FDIC proposed approval process.

We applaud the FDIC for wanting to modernize the brokered deposit rules but as it currently stands, the proposed rule hurts rather than helps community banks. The rule penalizes us for being small and outsourcing many operational tasks to external resources. Community banks are responsible for well over half of all small business loans. In times of crisis and in times of economic prosperity, institutions like mine play an important role in fueling our local and by extension our nation's economy. Please don't make it harder for me to compete with fintech providers, credit unions and megabanks for the stable source of deposits I need to fulfill our institution's mission and to serve our communities.

Thank you for allowing me to express my concerns and suggestions. I strongly encourage the FDIC to incorporate the above recommendations into the final rule so that community banks can continue to serve our local towns and support our local businesses especially after COVID-19.

Respectfully,



Shon B. Myers  
President & CEO  
Farmers & Merchants Bank  
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