August 11, 2006

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

Re: Proposal to Implement the One-time Assessment Credit Required by the Federal Deposit Insurance Reform Act of 2005 ("Reform Act")

Dear Sir or Madam:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to offer comments in connection with the FDIC proposal to implement the one-time assessment credit required by the recently enacted Federal Deposit Insurance Reform Act of 2005 ("Reform Act").

Summary of ICBA's Position

ICBA recommends that for purposes of allocating the one-time assessment credit and defining the term "successor", the FDIC utilize both the "follow the charter" approach for mergers and consolidations and the "follow the deposits" approach for purchases and assumption transactions involving deposit transfers. To use only the "follow the charter" approach would be an injustice to many community banks that have been involved in purchase and assumption agreements and have been acquiring deposits during the past ten years. While we agree that "following the deposits" significantly complicates the FDIC's job of allocating the credit, there are methods that the FDIC can employ to help make the approach operationally viable. ICBA also agrees with the FDIC's proposed notification and review procedure regarding the credits as well as its proposed policy for transferring credits once they are implemented.

[1] *The Independent Community Bankers of America represents the largest constituency of community banks of all sizes and charter types in the nation, and is dedicated exclusively to representing the interests of the community banking industry. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 265,000 Americans, ICBA members hold more than $876 billion in assets $692 billion in deposits, and more than $589 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

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Background and Proposal

The Reform Act requires the FDIC to provide by regulation an initial, one-time assessment credit to each "eligible" insured depository institution (or its successor) based on the assessment base of the institution as of December 31, 1996, as compared to the combined aggregate assessment base of all eligible institutions as of that date (the "1996 Base Ratio"). The aggregate amount of one-time credits is to equal the amount that the FDIC could collect if it imposed an assessment of 10.5 basis points on the combined assessment base of the Bank Insurance Fund and the Savings Association Insurance Fund as of December 31, 2001. An "eligible" insured depository institution is one that (1) was in existence on December 31, 1996, and paid a federal deposit insurance assessment prior to that date, or (2) is a "successor" to any such insured depository institution.

The FDIC proposes to define "successor" as only including the resulting institution in a merger or consolidation after December 31, 1996. Under this "follow the charter" approach, the definition would not include the assuming institution in a purchase and assumption transaction (such as a branch sale), even if substantially all of the assets and liabilities of an institution were acquired by the assuming institution. The FDIC believes that this definition is consistent with the general expectations of the industry, because it reflects the common legal meaning of the word "successor" and the principle that the resulting corporation in a merger or consolidation generally receives the rights, privileges, interests and liabilities of the merging or consolidating corporations.

The FDIC considered alternative approaches to the definition of successor that would "follow the deposits" but rejected them because they seemed less consistent with the purpose of the one-time credit and did not reflect the reasonable expectations of parties to transactions based on general corporate law principles**.** More importantly, the FDIC has serious concerns about the operational viability of a "follow the deposits" approach because of the lack of reliable data on purchase and assumption transactions. The FDIC does not maintain a database of all deposit transfer transactions that would be necessary to implement a "follow-the-deposits" rule. Therefore, most, if not all, of the necessary information would have to be collected from the industry. Furthermore, the FDIC would have to resolve disputes between institutions over who actually owns the pre-1997 deposits before a "follow the deposits" approach to allocating the one-time credit could be fully implemented. According to FDIC estimates, there have been roughly 3,850 bank mergers and consolidations and at least 1,400 and perhaps over 1,800 branch or deposit transactions since 1996.

In addition to defining "successor", the FDIC proposal would:

- Require the FDIC to send a Statement of One-time Credit notifying each bank of its 1996 assessment base ratio and share of the one-time credit;
- Allow a bank to challenge the amount of its one-time credit by submitting a review request within 30 days of receiving the Statement or an adjusted invoice;
- Require that a bank's one-time credit be applied against the bank's quarterly assessment payment. In calendar years 2008-2010, the credit would apply to 90% of the quarterly

assessment unless the institution exhibits financial, operation or compliance weaknesses; and

- Allow an institution to enter into a written agreement to transfer the credits to another financial institution provided the agreement is signed by representatives of both institutions and is filed with the FDIC.

ICBA's Position

Allocating Credits and Defining "Successor." **While we acknowledge that the "follow the deposit" approach is operationally more difficult for the FDIC to administer than the "follow the deposit" approach, we believe that the most equitable method of allocating the one-time assessment credits and defining the term "successor" is for the FDIC to use both approaches.** ICBA recommends that in cases of mergers or consolidations or de facto mergers or consolidations since December 31, 1996, than the FDIC should use the "follow the charter" approach and consider the credits transferred to the surviving entity. However, where two institutions have been involved in deposit transfers since December 31, 1996, than the credits should adhere to the deposits so that the purchasing institution can use them to offset future assessments. Using the "follow the deposits" approach for deposit transfers will not have any impact on the assessment credit amounts allocated to eligible institutions not involved in deposit transfers. Their assessment credits would be the same whether the FDIC uses only a "follow the charter" approach or both approaches as recommended by ICBA.

ICBA believes that any credit allocation system that does not recognize deposit transfers would penalize those community banks that have purchased deposits during the last ten years. The FDIC estimates that there have been as many as 1800 branch or deposit transactions since December 31, 1996. Many of these purchase and assumption transactions were significant transactions involving community banks. For instance, over the past ten years, community banks have been major beneficiaries of deposits spun-off by the resulting institutions involved in large bank mergers or consolidations. In some instances, these spun-off deposits have allowed community banks to increase their core deposits by over fifty percent and to branch into strategic locations. The "follow the charter" approach would effectively penalize community banks that have taken advantage of these opportunities.

We agree with the FDIC that the common legal meaning of the word "successor" and the principle that the resulting corporation in a merger or consolidation generally receives the rights, privileges, interests, and liabilities of the merging or consolidating corporations, supports using the "follow the charter" approach for mergers and consolidations. However, we also believe there are valid legal reasons for supporting a "follow the deposit" approach. Most purchasers of deposits paid a premium to the seller when they purchased the deposits and as part of the purchase and assumption agreement, agreed to assume the rights and liabilities associated with the purchased deposits. Just as in a merger transaction, the selling institution also agreed to convey all rights and privileges to the deposit liabilities. Therefore, the purchasing institution should reap the benefits of any subsequent credits or dividends that are issued or declared with regard to those deposit liabilities.

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While it is true that in many instances, parties to deposit transfer transactions during the past ten years were unaware that there could be credits or dividends associated with the deposit transfers, we would point out that parties involved in many merger transactions likewise were unaware of possible transfers of credits and dividends. Yet the FDIC proposal to adopt the "follow the charter" approach would allow for the transfer of credits in merger transactions. If the parties' knowledge of these credits is to be the deciding factor for determining whether the credits should transfer, then many transactions, whether mergers or purchase and assumption transactions, would not qualify.

Furthermore, since future assessments are to be based on deposits, it would follow that the credits should follow the deposits in purchase and assumption transactions so that they can be used as offsets to those assessments. Assessments have always been based on an institution's level of deposits and not on its charter. The FDIC also has experience with tracking specific types of deposits, as it has done with Oakar deposits[2], and tracking them from institution to institution.

While we understand that it is more difficult for the FDIC to compute credits using the "follow the deposit" approach, we offer three methods for consideration:

- Tracking branches: Under this approach, if eligible deposits were sold with one or more branches, then the FDIC could track the deposits back ten years by using the 1996 Summary of Deposits published by the FDIC. An eligible bank that purchased those branch deposits would then have their 1996 assessment base credited with the amount indicated in the 1996 Summary of Deposits data for the involved branches and the seller's assessment base would be debited by a corresponding amount.
- Percentage method: The FDIC would calculate the percentage of total deposits disclosed in the seller's quarterly call report prior to the deposit transfer and would use that percentage to adjust the seller's and purchaser's pre-1997 assessment base. For instance, if Bank A sold 10% of its deposits to Bank B on December 31, 1999 based on Bank A's Call Report data as of September 30, 1999, then provided that Bank A and Bank B were in existence on December 31, 1996, Bank A's pre-1997 assessment base would be debited by 10% and a corresponding amount would be credited to Bank B's pre-1997 assessment base.
- Discounted Growth Rate method: The purchaser's and seller's pre-1997 assessment base would be adjusted by the actual amount of the deposits transferred discounted by the average deposit growth rate (expressed as a percentage) of the selling institution since December 31, 1996. For instance, if Bank A sold deposits to Bank B on December 31, 1999, then Bank A's and Bank B's pre-1997 assessment base would be adjusted by the dollar amount of the deposits transferred as shown by the records of both banks but discounted by the deposit growth rate of Bank A during the three year period from 12/31/1996-12/31/1999.

[2] Oakar deposits, named after Representative Mary Rose Oakar, were deposits held by BIF-insured institutions that were formerly held by SAIF-insured institutions and were allowed to be passed from institution to institution without paying any entry or exit fees to BIF or SAIF.

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We would recommend that the FDIC use the "follow the deposits" approach only in those circumstances where the institutions involved have presented sufficient written evidence of a valid deposit transfer. In most instances, presenting a copy of an executed purchase and assumption agreement signed by the legal representatives of both parties together with a closing statement regarding the deposit transfer should be sufficient evidence. If the institutions participating in the deposit transfer disagree over the amount transferred, then the burden would be on the purchasing institution to prove its claim of the deposit amount transferred. Otherwise, the FDIC would use the amount claimed by the selling institution as the amount transferred. To further simplify the FDIC's administration of the credits, we would suggest that only significant deposit transfers—only those involving over 5% of the seller's total domestic deposits or over 10% of the purchaser's domestic deposits—be considered.

De Facto Mergers. We agree that the FDIC should consider a de facto merger—where an institution has conveyed all of its deposit liabilities and substantially all of its assets to a single acquiring institution—to be a "merger" and not a transfer of assets and deposits. Otherwise, the FDIC would be ignoring the legal realities of such transactions where the selling institution becomes nothing more than a shell corporation and the purchasing institution holds all of the seller's deposit liabilities and most of its assets and in effect, is the survivor. In the case of de facto mergers, credits should be considered transferred to the resulting institution.

We note that under our recommendation of recognizing both mergers and deposit transfers when allocating credits, it would not make a significant difference whether a de facto merger was considered a merger or a deposit transfer. Credits would always transfer to the resulting institution in such transactions.

Notification of and Review of Credit Amounts. We agree with the FDIC that each insured depository institution should be notified of its 1996 Base Ratio and its share of one-time assessment credits as soon as practicable after the FDIC approves the final rule. The notice would take the form of a Statement of One-time Credit informing every institution of its 1996 Base Ratio and providing an explanation of how the ratios and the resulting amounts were calculated. The FDIC proposes to provide the Statement through FDIC*connect* and by mail in accordance with existing practices for assessment invoices.

ICBA also agrees with the FDIC's proposed review procedure. Institutions would have 30 days from the date the FDIC made available its Statement to file a request for review with the FDIC's Division of Finance. The request would have to be accompanied by any documentation supporting the institution's claim and would include a list of those other institutions that could be directly or materially affected by granting the request for review. The Division of Finance would have 60 days to respond to the request. The requesting institution as well as any other institution materially affected by the Director's decision would then have 15 days to file an appeal with the FDIC's Assessment Appeals Committee. The AAC's determination would be final and not subject to judicial review.

Using and Transferring Credits. ICBA also agrees with the FDIC's proposal to automatically apply an institution's credits to its assessment to the maximum extent allowed by law. For fiscal year 2007 assessment periods, credits generally can offset 100% of the institution's assessment.

For assessments that become due for assessment periods beginning in fiscal years 2008, 2009, and 2010, the Reform Act provides that credits may not be applied to more than 90% of an institution's assessment. Therefore, under the proposal, credits would automatically apply to 90% of an institution's assessment, assuming the institution has sufficient credits.

ICBA also agrees that an institution should be allowed to transfer its credits after an institution's credit share has been finally determined and no request for review or appeal is pending. This would allow institutions that are parties to deposit transfers to provide in their purchase and assumption agreements provisions for transferring their credits. We agree that the FDIC should require the parties to submit their written agreements. Adjustments to each institution's credit amount would then be reflected with the next quarterly assessment invoice, so long as the institutions submit the written agreement to the FDIC at least ten business days prior to the FDIC's issuance of invoices for the next assessment period.

Conclusion

ICBA appreciates the opportunity to offer comments with regard to the FDIC's proposal to implement the one-time assessment credit required by the recently enacted Federal Deposit Insurance Reform Act of 2005. If you have any questions about our comments, please do not hesitate to contact me at 202-659-8111 or by email at Chris.Cole@icba.org.

Sincerely,

Christopher Cole

Christopher Cole

Regulatory Counsel