U.S. TRUST

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September 21, 2006

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

Attention: Comments

Re: **Proposed Rule on Risk Differentiated Assessments (RIN 3064-AD09)**

Dear Mr. Feldman:

United States Trust Company, National Association ("U.S. Trust")[1] welcomes the opportunity to comment on the Proposed Rule on Risk Differentiated Assessments (the "Proposal") that was recently issued by the Federal Deposit Insurance Corporation (the "FDIC").[2] U.S. Trust supports the goal of the FDIC of making deposit insurance assessments more risk sensitive, and therefore, fairer to insured depository institutions.

Schwab Bank:

In a separate letter, U.S. Trust's sister bank, Charles Schwab Bank, National Association ("Schwab Bank"),[3] is providing comments that address the Proposal's treatment of "new banks." Although U.S. Trust would not be treated as a "new bank" under the Proposal, it strongly supports the comments being made by Schwab Bank.

[1] U.S. Trust is a wholly-owned subsidiary of U.S. Trust Corporation which, in turn, is a wholly-owned subsidiary of The Charles Schwab Corporation ("Schwab".)

[2] 71 Fed. Reg. 41910 (July 24, 2006).

[3] Schwab Bank is also a wholly-owned subsidiary of Schwab.

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Volatile Liabilities:

U.S. Trust wishes to focus on that portion of the Proposal that would use the ratio of "volatile liabilities" to gross assets as a financial ratio when differentiating among depository institutions in Risk Category I.[4] In this regard, U.S. Trust is concerned with the Proposal's determination of which liabilities would be classified as "volatile."

The Proposal would identify the following as "volatile liabilities":

- Foreign office deposits,
- Federal funds purchased,
- Securities sold under agreements to repurchase, and
- Time deposits of $100,000 or more held in domestic offices.[5]

Uninsured Deposits:

The Proposal characterizes uninsured deposits[6] as "volatile" in the belief that it is likely that such deposits would be withdrawn if an institution's condition deteriorated. The Proposal based this conclusion on a study of the failure of the Hamilton Bank.[7] In contrast, U.S. Trust believes that such uninsured deposits are a stable source of funding for many institutions and should not be characterized as "volatile liabilities" in the absence of greater empirical evidence.

The Proposal would characterize uninsured deposits as "volatile" regardless of their term. However, term liabilities (including uninsured deposits) – e.g., those with a maturity of more than a year -- would provide stable funding to an institution even if the condition of that institution deteriorated. Such liabilities ameliorate volatility, and their presence is not indicative of a downgrade within one year. Therefore, they should not be considered "volatile liabilities."

Further, the characterization of such uninsured deposits as volatile liabilities would have a disparate impact on smaller institutions. Under the Proposal, the use of "financial ratios" including the ratio of "volatile liabilities" to gross assets to differentiate among depository institutions in Risk Category I would be:

[4] The "financial ratios" would be used as factors to differentiate among smaller institutions, i.e. those with less than $10 billion in assets. Prop. 12 C.F.R. § 327.9(d)(i) as proposed at 71 Fed. Reg. 41932. Their use would be phased-out as an institution's assets increased to $30 billion. *Id.* at § 327.9(d)(3)(vii).

[5] 71 Fed. Reg. at 41937.

[6] These would include foreign office deposits and deposits in domestic offices in excess of the insured amount, which is generally $100,000.

[7] 71 Fed. Reg. at 41953n.97.

- Applicable to smaller institutions -- i.e. those with less than $10 billion in assets.
- Phased-out as an institution's assets increased from $10 billion to $30 billion.
- Inapplicable to larger institutions -- i.e. those with assets of $30 billion or more.

This disparate impact would be amplified for specialized institutions like U.S. Trust that do not extensively gather retail deposits, and yet in their area of specialty, directly compete with larger institutions.

Even if it were assumed *arguendo* that all uninsured deposits should be treated as "volatile liabilities," the Proposal as written is still too broad. It would include as "volatile liabilities" a large amount of insured deposits. Proposed Appendix A[8] would define "volatile liabilities" as including "time deposits of $100,000 or more held in domestic offices" and state the amount of such "time deposits" of an institution should be obtained from the institution's quarterly Call Report.[9]

The amount of "time deposits of $100,000 or more held in domestic offices" is set forth at Memoranda Item 2.c of schedule RC-E to the Call Report. The amount entered there includes all balances of $100,000 or more and does not exclude that portion of such balances that is covered by deposit insurance. Moreover, the amount shown at forth at Memoranda Item 2.c includes brokered deposits issued to brokers in amounts of $100,000 or more even if "the underlying depositors' shares are in denominations of less than $100,000."

Accordingly, if the amount set forth at Memoranda Item 2.c of Schedule RC-E were included in "volatile liabilities," a significant amount of insured deposits would be included because:

- Generally, the first $100,000 (and in certain cases, the first $250,000) of time deposits in excess of $100,000 would be insured deposits.
- The time deposits issued to brokers in amounts of $100,000 or more where the shares of the underlying depositors were in amounts of less than $100,000 would also be insured deposits.

Such inclusion of insured deposits is not supported by the rationale that uninsured deposits are "volatile" because of the likelihood that uninsured deposits would be withdrawn if an institutions condition deteriorated. At a minimum, the Proposal should be amended so that insured deposits are excluded from the definition of "volatile liabilities."

[8] Prop. 12 C.F.R. Part 327, Subpart A, Appendix A, as proposed at 71 Fed. Reg. 41936 *et seq.*

[9] 71 Fed. Reg. at 41937.

Federal Funds and Repurchase Agreements:

The Proposal would treat as "volatile" all funding obtained by means of either the purchase of Federal funds or the sale of securities under agreements to repurchase. Again, the Proposal's measure of "volatility" would ignore the term of the transaction. Transactions involving either the purchase of Federal funds or the sale of securities under agreements to repurchase could be effected on a term basis and could have a maturity of, e.g., more than a year.

Inter-Affiliate Transactions:

The Proposal does not take into consideration that many depository institutions are part of a holding company structure. In many instances, depository institutions utilize transactions with their affiliates to achieve funding on an economic and flexible basis.

Inter-affiliate transactions involving either the purchase of Federal funds or the sale of securities under agreements to repurchase should not be considered "volatile." The affiliates of a depository institution are not likely to run for the door if the condition of the institution weakens. Bank holding companies are required to be a source of strength to their subsidiary banks.[10] In particular, transactions in Federal funds between sister banks should not be characterized as "volatile." Such banks are already tied together by the "cross guarantee" among affiliated depository institutions.[11]

Similarly, deposits raised by an affiliated "deposit broker" should be seen as more stable than those raised by an independent third party. This is especially true if both the depository institution and the "deposit broker" are wholly-owned by a common parent.

Federal Home Loan Advances:

The Proposal specifically requested comment on whether Federal Home Loan Advances should be should be included in the definition of volatile liabilities or, alternatively, whether higher assessment rates should be charged to institutions that have significant amounts of secured liabilities.[12]

In this regard, in neither the Preamble nor the Appendices to the Proposal did the FDIC fully articulate why Federal Home Loan Advances should be treated as "volatile." Such advances and securities sold under agreements to repurchase represent claims against the institution that are effectively secured. In the event of the insolvency of the institution, such liabilities would rank ahead of the claims of depositors and of the FDIC. In theory, such liabilities would present a greater risk to the deposit insurance fund.

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[10] 12 C.F.R. § 225.4(a)(1).

[11] 12 U.S.C. § 1815(e).

[12] 71 Fed. Reg. at 41929.

However, the probability of insolvency of depository institutions in Risk Category I is quite remote. Moreover, the point in distinguishing among institutions in Risk Category I is not to identify those institutions that might cause the FDIC greater loss in the unlikely event of insolvency, but rather to identify those that were more likely to be downgraded to another Risk Category. Again, neither the Preamble nor the Appendices to the Proposal explain why the use of such liabilities is indicative of an increased probability of a future downgrade.

Rather than being a source of volatility, U.S. Trust believes that Federal Home Loan Bank advances are a stable and a relatively inexpensive source of funding. Moreover, Federal Home Loan Bank System was established by Congress to provide funding to encourage and support housing finance. Imposing added costs on a depository institution's use of such advances would be in conflict with a public policy advanced by Congress. Accordingly, Federal Home Loan Bank advances should not be characterized as "volatile liabilities."

In conclusion, U. S. Trust appreciates the opportunity to express its views on the Proposal and hopes the comments contained in this letter are helpful. If you have any questions on the above, please contact the undersigned by telephone at (212) 852-1367 or by E-mail at john_sullivan@ustrust.com.

Very truly yours,

John B. Sullivan