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Sept 22, 2006

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

Re: RIN 3064-AD09, Proposed Risk Based Assessment Regulation

Dear Mr. Feldman:

UBS Bank USA (the "Bank") appreciates this opportunity to comment on the FDIC's proposed regulation on risk-based deposit insurance assessments.

The Bank is an FDIC-insured Utah industrial bank with a single office location in Salt Lake City, Utah. The Bank began accepting FDIC-insured deposits on September 15, 2003, and had deposit liabilities of approximately $18 billion as of August 30, 2006. The Bank is an indirect, wholly owned subsidiary of UBS AG, a Swiss banking corporation conducting a global financial services business directly and through operating subsidiaries throughout the world. UBS AG is registered as a financial holding company with the Federal Reserve Board, and is subject to the Bank Holding Company Act of 1956, as amended, through Section 8(a) of the International Banking Act of 1978, as amended.

The preamble to the proposed regulation asks for comment on a number of issues. Our comments, below, will focus on the proposed adverse treatment of "new" institutions.

The proposal would mandate that institutions be assessed at the highest rate within "Risk Category I" if they are "new" institutions, even if those institutions would otherwise qualify for the lower rate in that category. The proposal defines a "new" institution as one that has been in existence for less than seven years, subject to the ability of the FDIC to grant an exception when a new institution is created through a merger or consolidation with an existing institution based on a number of factors, including the relative sizes of the institutions.

The Supplementary Information accompanying the proposal offers essentially two justifications for this approach. First, the Supplementary Information states that "[o]n average, new institutions have a higher failure rate than established institutions." 71 Fed. Reg. 41,927 (July 24, 2006). While the Supplementary Information acknowledges that empirical studies indicate that newly chartered institutions actually have a *lower* probability of failure during the first three years of their existence, it is further noted that during the next four years, broadly speaking, failure rates for *de novo* institutions tend to exceed those for established institutions. The proposal, however, penalizes newly chartered institutions during this entire period with a higher deposit insurance assessment that is unrelated to their actual risk.

We are concerned that while the studies on which the proposal is based find important risk correlations for new institutions with things like capitalization and loan quality--correlations that exceed those found in established institutions--the proposal nonetheless takes a "one size fits all" approach, inappropriately failing to consider the critical distinctions among the various types of new depository institutions from a safety and soundness perspective. Most importantly from the perspective of the Bank, the proposal fails to differentiate the risk created by stand-alone de novo institutions and those that associated with a global banking organization.

By contrast, the Federal Reserve Bank of Chicago Working Paper upon which the "new institution" aspect of the proposal is based itself notes a distinction between *de novo* institutions that are unaffiliated with a bank holding company, and those that, like the Bank, have been chartered by an existing banking organization. The study points out that there is a significant and positive correlation between membership of a *de novo* bank in a multi-bank holding company structure and its survival time. R. DeYoung, "For How Long are Newly Chartered Banks Financially Fragile?" Federal Reserve Bank of Chicago Working Paper Series 2000-09, at 23 ("FRB Chicago Study"). Moreover, even the FRB Chicago Study did not attempt to more specifically differentiate banks chartered by strong, established bank holding companies or foreign banks like UBS AG. We do not believe that institutions, like the Bank, which are strategically created as part of a global banking enterprise with a history of operating banks in a safe and sound manner should be lumped together with other *de novo* institutions, which do not have the same resources, experience or track record.

The second set of justifications used by the Supplementary Information to penalize *de novo* institutions also appears to be a broad over-generalization that is not supported by the studies on which the proposal relies. The Supplementary Information indicates that higher assessment rates for new banks are warranted because the financial data of such institutions is harder to interpret and less meaningful, because rapid changes early in the life of an institution can make ratios volatile and because credit risk cannot be assessed until an institution's loan portfolio has an opportunity to season. To the contrary, the FRB Chicago Study notes "our results suggest that early warning signals may be *easier* to identify for de novo banks than for established banks, perhaps because banks in the early stages of their life cycles are less heterogeneous and hence simpler to model than mature banks." FRB Chicago Study, Abstract (emphasis added). Indeed, because *de novo* institutions are subject to higher capital requirements and closer scrutiny, including more frequent examinations, there is a better ability for the FDIC to determine quickly whether conditions are deteriorating at a new institution, so that increased assessments are warranted.

In light of the above, we respectfully suggest that the FDIC exclude from the new institution penalty any recently chartered institution whose parent is an established domestic or foreign bank, or a financial or bank holding company. Even if the FDIC is not willing to specifically exclude such institutions from the new institution penalty provision, we believe the FDIC should at least reserve the flexibility to exempt such institutions based on a review of the specific circumstances of the institution's parent holding company. Factors that should be considered include:

- Capital adequacy of the parent bank or bank/financial holding company;
- CAMELS ratings of the U.S. depository institutions it owns;
- Bank regulatory ratings of a foreign bank parent's branch and other offices in the United States;
- Capital levels of the de novo depository institution in excess of applicable "well capitalized" standards;
- Asset quality, funding sources and business plan of the de novo depository institution; or
- Consistency of business lines of the de novo depository institution with activities historically performed by holding company affiliates on a safe and sound basis.

Finally, if "new" institutions continue to be disadvantaged in the final rule, we respectfully suggest that the seven year period for "new" institutions, with the attendant higher assessments, is too long. By contrast, initial capital requirements and operating conditions on new charters typically have a duration of three years. While the end of that three year period corresponds with a period of increased risk *on average*, the three year operating history of such entities should provide clear sign-posts that will enable the FDIC to make a more individualized determination with respect to specific institutions. Accordingly, if a "new" institution penalty is retained in the final rule, it should expire at the end of three years unless the FDIC makes a specific determination that the condition of a particular institution warrants continued treatment under the "new" institution standard.

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We appreciate the FDIC's time and effort in preparing the proposal, as well as this opportunity to comment. If you have any questions, please contact me directly.

Sincerely,

Raymond Dardano
President/CEO
UBS Bank USA