First Niagara

Banking • Investments • Insurance

September 5, 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

Dear Mr. Feldman:

This letter contains the comments of First Niagara Bank regarding the FDIC's proposed rule on deposit insurance assessments. My comments are directed to the question of whether Federal Home Loan Bank (FHLB) advances should be included in the definition of "volatile liabilities" when the FDIC calculates risk-based premiums for deposit insurance or, alternatively, whether higher assessment rates should be charged to institutions that have significant amounts of secured liabilities.

FHLB advances are not volatile liabilities for FHLB members. FHLB advances have pre-defined, understood and predictable terms. Unlike deposits, FHLB advances do not evaporate due to circumstances outside of the control of an FHLB member. Experience has shown that deposits may be lost due to disintermediation arising from a variety of factors, such as special, short-term promotions in a particular market or the existence of higher returns to depositors on alternative assets. While some institutions can look to Wall Street for replacement liabilities, the money and capital markets have not functioned well as long-term, stable providers of wholesale funds to the community banks that comprise the bulk of the membership of the FHLB System.

As established by Congress, the primary purpose of the FHLB System is to provide a source of long-term liquidity for FHLB members. Throughout their 75-year history, the FHLBs have performed this mission successfully. The FHLBs are a stable, reliable source of funds for member institutions, and the availability of such credit has a predictable, beneficial effect on members' business plans. Given the value of such a stable source of funding, it is not surprising that more than 8,200 financial institutions are members of the FHLB System. It would be illogical to include FHLB advances in the definition of volatile liabilities, given the stability of the FHLBs, the reliable availability of FHLB advances as a source of wholesale funding, and the beneficial and predictable effect of such funding on members' business plans.

Deposit insurance premiums should be based on an institution's actual risk profile, taking into account the institution's supervisory rating and capital ratios. Banks that are engaged in excessively risky activities should pay a higher premium, regardless of whether those activities are financed by insured deposits, FHLB advances, or alternative wholesale funding sources. The professional and capable FDIC examination staff is better suited to determining a bank's risk profile than an inflexible formula imposed on all insured institutions, regardless of circumstances.

Discouraging borrowing from the FHLBs would be counterproductive to reducing the risk of failure of FDIC-insured institutions. In fact, discouraging the use of FHLB advances could lead to the perverse effect of increasing risks to FHLB members. Borrowers frequently use FHLB advances for liquidity purposes and to manage interest-rate risk, as well as to fund loan growth. In many markets, the supply of deposit funds is inadequate to meet loan demand and prudent financial

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management needs. Curtailing the use of FHLB advances would force institutions to look to alternative, often more costly wholesale funding sources that are demonstrably more volatile, thereby reducing profitability and increasing liquidity risk.

Penalizing the use of FHLB advances through the imposition of insurance premiums also would conflict with the intent of Congress in establishing the FHLBs, in opening membership in FHLBs to commercial banks in FIRREA, and, more recently, in adopting the Gramm-Leach-Bliley Act, which expanded small banks' access to FHLB advances. The FHLBs' mission is to provide financial institutions with access to low-cost funding so they may adequately meet communities' credit needs to support homeownership and community development. Charging higher assessments to banks utilizing FHLB advances would, in effect, use the regulatory process to vitiate the FHLBs' mission as established and repeatedly reaffirmed by Congress.

During the discussions on FDIC reform legislation over the past several years, Congressional committees and principal sponsors of FDIC reform expressed concern that the FDIC would adversely affect FHLB advances in developing a risk-based insurance assessment proposal. The Congressional intent has been expressed in both the House and Senate on a bi-partisan basis. Both the House Budget Committee report on reconciliation (November 7, 2005) and the House Financial Services Committee report on deposit insurance reform (April 29, 2005) contained such expressions of concern. In addition, Senator Tim Johnson (D-SD), in a Senate Floor statement on November 3, 2005, stated that FDIC reform legislation was not intended to result in increased insurance premiums simply because an institution holds FHLB advances. Congressman Spencer Bachus (R-AL) gave a similar statement on the House Floor on December 19, 2005. Congressman Richard Baker (R-LA) also made statements on the House Floor, on April 7, 2003 and June 5, 2002, expressing strong concern that the FDIC might classify institutions with certain amounts or percentages of FHLB advances as more risky and, therefore, charge them higher premiums. Congressman Baker said that such actions would contradict Congress' clear intent to broaden access to FHLB advances under the Gramm-Leach-Bliley Act. In brief, the legislative history indicates that the FDIC should not charge premiums based on an institution's use of FHLB advances.

Finally, a regulatory and legal structure is already in place to ensure collaboration between the FDIC and the FHLBs. If an FDIC-insured institution is experiencing financial difficulties, the FDIC and the relevant FHLB are required by regulation to engage in a dialogue to ensure that the institution has adequate liquidity while minimizing other risks, including losses to the FDIC. In addition, the FHLBs are provided with the legal authority for confidential access to examination reports to assist with this analysis.

The cooperative relationship between the FHLBs and their member financial institutions has worked remarkably well for 75 years. FHLB advances serve as a critical source of credit for housing and community development purposes, support sound financial management practices, and allow member banks throughout the nation to remain competitive. FHLB membership has long been viewed as protection for the deposit insurance funds because FHLB members have access to guaranteed liquidity. Penalizing financial institutions for their cooperative relationship with the FHLBs would result in their being less competitive, limit credit availability in the communities they serve, and limit their use of a valuable liquidity source, all for no justifiable economic or public policy reason. Accordingly, I urge the FDIC not to include FHLB advances in the definition of volatile liabilities when calculating risk-based premiums for deposit insurance.

Sincerely,

Michael W. Harrington

Michael W. Harrington
Senior Vice President and Treasurer