THE FINANCIAL SERVICES ROUNDTABLE

Impacting Policy. Impacting People.

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November 19, 2007

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

Re: Advance Notice of Proposed Rulemaking: Assessment Dividends, RIN 3064-AD19

Dear Mr. Feldman:

The Financial Services Roundtable[1] ("Roundtable") appreciates the opportunity to comment on the Advanced Notice of Proposed Rulemaking ("ANPR") published on September 18, 2007,[2] pertaining to assessment dividends. This ANPR is the first step in the Federal Deposit Insurance Corporation's ("FDIC") process of developing "a permanent final rule to implement the dividend requirements of the Federal Deposit Insurance Reform Act of 2005 ("Reform Act") and the Federal Deposit Insurance Reform Conforming Amendments Act of 2005" to replace existing temporary FDIC regulations on assessment dividends which will expire on December 31, 2008.

Summary of this comment letter

The FDIC has established a Designated Reserve Ratio ("DRR") of 1.25% for the Deposit Insurance Fund's ("DIF") and is in the process of reaching that level by levying what is tantamount to an across-the-board, non-risk-sensitive fund-building charge of 3 basis points ("bps") in addition to a risk-based premium. Most likely, the DIF reserve ratio will reach 1.25% next year or in 2009. Each basis point of this fund-building charge currently costs the banking industry almost $700 million annually. This is an expensive tax on deposits presumably intended to build the DIF to an excessively high 1.25% reserve ratio.

For the Category I banks which accounted for 98.4% of the DIF assessment base on March 31, 2007, that fund-building charge comes on top of a "base assessment rate schedule" of 2 bps to 4 bps. Where a bank falls within that premium rate range reflects an FDIC determination of the bank's risk of failure. Consequently, Category I banks currently pay an annual premium rate between 5 bps and 7 bps.

In previous communications to the FDIC,[3] the Roundtable has strongly expressed its position that the DRR of the FDIC's DIF does not need to rise materially above the statutory

[1] The Financial Services Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, investment products and services to the American consumer. Roundtable member companies provide fuel for America's economic engine accounting directly for $18.3 trillion in managed assets, $678 billion in revenue and 2.1 million jobs.

[2] 72 *Federal Register* 53181 (September 18, 2007).

[3] August 16, 2006; September 22, 2006; October 27, 2006; and November 1, 2007.

minimum of 1.15% due to the stability of deposit levels, the lengthy time period allowed by law to restore the DIF reserve ratio to 1.15% should it drop below that level, and the insignificant risk of loss that insured institutions pose to the DIF in today's regulatory environment, as reflected in the attached table (Base Case Scenario).

Rather than continuing to levy premiums at a rate sufficient to build the DIF reserve ratio to 1.35% (at which point assessment dividends can be paid), the FDIC should trim its premiums sufficiently to hold the reserve ratio at or below 1.25%. However, the Roundtable does not consider the 1.25% reserve ratio to be the floor below which the reserve ratio should never drop. Rather, the 1.25% reserve ratio is simply the mathematical mid-point in the permissible DRR range Congress established for the DIF.

In addition to eliminating the fund-building charge, holding the reserve ratio at or below 1.25% could possibly enable the FDIC to lower its base rate schedule for Category I institutions. As the FDIC noted in this ANPR, "the FDIC can, if it chooses, reduce the probability of a dividend occurring thereafter" if it reduces the base rate schedule below the current 2 bps to 4 bps. The Roundtable *strongly recommends* that the FDIC make that choice, reducing the base rate schedule to 0 bps to 2 bps, if necessary, to hold the reserve ratio to 1.25%, or even lower.

Discussion

As the ANPR states, "the Federal Deposit Insurance Act ("FDI Act"), as amended by the Reform Act, requires that the FDIC, under most circumstances, declare dividends from the [DIF] when the reserve ratio at the end of a calendar year exceeds 1.35 percent, but is no greater than 1.5 percent. In that event, the FDIC generally must declare one-half of the amount in the DIF in excess of the amount required to maintain the reserve ratio at 1.35 percent as dividends to be paid to insured depository institutions." [emphasis supplied]

Essentially, the FDIC has the statutory authority to levy premiums at a sufficiently high level to build the DIF reserve ratio to 1.35% and then, after the reserve ratio reaches that level, to continue to levy premiums at a sufficiently high rate to build the reserve ratio to 1.50% even after paying a portion of the premium assessment as an assessment dividend once the reserve ratio reaches 1.35%. In effect, institutions will pay the FDIC substantial premiums in the near future with the hope of a partial return of those premiums, in the form of a dividend, sometime in the distant future.

The Base Case Scenario table in the attachment quantifies how costly it will be to the banking industry, its customers, and the economy overall for banks to pay a sufficient amount of premiums to build the DIF to 1.35% so that the FDIC can then begin returning a portion of future premium payments to banks in the form of assessment dividends. The following bullet points reflect these most-reasonable assumptions in this table:

- The DIF reaches a 1.25% reserve ratio at the end of 2009.
- Both insured deposits and the DIF assessment base grow 5% annually thereafter, which approximates the annual growth rate over time for nominal GDP.
- The annual yield on DIF investments is 5%.

Based on these assumptions, the FDIC would have to charge an additional across-the-board annual premium of approximately .6 bps over and above the premium rates needed to hold the DIF reserve ratio at 1.25% to build the reserve ratio from 1.25% to 1.35% over a ten-year period (2010 to 2019). If the FDIC sought to build the reserve ratio from 1.25% to 1.35% over a five-year period (2010 to 2014), it would have to charge an additional across-the-board premium rate of approximately 1.2 bps. Altering the above assumptions to reflect 3% and 7% annual growth rates for insured deposits and the DIF assessment base (appended as the Slow Growth Scenario and the Fast Growth Scenario) and making corresponding adjustments in the DIF investment yield (4% and 6%) does not materially alter these estimates of the additional premium rate banks would have to pay to build the reserve ratio to 1.35% so that the FDIC could then begin rebating a portion of premiums collected after the reserve ratio exceeds 1.35%.

To express this additional cost to the banking industry in another way, the present value, as of the end of 2009, of the additional premium assessments needed to build the DIF reserve ratio to 1.35% is approximately $4 billion. This amount is an unnecessary, burdensome, and dead-weight tax the FDIC should not impose on the banking industry, its customers, and the economy.

Once the DIF reserve ratio reached 1.35%, there would be an additional cost to the banking industry if premiums were collected at a sufficiently high rate to pay dividends since the FDIC can pay dividends equal to only one-half of any increase in the reserve ratio above 1.35%. While the Roundtable has not estimated that additional cost, it certainly is well above zero and therefore not beneficial to the banking industry, its customers, or the economy.

Therefore, the Roundtable *recommends* that the FDIC take such actions as are necessary to hold the DIF reserve ratio at or below 1.25%, even if that means reducing the base rate schedule for Category I banks to as low as 0 bps to 2 bps. Further, so as to not overshoot its present 1.25% DRR target, the FDIC should begin to reduce its fund-building charge as the reserve ratio approaches 1.25%. Slowing the speed at which the reserve ratio reaches 1.25% is consistent with the Roundtable's November 1, 2007, letter to the FDIC Board of Directors commenting on the 2008 assessments rates for the DIF.

The FDIC should adopt a highly simplified dividend policy should the DRR reach 1.35%

Even if the FDIC acts aggressively, as it should, to hold the DIF reserve ratio at or below 1.25%, it is conceivable that the reserve ratio might reach 1.35%, even with a base rate schedule for Category I banks of 0 bps to 2 bps. This could happen through a combination of a substantial reduction in the FDIC's operating expenses, slow deposit growth relative to economic growth, a decline in insured deposits as a percentage of total domestic deposits, a continued low level of bank insolvency losses, and an increased rate of return on the FDIC's investment portfolio. However, under this scenario, it would take many years, if not several decades, for the reserve ratio to reach 1.35%, if it ever did.

Accordingly, many years would pass before the FDIC would pay any assessment dividends. However, since the FDIC needs to adopt a permanent Assessment Dividends rule by the end of next year, the Roundtable *recommends* that the FDIC adopt the Payments Method option, structured as simply as possible. The payments look-back period should be relatively short, with certainly no more than a three-year or a five-year look-back. So as to discourage risky banking, premium payments in excess of the maximum rate for Category I banks should be excluded from the premium-payments calculation. Given the administrative difficulty of tracking mergers, acquisitions, and branch purchases and sales over several decades, no weight should be given to the 1996 assessment base or to any merger, acquisition, purchase or sale transaction that closed prior to the beginning of the premium-payments look-back period. The FDIC also should not attempt to introduce premium redistribution into a permanent assessment dividends rule by differentiating, such as between "newer" and "older" institutions, as that would add unnecessary complexity to the rule.

Conclusion

The Roundtable understands that the FDIC needs to adopt a permanent Assessment Dividends rule by the end of next year. However, there is no urgency for the FDIC to levy premiums at rates that would steadily build the DIF reserve ratio to 1.35%. As noted above, the present-value cost of the additional premium charges needed to build the reserve ratio to 1.35% falls in the range of $4 billion – creating a significant cost burden on the American banking industry. Instead, the FDIC should set the premium rate range for Category I banks to hold the reserve ratio to no more than 1.25%, even if that means dropping the lower end of a 2 bps rate range for Category I banks to as low as 0 bps. Although it is highly unlikely that the reserve ratio would ever reach 1.35% if the FDIC takes the steps necessary to hold the reserve ratio at or below 1.25%, the FDIC should adopt a highly simplified Payments Method procedure as its permanent Assessment Dividends rule on the slight chance that the reserve ratio would eventually grow to 1.35%.

The Roundtable welcomes the opportunity to work with the FDIC to refine the design of an Assessment Dividends rule based on a highly simplified version of the Payments Method option described in the ANPR. Please contact me or Melissa Netram of the Roundtable staff at 202-289-4322 if you have any questions regarding this matter.

Sincerely,

Richard M. Whiting

Richard M. Whiting
Executive Director and General Counsel

Attachment

Appendix I - Deposit Insurance Fund projection, based on the FDIC's Assessment Dividends proposal

Base Case Scenario

Dollars in thousands

						10-year build-up to 1.35%			5-year build-up to 1.35%		
End of Year (EOY)	Rate of growth = 5.0% Insured deposits (EOY)	DIF balance at ratio of 1.25%	1.35%	Fund balance differential	Annual growth rate in assessment base = 5.0%	Additional Assessment rate (bp) = **0.607**	DIF investment yield = 5.0%	Additional growth in DIF balance	Additional Assessment rate (bp) = **1.214**	DIF investment yield = 5.0%	Additional growth in DIF balance
Memo: 6-30-07	4,229,874,000	51,227,000			6,815,248,000						
2009	4,561,400,000	57,017,000	N/A								
2010	4,789,470,000	59,868,375	64,657,845	4,789,470	7,700,000,000	467,390	11,685	479,075	934,780	23,370	958,150
2011	5,028,943,500	62,861,794	67,890,737	5,028,944	8,085,000,000	490,760	36,223	1,006,057	981,519	72,445	2,012,114
2012	5,280,390,675	66,004,883	71,285,274	5,280,391	8,489,250,000	515,297	63,185	1,584,540	1,030,595	126,371	3,169,079
2013	5,544,410,209	69,305,128	74,849,538	5,544,410	8,913,712,500	541,062	92,754	2,218,356	1,082,125	185,507	4,436,711
2014	5,821,630,719	72,770,384	78,592,015	**5,821,631**	9,359,398,125	568,115	125,121	2,911,592	1,136,231	250,241	**5,823,184**
2015	6,112,712,255	76,408,903	82,521,615	6,112,712	9,827,368,031	596,521	160,493	3,668,606			
2016	6,418,347,868	80,229,348	86,647,696	6,418,348	10,318,736,433	626,347	199,089	4,494,042			
2017	6,739,265,261	84,240,816	90,980,081	6,739,265	10,834,673,254	657,665	241,144	5,392,850			
2018	7,076,228,524	88,452,857	95,529,085	7,076,229	11,376,406,917	690,548	286,906	6,370,304			
2019	7,430,039,951	92,875,499	100,305,539	**7,430,040**	11,945,227,263	725,075	336,642	**7,432,022**			
				Additional premium payments		**5,878,781**			**5,165,250**		
				Present value of additional premium payments at 12-31-09:							
				At a 5% discount rate		4,451,333			4,451,333		
				At a 10% discount rate		3,477,294			3,879,890		
				Average of four present values		**4,064,963**					

Appendix II - Deposit Insurance Fund projection, based on the FDIC's Assessment Dividends proposal
Slow Growth Scenario
Dollars in thousands

						10-year build-up to 1.35%			5-year build-up to 1.35%		
End of Year (EOY)	Rate of growth = 3.0% Insured deposits (EOY)	DIF balance at ratio of 1.25%	DIF balance at ratio of 1.35%	Fund balance differential	Annual growth rate in assessment base = 3.0%	Additional Assessment rate (bp) = **0.573**	DIF investment yield = 4.0%	Additional growth in DIF balance	Additional Assessment rate (bp) = **1.173**	DIF investment yield = 4.0%	Additional growth in DIF balance
Memo: 6-30-07	4,229,874,000	51,227,000			6,815,248,000						
2009	4,561,400,000	57,017,000	N/A								
2010	4,698,242,000	58,728,025	63,426,267	4,698,242	7,700,000,000	441,210	8,824	450,034	903,210	18,064	921,274
2011	4,839,189,260	60,489,866	65,329,055	4,839,189	7,931,000,000	454,446	27,090	931,571	930,306	55,457	1,907,038
2012	4,984,364,938	62,304,562	67,288,927	4,984,365	8,168,930,000	468,080	46,624	1,446,275	958,215	95,446	2,960,699
2013	5,133,895,886	64,173,699	69,307,594	5,133,896	8,413,997,900	482,122	67,493	1,995,890	986,962	138,167	4,085,828
2014	5,287,912,763	66,098,910	71,386,822	**5,287,913**	8,666,417,837	496,586	89,767	2,582,244	1,016,571	183,765	**5,286,163**
2015	5,446,550,145	68,081,877	73,528,427	5,446,550	8,926,410,372	511,483	113,519	3,207,246			
2016	5,609,946,650	70,124,333	75,734,280	5,609,947	9,194,202,683	526,828	138,826	3,872,900			
2017	5,778,245,049	72,228,063	78,006,308	5,778,245	9,470,028,764	542,633	165,769	4,581,302			
2018	5,951,592,401	74,394,905	80,346,497	5,951,592	9,754,129,627	558,912	194,430	5,334,644			
2019	6,130,140,173	76,626,752	82,756,892	**6,130,140**	10,046,753,515	575,679	224,899	**6,135,222**			
				Additional premium payments		**5,057,978**			**4,795,265**		
				Present value of additional premium payments at 12-31-09:							
				At a 4% discount rate		4,063,467			4,259,648		
				At a 8% discount rate		3,331,194			3,811,863		
				Average of four present values		**3,866,543**					

Appendix III - Deposit Insurance Fund projection, based on the FDIC's Assessment Dividends proposal
Fast Growth Scenario
Dollars in thousands

						10-year build-up to 1.35%			5-year build-up to 1.35%		
End of Year (EOY)	Rate of growth = 7.0% Insured deposits (EOY)	DIF balance at ratio of 1.25%	1.35%	Fund balance differential	Annual growth rate in assessment base = 7.0%	Additional Assessment rate (bp) = **0.642**	DIF investment yield = 6.0%	Additional growth in DIF balance	Additional Assessment rate (bp) = **1.254**	DIF investment yield = 6.0%	Additional growth in DIF balance
Memo: 6-30-07	4,229,874,000	51,227,000			6,815,248,000						
2009	4,561,400,000	57,017,000	N/A								
2010	4,880,698,000	61,008,725	65,889,423	4,880,698	7,700,000,000	494,340	14,830	509,170	965,580	28,967	994,547
2011	5,222,346,860	65,279,336	70,501,683	5,222,347	8,239,000,000	528,944	46,419	1,084,533	1,033,171	90,668	2,118,386
2012	5,587,911,140	69,848,889	75,436,800	5,587,911	8,815,730,000	565,970	82,051	1,732,553	1,105,493	160,268	3,384,146
2013	5,979,064,920	74,738,312	80,717,376	5,979,065	9,432,831,100	605,588	122,121	2,460,262	1,182,877	238,535	4,805,559
2014	6,397,599,464	79,969,993	86,367,593	**6,397,599**	10,093,129,277	647,979	167,055	3,275,296	1,265,678	326,304	**6,397,541**
2015	6,845,431,427	85,567,893	92,413,324	6,845,431	10,799,648,326	693,337	217,318	4,185,951			
2016	7,324,611,627	91,557,645	98,882,257	7,324,612	11,555,623,709	741,871	273,413	5,201,236			
2017	7,837,334,441	97,966,681	105,804,015	7,837,334	12,364,517,369	793,802	335,888	6,330,926			
2018	8,385,947,852	104,824,348	113,210,296	8,385,948	13,230,033,585	849,368	405,337	7,585,631			
2019	8,972,964,201	112,162,053	121,135,017	**8,972,964**	14,156,135,936	908,824	482,403	**8,976,857**			
				Additional premium payments		**6,830,023**			**5,552,799**		
				Present value of additional premium payments at 12-31-09:							
				At a 6% discount rate		4,866,631			4,641,373		
				At a 12% discount rate		3,624,797			3,942,550		
				Average of four present values		**4,268,838**					