ICBA
Independent Community Bankers of America®

October 26, 2018

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

Re: Limited Exception for a Capped Amount of Reciprocal Deposits from Treatment as Brokered Deposits (RIN 3064-AE89)

Dear Mr. Feldman:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the FDIC's proposal to conform its current regulations that implement brokered deposits and interest rate restrictions with changes to section 29 of the Federal Deposit Insurance Act (the "FDI Act") made by section 202 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (the "Regulatory Relief Act") related to reciprocal deposits, which took effect May 24, 2018. This rulemaking is the first part of a two-part effort to revise the brokered deposit rules. The second part, which is planned for later this year, will seek comment on the brokered deposit regulations generally including the interest rate restrictions that apply to brokered deposits.

Prior to the enactment of the Regulatory Relief Act, all reciprocal deposits were classified as brokered deposits. Section 202 of the Regulatory Relief Act amends section 29 of the FDI Act to except a capped amount of reciprocal deposits from treatment as brokered deposits for certain insured depository institutions. Even though Section 202 was effective on the date of enactment (i.e., May 24, 2018), the FDIC is proposing to amend its regulations to conform with the statutory amendments. According to the FDIC, as of March 31, 2018, there were 5,616 FDIC-insured institutions. Of these, 2,528 institutions report having brokered deposits which totaled $980 billion. Of the institutions reporting brokered deposits, 1,185 institutions also report having reciprocal deposits, totaling $48 billion.

[1] The Independent Bankers of America® creates and promotes an environment where community banks flourish. With more than 52,000 locations nationwide, community banks constitute 99 percent of all banks, employ more than 760,000 Americans and are the only physical banking presence in one in five U.S. counties. Holding more than $4.9 trillion in assets, $3.9 trillion in deposits, and $3.4 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America. For more information, visit ICBA's website at www.icba.org.

ICBA's Comments

Community banks that hold reciprocal deposits were very pleased when the Regulatory Relief Act was enacted. Reciprocal deposits allow a community bank to accept a deposit from its customer that exceeds the $250,000 insurance limit and distribute portions of it through a network of banks and in turn receive a like amount of reciprocal deposits from other banks in the network. This solution allows a large local depositor – such as a local government or foundation – to obtain full deposit insurance coverage and allows banks to accept an equivalent amount of deposits to support local lending.

Before the Regulatory Relief Act was enacted, reciprocal deposits were caught up in the definition of "brokered deposit" under the FDI Act even though studies showed that reciprocal deposits act similarly to other core deposits: they are from local customers, earn the local interest rate, and are stable sources of funding. Because reciprocal deposits were classified as brokered deposits, their status was always a concern to community banks particularly if the bank were ever downgraded to less than well capitalized under the FDIC's Prompt Correction Action (PCA) rules. If that happened, the bank would have to divest itself of all brokered deposits (including reciprocal deposits) if it could not obtain a waiver from the FDIC.

ICBA commends the FDIC for conforming its regulations with the statutory changes and clarifying a number of points about the reciprocal deposit exception in the brokered deposits rule. Furthermore, we agree with the FDIC that if 12 CFR Section 337.6 had not been amended to conform to the statutory changes, many community banks would have remained confused about the statutory changes for call report purposes.

For instance, the rule spells out that an "agent institution" is an insured depository institution that places a covered deposit through a deposit placement network at other insured depository institutions in amounts that are less than or equal to the standard maximum deposit insurance amount, and specifies the interest rate to be paid for such amounts. As long as the institution is well capitalized and well rated (i.e., a composite CAMELS rating of either "1" or "2") the institution is an "agent institution." An "agent institution may accept reciprocal deposits up to the lesser of (1) $5 billion or (2) an amount equal to 20 percent of the agent institution's total liabilities—which the proposal refers to as the "general cap."

The Definition of "Special Cap" Needs to be Consistent with the Statute

While we have no concerns with the definitions of "agent institution" and "general cap," we believe the FDIC is misinterpreting the statute in how it defines the "special cap." According to the FDIC's interpretation of the proposed rules, the special cap applies if the institution is either not well rated or not well capitalized. In this case, the institution can meet the definition of "agent institution" only if it *maintains* or *holds* its reciprocal deposits at or below the special cap, which is the average amount of reciprocal deposits held at quarter-end during the last four quarters preceding the quarter that the institution fell below well capitalized or well

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rated. If that special cap amount is below the amount of reciprocal deposits that the institution currently holds, then, according to the FDIC's interpretation, the institution must reduce its reciprocal deposits to the lower amount.

However, the statutory language is clear that the prohibition that applies to institutions that are not well rated or not well capitalized only refers to receiving deposits, not to maintaining or holding them. Nowhere does the new section 29(i) of the FDI Act, added by section 202 of the Regulatory Relief Act, limit the amount of reciprocal deposits that an institution can "maintain," "retain," or "hold." Merely retaining reciprocal deposits that an institution accepted before becoming subject to the special cap is not "receiving" deposits; accordingly, there is no basis to say that the institution must necessarily "lower its reciprocal deposits to within the special cap."

For instance, if an institution holds $50 million in reciprocal deposits and then is downgraded to a composite rating of "3" or below, the institution should only be prohibited under the special cap from *receiving* deposits that would cause it to exceed its cap, not *retaining* them in the amount of $50 million. This would be true even if the institution's preceding four-quarter average of reciprocal deposits was $25 million, because the institution is merely retaining existing deposits and is not "receiv[ing]" deposits that cause the average to be exceeded. The institution should be able to keep its $50 million in reciprocal deposits until they mature or until customers withdraw them.

Moreover, the institution should be free to accept additional reciprocal deposits as long as it does not exceed the institution's preceding four-quarter average of reciprocal deposits. For instance, if the preceding four-quarter average of reciprocal deposits was higher—say $75 million—then the institution should be able to accept $25 million more in reciprocal deposits.

Conclusion

The FDIC should be commended for conforming its regulations in 12 CFR Section 337.6 with the statutory changes of Section 202 of the Regulatory Relief Act. Our only concern is with the FDIC's interpretation of how to apply the "special cap" and specifically that the prohibition only applies to receiving deposits and not retaining them.

Overall, ICBA was very pleased with the change in the law and the brokered deposit exception for reciprocal deposits. From the standpoint of deposit insurance assessments, the FDIC estimates that only 30 banks would have lower assessments resulting in a reduction of about $4.3 million annually in aggregate assessment revenue to the Deposit Insurance Fund. We believe that is a small price to pay for the change in the law. ICBA looks forward to the second part of the rulemaking when the FDIC will seek comment on the brokered deposit regulations generally including the interest rate restrictions that apply to brokered deposits.

ICBA appreciates the opportunity to comment on the FDIC's proposed regulations concerning the reciprocal deposit exception to the brokered deposit rules. If you have any questions or would like additional information, please do not hesitate to contact me by email at Chris.Cole@icba.org.

Sincerely,
/c/Christopher Cole

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