October 16, 2019

To Robert E. Feldman, Executive Secretary

Attention: Comments Regarding September 4, 2019 - Interest Rate Restrictions on Institutions That Are Less Than Well Capitalized
12 CFA Part 337
Comment Request (RIN 3064–AF02)

Federal Deposit Insurance Corporation, 550 17th Street, NW, Washington, DC 20429

Dear Mr. Feldman,

Thank you again for the opportunity to comment. My earlier comment letter describes my bank, so I will not repeat that. I would like to submit these additional comments in the order that the subject matter appears in the NPR.

I am in total agreement with the purpose of the proposed rule, and am very grateful that the FDIC has recognized the problem and is planning a solution.

Calculation of National Rate
Using the rates being reported in the current rate survey has yielded a National rate that is well below market rates, as illustrated in Chart 1. I think it is imperative that the new rules give a permanent solution across all rate cycles and all deposit terms so that the threat of an artificial liquidity crisis doesn't cause the DIF any further unnecessary losses. I know we are all united in that effort and goal. The question of how to properly weight each institution's reported rates doesn't have an answer that will ever produce anything close to a true market rate as long as the institutions' actual rates being paid are not reflected in the surveyed rates that are being used to calculate the rate cap. As illustrated in the NPR, there is not a lot of difference in the per branch method and the market share method. I would prefer that two or three of the other proposed methods be used than to continue to use this survey which has, for the last four years, produced a national average rate that is below true market rates.

The NPR lists the reasons why the surveyed rates do not accurately reflect actual rates being paid. Because it is known that the surveyed rates omit vital information on actual rates paid, the rate cap should be based on some other, more accurate information.

Local Rate Cap Calculation
Offering 90 percent of the highest rate being paid in a local market is not usually going to be high enough to attract or retain deposits. This calculation needs to result in a rate that allows a troubled bank to be able to at least retain its current deposit base.

Section 29 and Local Rate Cap
The law restricts a "troubled" institution from offering rates significantly higher than the prevailing rates being offered in that institution's market area. I guess the law has been interpreted to mean that credit union rates can't be used for establishing a local rate cap. Although credit unions can usually offer very competitive rates, internet banks usually offer the highest rates in any market. Therefore, whether or not a credit union's rates should be used to calculate a local rate is a less important question than whether or not internet rates which are being offered, or available, within a certain market area may be used.

To give two examples of "local" market competition, I recently had these scenarios happen in one day:

1. A CD-only current customer came in to get our rates on a 5 year non-jumbo CD. I quoted a 2.02% APY, but he stated he could get 2.60% APY from our local credit union. The current National rate is 1.02 and the rate cap is 1.77. I assure you that 90% of 2.60% would not bring in that deposit.
2. A long-time, multi-services customer had a 12 month jumbo CD maturing. I quoted 2.02% for the renewal, and he cited an internet rate of 2.50% which was for non-jumbo amounts. Today's National rate for this CD is 0.59 and the rate cap is 1.34.

Prevailing Rate

These are very typical situations, and probably happen just like this thousands of times each day across the country. If a poll were taken of every bank across the country, I believe the vast majority of bankers would say that the prevailing rate in any market area is far, far above the FDIC-defined national rate. I suppose at issue here is the definition of prevailing. That aside, we know that an institution will be put in a liquidity crisis if it's not allowed to at least pay a competitive rate for deposits, and we know that the intent of the law and the rules was never to put an otherwise viable FI into an artificial crisis.

Proposed National Rate Cap

We are on the right track (correcting the flawed rate cap and adding an additional option for calculating the rate cap) – but on the wrong train (still using the flawed survey and not capturing actual rates being paid). "The rate offered at the 95^{th} percentile of rates weighted by domestic deposit share" may come very close to approximating a prevailing rate, even though the rates used from the survey are, for the most part, not the actual rates being paid. Because of the fact that the survey doesn't represent actual market rates, I can not agree that the 95^{th} percentile sets a reasonable proxy for rates that significantly exceed the prevailing rate. If we could agree that the 95^{th} percentile does give us a prevailing rate, then we would need to add the 75 basis points to that number to arrive at the "significantly exceeds" rate. The second alternative, as illustrated in Chart 2, is worse than the current rate cap in three categories, and not much better in the rest. I believe other alternatives would be more dependable and accurate.

Table 3, Proposed Rate Cap as of May 20, 2019

While this table illustrates that the new rate cap would be a lot better than the current rate cap, it still is not high enough to allow troubled banks to attract or retain deposits over all terms. On that date, our rates (APY's) were priced just to maintain our status quo, and those above the new rate cap were as follows:

6 month CD 2.49 (local credit union offering 1.75)
24 month CD 2.80
36 month CD 2.95
48 month CD 3.05
60 month CD 3.21
We don't offer 1 month and 3 month CDs.

During May, according to the same rate survey used by the FDIC for these calculations, one of our competitors was offering a 1 month CD rate at 2.50% APY! Another bank was offering 2.65% APY for a 9 month CD (rate cap as proposed would allow an APY of 1.21% for 9 months).

Historical Data, Appendix 1

First Three Charts

As illustrated in these charts, the proposed rate cap would not be high enough to allow a restricted institution to compete for deposits in most rate environments. That is, if you allow the assumption that the Average of Top 10 Offered Rates is a fair proxy for current actual (prevailing) market rates.

CD Charts

These charts clearly show that the proposed rate caps will still not allow restricted FIs to compete for deposits and avoid a liquidity crisis across all rate environments. Bringing in the original rate cap which was used from 1992 to 2009 corrects the deficiencies in the first few years (2005-2008-ish) and the last several years (2013+ in the longer terms and 2015+ in the shorter terms). However, none of the rate caps on these charts provide a solution for the 2008-2009 environment. This is the missing piece that must be found. It looks to me like using the higher of the original cap and the "missing piece" formula is what is needed. I would be interested to see how my suggestion of the 95th percentile plus 75 b.p. looks on the charts. However, there is probably a better "missing piece" formula that doesn't continue to use the current flawed rate survey.

Local Rate Cap

Offering 90 percent of a competitor's rate will not be enough to attract or retain most deposits. I would suggest setting a cap of 75 basis points above the top rate in the market. Also, in determining competing institutions within a market area, rates offered by an online bank in that FI's market area should be allowed to be used in determining the local rate cap. If the national rate cap gets set at an actual workable level, then local rate caps should be irrelevant. Also in that case, troubled FIs would also be able to compete outside of their local market for deposits.

I welcome the proposed change in allowing the use of off-tenor products in calculating a local rate cap, and the proposal to eliminate the two-step process.

Treatment of Non-Maturity Deposits for Purposes of the Interest Rate Restrictions

Although I'm not sure how many systems are sophisticated enough to handle the proposed interpretation, I think this option could be helpful in some cases. Again, however, if we can get the rate cap to work consistently in all rate environments, the need for this should be minimal.

Alternatives

I'm in favor of using at least two or three methods and using the highest of all methods approved. The original method using U.S. Treasury rates seems to be the most accurate in all except one of the cycles pictured in Chart 3. I strongly believe that the UST rate does warrant the multiplier plus 75 b.p. There are many places over the years where the old method is barely above the Top Rates, and as I said, I think the Top Rates are a close representation of actual market rates.

For non-maturity deposits, you could use the higher of the 3 month Treasury or the high end of the Fed Funds target and then add 75 bp.

Average of the Top-Payers

I think using the average of the top-25 rates offered would only be workable if that rate itself was considered to be the prevailing rate, and the 75 bp cushion was added to it to cover the "significantly exceeds" interpretation. I don't understand how the interpretation came about that an "average" rate, using all rates to calculate it, could be equivalent to a prevailing rate. Doesn't "prevailing" mean something totally different than what "average" means?

It would help to be able to see some of the alternatives illustrated in charts over many years to see how they perform through economic fluctuations.

One Vote Per Institution
The one bank one vote seems better than the old cap and worse than the proposed cap. Let's don't do worse.

Impact of the Proposed Rule in Less Favorable Economic Environments
A less-than-well-capitalized FI needs to be able to maintain its deposits and liquidity during stress events so as to avoid an unnecessary liquidity shortfall that could result in the failure of the bank and loss to the DIF. It has been our experience with regulators that there are plenty of tools available to curtail excessive growth when it appears to be causing an undesirable scenario. Using these tools on a case-by-case, as-needed basis seems to be a better idea than tying the hands of everyone with constrictive rules. No bank wants to pay a rate that significantly exceeds the current market rate. In this day and time, money markets are advanced to a point that no bank has to pay above-market rates for funding. Market rates that are available to all insured FIs are fairly well-defined, and within a relatively narrow range. The problem of excessive growth would be better handled by close supervision and proper regulator pressure. What we do know is that not allowing a problem bank to pay competitive rates on deposits is a recipe for an artificial liquidity crisis and possible failure, followed by a loss to the DIF.

Thank you so much again for addressing this serious problem. I hope the final rule will result in a rate cap which is workable throughout all cycles.

Sincerely,

Mary Fowler, CEO
The Peoples Bank
Magnolia, AR