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

Re: RIN 3064-AF02

Ladies and Gentlemen:

On behalf of Promontory Interfinancial Network, LLC ("*Promontory Network*"),[1] I write to comment on the Notice of Proposed Rulemaking on the Interest Rate Restrictions on Institutions That Are Less Than Well Capitalized, issued by the Federal Deposit Insurance Corporation (the "*FDIC*") and published in the Federal Register on September 4, 2019 (the "*NPR*").[2]

INTRODUCTION AND SUMMARY

The NPR requests "comment on a proposal that attempts to ensure that deposit interest rate caps appropriately reflect the prevailing deposit interest rate environment, while continuing to ensure that less than well capitalized institutions do not solicit deposits by offering interest rates that significantly exceed prevailing rates on comparable deposit products."[3]

In addition to proposing a change in how interest rate ceilings are determined, the NPR states that the FDIC is "considering an interpretation" of the Federal Deposit Insurance Act (the "*FDI Act*") that addresses when "non-maturity deposits are viewed as 'accepted' and 'solicited' for purposes of the interest rate restrictions."[4] The NPR also mentions that the FDIC plans to institute a future rulemaking on the meaning of the term "accepted."[5]

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[1] Founded in 2002, Promontory Network provides services to the banking and brokerage industries. Promontory Network's deposit allocation and sweep services include CDARS®, the Certificate of Deposit Account Registry Service®, for time deposits, ICS®, the Insured Cash Sweep® service, for non-time deposits, and IND®, the Insured Network Deposits® service, for non-time deposits swept to banks primarily by broker-dealers.

[2] FDIC, *Notice of Proposed Rulemaking on Interest Rate Restrictions on Institutions That Are Less Than Well Capitalized*, 84 Fed. Reg. 46,470 (Sept. 4, 2019).

[3] *Id*. at 46,471.

[4] *Id*. at 46,479.

[5] *Id*.

The NPR acknowledges – quite correctly, in Promontory Network's view – that section 29(e) of the FDI Act restricts interest rates only on deposits that a bank accepts while the bank is not well capitalized. Consistent with section 29(e), the NPR states that, under the proposed interpretation, no rate restriction applies to deposits that are accepted in a non-maturity deposit account before a bank becomes not well capitalized.[6] The NPR adds – again quite correctly, we believe – that "the balance in the initial account would continue to not be subject to the interest rate restrictions so long as no additional funds were accepted" in that account.[7]

The NPR also states, however, that, under the proposed interpretation, the interest rate for an entire account will be restricted if any new deposits are added to it.[8] Promontory Network agrees that, in such circumstances, a limitation that applies to an entire account might be appropriate if there could be only one interest rate for the entire account. But interest rates for an account can be tiered in a way that applies different interest rates to different parts of the balance. When a bank finds that it can more efficiently use a tiering approach to comply with a rate restriction, the bank should be permitted do so.

In addition, the FDIC should reconsider its stated plan to address in a future rulemaking when deposits are "accepted" for purposes of restrictions related to prompt corrective action ("*PCA*"). The FDI Act's language is unambiguous, and the FDIC has long interpreted "accept," and has more recently interpreted the related word "receive," in a manner consistent with the statutory language. Suggesting that the meaning is in doubt when there is no valid ground for doubt would not be helpful.

DISCUSSION

A. The NPR correctly acknowledges that, under section 29(e) of the FDI Act, no rate restriction applies to deposits that a bank accepts while it is well capitalized.

In keeping with the clear language of section 29(e) of the FDI Act, the NPR recognizes that interest rate restrictions do not properly apply to "balances in a money market [deposit] account or other savings account, as well as transaction accounts, at the time an institution falls below well capitalized."[9]

Paragraph (1) of section 29(e) defines "covered insured depository institution" as an insured depository institution that:

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[6] *Id.*

[7] *Id.*

[8] *Id.*

[9] *Id.*

(i) under subsection (c) or (d), accepts funds obtained, directly or indirectly, by or through a deposit broker; or

(ii) . . . accepts reciprocal deposits while not well capitalized.[10]

All the funds and reciprocal deposits described in paragraph (1) are funds or reciprocal deposits that a bank accepts while not well capitalized. Subsection (c) of section 29 permits a bank that is adequately capitalized, but not well capitalized, to accept brokered deposits pursuant to an FDIC waiver, and subsection (d) of section 29 permits acceptance of brokered deposits while not well capitalized for certain conservatorships.[11] Subsection (i) of section 29 permits a bank that is not well capitalized to accept reciprocal deposits under certain circumstances.[12]

Paragraph (2) of section 29(e) states:

> A covered insured depository institution may not pay a rate of interest on <u>funds or reciprocal deposits described in paragraph (1)</u> that, at the time that the funds or reciprocal deposits are accepted, significantly exceeds the limit set forth in paragraph (3).[13]

Because all the "funds or reciprocal deposits described in paragraph (1)" are funds or reciprocal deposits that a bank accepts while not well capitalized, the prohibition in paragraph (2), by its terms, applies only to such funds or reciprocal deposits.

B. The NPR states that the interest rate on an entire account will be restricted if any new deposits are added to it, but the statutory language does not support this result.

The NPR states that, under the FDIC's proposed interpretation, if funds are deposited in an account after a bank becomes not well capitalized, "the entire balance of the account would be subject to the interest rate restrictions."[14] The NPR makes it possible to avoid this result only by accepting no new dollars or by depositing new dollars in a new account: "If, however, the same customer deposited funds into a new account and the balance in that account was subject to the interest rate restrictions, the balance in the initial account would continue to not be subject to the interest rate restrictions so long as no additional funds were accepted."[15]

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[10] 12 U.S.C. § 1831f(e)(1).

[11] *Id.* §§ 1831f(c), 1831f(d).

[12] *Id.* § 1831f(i).

[13] *Id.* § 1831f(e)(2) (emphasis added).

[14] NPR, *supra* note 2, at 46,479.

[15] *Id.* As a threshold point, Promontory Network notes that NPR initially states in general terms that the FDIC "is considering an interpretation under which nonmaturity deposits are viewed as 'accepted' and 'solicited' for purposes of the interest rate restrictions at the time any new non-maturity deposits are placed at an institution." *Id.* If the proposed interpretation asserted that <u>all</u> non-maturity deposits could be viewed as accepted or solicited at the time <u>any</u>

Seeking to provide a practical way to monitor application of rate restrictions to non-maturity deposits is understandable and reasonable. If an account contains $100 that an institution accepted while it was well capitalized, and a new $50 is added to the account after the institution becomes not well capitalized, the FDI Act restricts the interest rate only on the additional $50. But if a single rate applies to the entire $150 balance, then that rate must remain within the rate restriction to comply for the added $50. In many cases, the easiest solution may be simply to open a separate account for new dollars that will be subject to the restriction. The proposed interpretation recognizes that such a solution is fully compliant.

Nevertheless, the proposed interpretation appears to rest on an unstated assumption, which is that only one interest rate can apply to the entire balance in a single account. Contrary to this assumption, banks can and do pay "tiered interest," and in one form of tiered interest, a bank pays interest at different rates on different parts of a depositor's balance.[16] There is no apparent reason a bank could not tier interest in a way that would apply an unrestricted rate to the part of the balance that consists of brokered or reciprocal deposits received before the bank became not well capitalized and apply a restricted rate only to new brokered or reciprocal deposits in the account.[17]

With interest tiering, the restricted rate would apply on a last-in, first-out basis. After the bank became not well capitalized, the interest rate on the previously-accepted deposits in the account would – as under the statute it must – remain unrestricted, and only the rate on new deposits in the account would be restricted. Any withdrawal would then deplete the part of the account containing such new deposits ("*restricted-rate funds*") until no more restricted-rate funds were in the account. For example, if the account held $100 when the bank became not well capitalized, an additional $50 deposited in the account would be restricted-rate funds. A subsequent $30 withdrawal would deplete the restricted-rate funds, leaving intact $20 in restricted-rate funds as well as the original $100, for which the rate would not be restricted. A further $40 withdrawal would delete the remaining $20 of the restricted-rate funds plus $20 of the original $100, leaving funds to which no restriction applied ("*unrestricted-rate funds*") in the amount of $80. Thereafter, no more than $80 would be unrestricted-rate funds, and the process would

new non-maturity deposits were placed <u>at an institution</u>, then it would be inconsistent not only with the plain language of the statute, but also with the more detailed description of the proposed interpretation in the NPR.

The NPR states that, if the same customer deposits any new funds into a new account, "the balance in the initial account would continue to not be subject to the interest rate restrictions so long as no additional funds were accepted." *Id*. We therefore understand that the proposed interpretation is <u>not</u> one in which <u>all</u> non-maturity deposits are viewed as accepted or solicited when any new such deposits are placed at the bank, but one in which all non-maturity deposits <u>in an account</u> are viewed as accepted or solicited when any new such deposits are placed <u>in the account</u>.

[16] *See* Bureau of Consumer Financial Protection, Regulation DD, 12 C.F.R. Part 1030, app. A, part I(D), Tiering Method B (describing interest tiering in which different rates apply to different parts of the balance).

[17] A calculation of annual percentage yield ("*APY*") might be complicated, but Regulation DD often does not require an APY disclosure for accounts that hold brokered or reciprocal deposits. When a custodian rather than a consumer holds an account, as is usually the case for such deposits, only the advertising requirements apply. *See* 12 C.F.R. §§ 1030.1(c), 1030.2(a) (referring to the advertising requirements of 12 C.F.R. § 1030.8). The advertising requirements mandate disclosure of an APY only "[i]f an advertisement states a rate of return." 12 C.F.R. § 1030.8(b).

continue. The effect would be the same as if deposits after the bank became not well capitalized were placed in a separate account from which withdrawals occurred before depletion of the original account. The following table illustrates:

Last-In, First-Out Tiering Illustration

Day	Category/Transaction	Total Balance	Unrestricted-Rate Balance	Restricted-Rate Balance
1	Bank Is Well Capitalized	$100	$100	$0
2	Bank Becomes Not Well Capitalized	$100	$100	$0
3	$50 Deposit	$150	$100	$50
4	$30 Withdrawal	$120	$100	$20
5	$40 Withdrawal	$80	$80	$0
6	$30 Deposit	$110	$80	$30

Although banks might opt for the separate account method outlined in the NPR, the objective of providing a practical way to monitor application of the rate restrictions can be equally well met if a bank determines that it can more efficiently apply the restrictions through a single account with such a tiering approach, perhaps through the use of sub-accounting for internal tracking of the separate components of the balance. As long as the tiering approach prevents the payment of interest at a prohibited rate on brokered or reciprocal deposits that the bank accepts while not well capitalized, such an alternative solution is also fully compliant.

In one of the questions for comment, the NPR specifically asks with respect to the proposed interpretation: "Would there be substantial operational difficulties for institutions to monitor additions to these existing accounts in order to determine when they would be subject to the interest rate restrictions?"[18] The desire not to create operational difficulties at an already challenging time for a bank supports giving banks the option of complying either through a new account or through rate-tiering as described above.

Adding the rate-tiering option not only would bring the NPR's interpretation into more complete harmony with the statute, but also would further the policy goal of protecting the safety and soundness of weakened banks. The NPR itself recognizes that statutory terms such as "significantly exceeds" reflect the importance of avoiding excessive restriction of interest rates that could impair "create an unintentional liquidity strain" and prevent them from being competitive "when they are most in need of predictable liquidity," thus potentially "creat[ing] severe funding problems."[19]

If a bank must reduce the rate at which it pays interest on previously-accepted deposits in an account merely because the bank chooses to apply a rate restriction through rate-tiering, rather

[18] NPR, *supra* note 2, at 46,493.

[19] *Id.* at 46,473.

than establishing a separate account, the bank may lose vital funding for no good reason. This effect is more likely to harm the Deposit Insurance Fund than to help it.

C. The FDIC should reconsider its stated plan to address in a future rulemaking when deposits are "accepted."

The NPR states: "The FDIC plans to address in a future rulemaking when deposits are 'accepted' for purposes of [specified] PCA-related restrictions, both for non-maturity deposits, such as transaction accounts and MMDAs, as well as for certificates of deposits and other time deposits."[20] Because the statutory language is unambiguous, however, the FDIC cannot depart from it.[21] By seeming to suggest that the FDIC might even consider departing from the statutory language, a rulemaking could unintentionally create an unnecessary problem.

The FDIC has long interpreted "accept," and has more recently interpreted the related word "receive," in a manner consistent with the plain language of the FDI Act. On several occasions, the FDIC has even corrected documents that suggested otherwise. For example:

- In January 2015, the FDIC issued a financial institution letter accompanied by an FAQ document.[22] The document erroneously suggested that section 29(a) of the FDIC Act, which prohibits not well capitalized institutions from accepting brokered deposits, prohibits such an institution "from continuing to hold brokered" non-maturity deposit accounts and declared that the institution "must close these accounts."[23] After this issue was raised with senior officials, the FDIC corrected the error in FAQ F5 by withdrawing the erroneous statement quoted above when it issued a revised FAQ document for public comment on November 13, 2015.[24]

- Although no commenter disagreed with the revised FAQ F5, on June 30, 2016, the FDIC issued a new financial institution letter with a further revised version of the FAQs that reinserted erroneous language, indicating that an adequately capitalized institution would be required to request a waiver from the FDIC to "retain or accept" brokered deposits.[25] The issue was again raised with senior officials. The FDIC then issued a further revised version of the FAQ document with a technical correction that deleted

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[20] *Id*. at 46,479

[21] As the Supreme Court famously declared in *Chevron U.S.A. Inc. v. National Resources Defense Council, Inc.*, 467 U.S. 837 (1984), courts and agencies alike "must give effect to the unambiguously expressed intent of Congress." *Id.* at 842-43.

[22] FIL-2-2015, *Guidance on Identifying, Accepting, and Reporting Brokered Deposits* (Jan. 5, 2015).

[23] *Id*., FAQ F5, accompanying FIL-2-2015.

[24] FIL 51-2015 (Nov. 13, 2015).

[25] FIL 42-2016 (June 30, 2016).

"retain or," clarifying that section 29(a) of the FDI Act applies only to deposits that arrive after an institution becomes not well capitalized.[26]

- More recently, in September 2018, the FDIC issued a Notice of Proposed Rulemaking to implement section 202 of the Economic Growth, Regulatory Relief, and Consumer Protection Act. That document contained language that could have been taken to mean that the so-called "special cap" of section 29(i) of the FDI Act, which pertains to the amount of reciprocal deposits that certain institutions can "receive," also restricted the amount of reciprocal deposits that such institutions could "maintain," "retain," or "hold."[27] In December 2018, the FDIC issued the final rule and stated: "Transactional reciprocal deposits are viewed as being 'received' daily."[28] Subsequently, however, the FDIC issued a technical correction modifying the Final Rule to eliminate that language, noting that "[t]he FDIC does not intend [the problematic language] to change existing interpretations related to accepting or receiving deposits."[29]

Other publications from the FDIC further confirm its longstanding interpretation of the term "accept" in the context of section 29:

- In a June 2009 report, the FDIC's Office of Inspector General ("*OIG*") reproduced excerpts from the FDIC's standard form of notification letter to institutions that have dropped to adequately capitalized status. The letter states that "[b]rokered deposits that were previously accepted while the institution was well capitalized . . . do not require a waiver."[30]

- In an earlier advisory opinion on pass-through insurance for employee benefit plans, which at the time of the guidance were eligible for pass-through insurance only if the bank could accept brokered deposits, the FDIC advised that, if an existing deposit had "a stated maturity," such as a time deposit, and was "renewed or 'rolled over' after the prohibition [of the acceptance of brokered deposits became] applicable," the deposit would be "considered newly accepted at the time of renewal and no longer eligible for

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[26] FDIC, *Identifying, Accepting and Reporting Brokered Deposits, Frequently Asked Questions*, F1 (June 30, 2016, with technical correction on July 14, 2016), https://www.fdic.gov/news/news/financial/2016/ fil16042b.pdf.

[27] FDIC, *Limited Exception for a Capped Amount of Reciprocal Deposits From Treatment as Brokered Deposits*, 83 Fed. Reg. 48,562, 48564 (Sept. 26, 2018).

[28] FDIC, *Limited Exception for a Capped Amount of Reciprocal Deposits From treatment as Brokered Deposits*, 84 Fed. Reg. 1,346, 1349 n.28 (Feb. 4, 2019).

[29] FDIC, *Limited Exception for a Capped Amount of Reciprocal Deposits From treatment as Brokered Deposits; Technical Amendments*, 84 Fed. Reg. 15,096 (Apr. 15, 2019).

[30] FDIC, Office of Inspector General, *FDIC's Brokered Deposit Waiver Application Process*, Report No. AUD-09-015, https://www.fdicig.gov/publications/reports09/09-015-508.shtml, at 15 (June 2009) (emphasis added). The reason that funds that were "previously accepted" do not require a waiver is that section 29 does not prohibit a bank from continuing to "hold" or "retain" such funds, so there is no prohibition to be waived.

> pass-through insurance."[31] The advisory opinion added, however, that funds previously "deposited with no stated maturity" would not be deemed to have been "renewed or 'rolled over'" after the prohibition of acceptance and therefore would "continue to be eligible for pass-through insurance until withdrawn."[32]

Although the NPR refers to a planned future rulemaking on when deposits are "accepted" for purposes of PCA-related restrictions, the current rulemaking already applies "accepted" in the context of rate restrictions, which are PCA-related. In applying the term, the current rulemaking necessarily rejects any idea that a bank somehow repeatedly "accepts" or "receives" the same non-maturity deposit after the bank has already credited the funds to an account. If existing balances were treated as being re-"accepted" or re-"received" every day on which they were retained, for example, the NPR simply could not say, as it does, that, if a customer "deposited funds into a new account and the balance in that account was subject to the interest rate restrictions, the balance in the initial account would continue to not be subject to the interest rate restrictions so long as no additional funds were accepted."[33] It is not clear why the FDIC would continue to apply existing practice in the current rulemaking, but simultaneously signal that a future rulemaking conceivably might adopt an unsupported interpretation of the FDI Act.

Accordingly, we suggest that the notice of the final rule in the current rulemaking simply affirm the plain meaning outlined above, rather than – by suggesting that there is an open issue on the question – creating confusion and uncertainty where none should exist. At a minimum, the notice should make clear that the FDIC, in any proposed new rule, will not adopt an interpretation that would be inconsistent with the necessary premise of the current interpretation that, for PCA-related purposes, a bank does not again "accept" or "receive" the same non-maturity deposit after the funds have already been credited to an account at the bank.

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[31] FDIC, *Advisory Opinion* 92-96 (Dec. 18, 1992), https://www.fdic.gov/regulations/laws/rules/4000-7870.html. Then-effective rules did not provide for insuring an employee benefit plan deposit "accepted by an insured depository bank which, at the time the deposit is accepted, may not accept brokered deposits." 58 Fed. Reg. 29,952 (May 25, 1993). As a result, the FDIC interpretation under this rule is instructive. Indeed, the FDIC stated that it viewed its approach under these rules as consistent with its brokered deposit regulations. FDIC, *Advisory Opinion* 92-96, *supra*.

[32] *Id*.

[33] NPR, *supra* note 2, at 46,479.

Thank you for considering our comments. Should you wish to discuss them further, please contact the undersigned at (703) 292-3338 (dphillips@promnetwork.com).

[redacted]

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