ICBA
Independent Community
Bankers of America®

November 4, 2019

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

Re: Interest Rate Restrictions on Institutions That Are Less Than Well Capitalized (RIN 3064-AF02)

Dear Mr. Feldman:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on proposed revisions to FDIC regulations relating to interest rate restrictions that apply to less than well capitalized insured depository institutions (IDIs). Under the proposal, the FDIC would amend the methodology for calculating both the national rate and the national rate cap for deposit products. The national rate would be the weighted average of rates paid by all IDIs for a given deposit product, where the weights are each IDI's market share of domestic deposits. The national rate cap for a particular product would be set at the higher of (1) the 95th percentile of rates paid by IDIs for that product weighted by each IDI's share of total domestic deposits, or (2) the proposed national rate for that product plus 75 basis points.

Furthermore, the FDIC is proposing a simplified version of the current local rate cap calculation. Under the proposal, less than well capitalized IDIs could offer up to 90 percent of the highest rate paid on a particular deposit product in the IDI's local market area.

Background

Section 29 of the Federal Deposit Insurance Act imposes interest rate restrictions on IDIs that are less than well capitalized. Section 29 restricts these institutions from soliciting deposits by

[1] *The Independent Community 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.*

offering rates of interest on deposits that are "significantly higher" than the prevailing rates of interest on deposits offered by other IDIs having the same type of charter in such IDI's normal market area.

The FDIC has implemented the Section 29 statutory restrictions through two rulemakings. As part of the 1992 rulemaking, the "national rate" was defined as "(1) 120 percent of the current yield on similar maturity U.S. Treasury obligations or (2) in the case of any deposit at least half of which is uninsured, 130 percent of such applicable yield. At the time of the 1992 rulemaking, the FDIC did not have readily available data on actual deposit rates paid and used Treasury rates as a proxy.

When yields on Treasury securities began to plummet in 2009, the FDIC redefined the "national rate. With the benefit of having data on offered rates available on a substantially real-time basis, the FDIC redefined the "national rate" as a simple average of rates paid by all IDIs and branches for various deposit products. These products include non-jumbo and jumbo CDs of various maturities, as well as savings, checking and money market deposit accounts. As part of the 2009 rulemaking, the FDIC also said that because deposit pricing had become increasingly national in scope, the agency would presume that the prevailing rate in an institution's market area would be the FDIC-defined national rate.

Currently, the FDIC uses an outside data aggregator to compute the simple averages for the various deposit products and determines the national rate cap by adding 75 basis points to each average rate. The FDIC then publishes on a weekly basis the national rate averages and corresponding national rate caps on its website.

The FDIC is now proposing a two-prong national rate cap. Instead of just 75 basis points over the national rate, the rate cap would be the higher of (1) the 95th percentile of rates paid by IDIs for that product weighted by each IDI's share of total domestic deposits, or (2) the proposed national rate for that product plus 75 basis points. Furthermore, instead of using a simple average rate paid by all IDI branches for a given deposit product, the national rate would be computed by using the weighted average of rates paid by all IDIs on a given deposit product, where the weights are each IDI's market share of domestic deposits.

ICBA's Position

National Rate Caps

ICBA commends the FDIC for proposing these changes and for recognizing that for the past four years, the 2009 national rate caps have not even been close to current Treasury yields nor to what the community banks must pay to obtain deposits through a listing service or third-party broker. Consequently, the current national rate caps have restricted less than well capitalized banks from competing for market rate funding creating an unintentional liquidity strain on those banks competing in the national markets. Furthermore, the caps have been so low as to be inconsistent with the Section 29 statutory requirement that a bank is prohibited from offering a rate that "significantly exceeds" or is "significantly higher" than the prevailing rate.

Because the current national rate caps are based on a survey of deposit products at all bank branches rather than on a per-charter basis, the mega-banks with their large branch networks are overrepresented. Since the large banks recently have been offering more deposit products with special features, such as rewards checking, higher rates on odd-term maturities, negotiated rates, and cash bonuses, this has furthered distorted the national rates since these features are not included in the calculation of the posted national rate. Meanwhile, branchless and rapidly growing web-based banks such as Ally and Goldman Sachs are underrepresented, contributing as much to the current calculation of national rates as the smallest community banks.

ICBA commends the FDIC for recognizing this problem and proposing that the national rate be based on a weighted average of rates paid by all IDIs for a given deposit product, where the weights are each IDI's market share of domestic deposits. **However, ICBA still urges the FDIC to base the national rate caps on the greater of (1) the original pre-2009 restrictions which was 120 percent of the current yield of similar maturity U.S. Treasury obligations (or, in the case of any deposit at least half of which is uninsured, 130 percent of such applicable yield), or (2) the post-2009 restrictions except that the rate cap should be 100 basis points higher than the national rate, not 75 basis points higher. This cap would ensure that less than well capitalized banks could compete for funds in the national market and yet would be consistent with the Section 29 prohibitions. We also strongly recommend that credit union rates be represented in the national rate cap. There is no legitimate reason for excluding credit unions from the national rate cap since they compete so vigorously with community banks for deposits.**

With regard to how the national rate is computed, the FDIC should use a per-IDI or per-charter approach so that community banks would be better represented. Even though weighting each IDI based on market share is much better than the present "per-branch" system, the proposed methodology for computing the national rate based on an IDI's market share of total domestic deposits would unfairly distort the results in favor of the larger institutions with the largest branch networks. In addition, basing the national rate on a per-IDI basis would be a lot simpler to compute particularly if credit unions are included in the calculation.

Our recommended national rate cap standard—an amalgam of both the pre-and post-2009 restrictions on brokered deposits (with certain modifications)—would work well in both a low interest rate environment as we had experienced for so many years after the economic downturn, as well as in a normal or high interest rate environment. Under any interest rate scenario, the national rate caps would never be lower than (1) 120 percent of the current yield on U.S. Treasury obligations or (2) 100 basis points over what banks and credit unions are currently paying on their deposits. This new standard would address the distortions created by branchless internet banks while offering a fairer assessment of the deposit rates that financial service competitors offer.

Furthermore, the first prong of the proposed national rate cap—the 95th percentile of rates paid by IDIs weighted by each institution's share of total domestic deposits—would be very difficult to compute on a national basis for each deposit product. The FDIC acknowledges this difficulty and says that this would require the agency to publish the rate caps on a monthly basis in lieu of a weekly basis as is the current process. Our proposal would not only be simpler to compute but would provide immediate and continuous relief to institutions subject to the interest rate restrictions.

Local Rate Caps

While the proposal continues to presume that the national rate cap applies to rates offered on all deposits by less than well capitalized institutions, it does continue to provide for a local rate cap alternative. ICBA commends the FDIC for proposing a substantially simplified local rate cap process.

Under the proposal, if a less than well capitalized bank can provide sufficient evidence that any bank and credit union was offering a rate on a particular deposit product in excess of the national rate, than the institution would be allowed to offer 90 percent of the competing institution's rate on the particular product. This would replace the current methodology that requires the local rate cap to be the average of the rates offered by all competing institutions for a particular product plus 75 basis points.

The proposal would also eliminate the current two-step process where less than well capitalized IDIs request a high rate determination from the FDIC and, if approved, calculate the prevailing rate within local markets. Instead, a less than well capitalized institution would need to notify its appropriate FDIC regional office that it intends to offer a rate that is above the national rate cap and provide evidence that it is competing against an institution or credit union that is offering a rate in its local market area in excess of the national rate cap. The institution would then be allowed to offer 90 percent of the rate offered by a competitor in the institution's local market area. The institution would be expected to calculate the local rate cap monthly, maintain records of the rate calculations for at least two exam cycles and, upon the FDIC's request, provide the documentation to the appropriate FDIC regional office and to examination staff during any subsequent exams.

While we commend the FDIC for substantially streamlining the local rate cap process, we recommend that a less than well capitalized institution be allowed to offer at least up to 95 percent of the competing institution's rate on a particular product in lieu of 90 percent. Using the higher percentage would provide additional flexibility for less than well capitalized institutions to compete with local competition offering rates in excess of the national rate cap.

However, we do support the provision of the proposal that a less than well capitalized institution seeking to offer a deposit product with an "off-tenor maturity" such as a 26-month CD would be able to do so provided that its local competitor was also using a 26-month product. This flexibility should address another problem with the current local rate cap—that it does not incorporate deposit products with off-tenor maturities.

National Rate Caps and Well-Capitalized Institutions

ICBA commends the FDIC for revising its Risk Management Supervision Manual of Examination Policies to clarify that national rate caps apply only to institutions that are less than well capitalized. Over the past three years, ICBA has consistently heard from members that regulators are bringing up the national rate caps during exams of well-capitalized banks, claiming that deposits paid in excess of the rate caps are "volatile funding" and insisting that the banks explain what will happen to their deposits if they are suddenly downgraded. We believe this is a misapplication of brokered deposit policy and inconsistent with the goals of Section 29 of the FDI Act which are to restrict brokered deposits at troubled institutions, not those that are well-capitalized. We certainly hope that by revising the FDIC Risk Management Supervision Manual of Examination Policies, FDIC examiners will no longer classify brokered deposits at well capitalized banks as "volatile funding" simply because their interest rates exceed the national rate caps.

Conclusion

In conclusion, ICBA commends the FDIC for proposing changes to the national rate and the national rate caps and recognizing that, at least for the past four years, the 2009 national rate caps have been too restrictive and have prevented less than well capitalized banks from competing for market rate funding. Although the FDIC's proposal is a significant improvement over the current way the national rate and the rate caps are determined, we urge that the national rate caps be based on the greater of (1) the original pre-2009 restrictions which was 120 percent of the current yield of similar maturity U.S. Treasury obligations or (2) the post-2009 restrictions, except that the rate cap should be 100 basis points higher than the national rate, not 75 basis points higher. We also strongly urge that credit union rates be represented in the national rate cap. Regarding how the national rate is computed, the FDIC should use a per-IDI or per-charter approach so that community banks would be better represented.

While we commend the FDIC for substantially streamlining the local rate cap process, a less than well capitalized institution should be allowed to offer at least up to 95 percent of the competing institution's rate on a particular product in lieu of 90 percent. In addition, we hope that a change to the FDIC's exam policies will mean that FDIC examiners will no longer classify brokered deposits at well capitalized banks as "volatile funding" simply because their interest rates exceed the national rate caps.

ICBA appreciates the opportunity to comment on this proposed rulemaking. If you have any questions or would like additional information, please do not hesitate to contact me at (202) 821-4431 or Chris.Cole@icba.org.

Sincerely,
/s/ Christopher Cole

Christopher Cole
Executive Vice President and Senior Regulatory Counsel