November 4, 2019

Via Electronic Mail

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

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

Dear Mr. Feldman:

Ally Bank, American Express National Bank, Barclays Bank Delaware, CIT Bank, N.A., and TIAA, FSB (collectively, the "Commenting Banks") submit this letter in response to the Federal Deposit Insurance Corporation's ("FDIC") notice of proposed rulemaking ("NPR") on revisions to its regulations relating to interest rate restrictions that apply to less than well capitalized insured depository institutions.[1] The Commenting Banks appreciate the opportunity to provide input to the FDIC and strongly support the FDIC's decision to consider alternative approaches to the proposed revised calculation of the national rate that may better reflect today's digital marketplace (e.g., internet website, mobile applications) for deposits.

The Commenting Banks represent many of the leading digitally-based direct banks in the United States. The business model of the digital banks generally focuses on utilizing advances in technology to establish direct relationships with our customers through digital channels, including online and through mobile applications. Digital banks, including the Commenting Banks, often operate with few or no physical branches, offering services to customers nationwide via the internet. Without the costs associated with maintaining brick and mortar branches, digital banks can typically offer higher interest rates to customers, a central feature in our business model embraced by a growing base of customers who are increasingly demanding digitally-based financial services.

The Commenting Banks agree with the FDIC that the methodology for calculating interest rate restrictions for less than well capitalized banks should be revisited. We support the FDIC's goal of ensuring that the rate cap is "reflective of the prevailing rates offered by *all institutions*." (emphasis added). The FDIC's current approach for setting rate caps has not evolved to reflect technological advancements, changes in business practices, and shifts in consumer behavior in banking.

Unfortunately, the FDIC's current rate cap methodology, adopted long before the emergence of internet-based consumer banking, disadvantages digital banks. We believe the national rate calculation does not

[1] 84 Fed. Reg. 46470 (Sept. 4, 2019).

reflect the true market rate for sourcing deposits in today's increasingly digital marketplace. The proposed revised methodology included in the NPR is a welcome effort to improve the calculation of the national rate. However, we believe that the proposed methodology still uniquely disadvantages digitally-based business models and, accordingly, would benefit from further refinement, as discussed in further detail below.

To ensure the rate cap is reflective of the digital marketplace for deposits and does not impede consumer choice, the Commenting Banks recommend that:

I. The FDIC revise the definition of "normal market area" to expressly permit consideration of a bank's business model and other non-geographic factors;

II. Digital banks should be eligible for a rate cap determination that is properly calibrated to digital banks' unique "normal market area," thereby giving digital banks the same flexibility afforded to more traditional branch banks; and

III. The FDIC amend its supervisory manuals and guidance to remove outdated references to "Internet deposits" as being categorically "Rate Sensitive" or "Wholesale" funding.

I. The FDIC Should Revise the Definition of "Normal Market Area" to Expressly Permit Consideration of a Bank's Business Model and Other Non-Geographic Factors.

Section 29 of the Federal Deposit Insurance Act limits an insured depository institution ("IDI") that is less than well capitalized from paying rates that are "significantly higher" than the rates offered in the IDI's "normal market area" or the national rate for deposits accepted outside its normal market rate. Section 29 does not define a number of terms important to interpreting the interest rate restriction, including "normal market area." Under the FDIC's regulations at 12 CFR 337.6(b), "normal market area" is defined solely in terms of geography.

While a geographic focus for "normal market area" may have made sense when the statute was written, this analysis is problematic today because it fails to incorporate the dynamics of a national marketplace for digital banks. A geographic-based construct that does not reflect business model considerations ignores the competitive market forces that impact a digital bank's pricing decisions. Under the proposed rule, the FDIC would retain the definition of an IDI's normal market area as any readily-defined geographic area in which the IDI solicits depositors by offering rates on a particular deposit service. This would inappropriately deprive digital banks from the normal market area option. To the detriment of consumer choice, this unfairly tilts the playing field and gives traditional brick and mortar branch banks greater rate cap latitude.

The FDIC should revise its definition of "normal market area" to allow consideration of a bank's business model and market segment to account for non-geographic factors. As the FDIC has acknowledged in its ANPR, "institutions also have created new products that do not fit into the posted national rates and rate cap."[2]

We defer to the FDIC and its supervisory discretion to determine which IDIs should be included in the calculation of the normal market rate for digital banks. We suggest that the FDIC could differentiate between the rate for non-digital banks and digital banks using a separate designation for the latter such as

[2] *Id.*

"digital normal market area," and applying a more appropriate rate cap calculation for such banks. To determine the universe of banks that can utilize the "digital normal market area," we believe there are a number of factors that the FDIC could consider, including whether: 1) the marketing channels used to source deposits are predominately digital; 2) new accounts are opened primarily via the bank's digital banking platform (e.g., internet website, mobile applications); and 3) the customer primarily accesses the account on a digital platform. This definition could include online-only accounts offered by banks with physical branches, provided the customer primarily accesses the account on a digital platform, and the bank offers the product nationwide. Additionally, the FDIC currently collects information about the service level of branch offices in Section 7 of the annual Summary of Deposits ("SOD") survey. The FDIC could use the SOD as one factor, among others, in determining the IDIs in the "digital normal market area."

II. Digital Banks Should Be Eligible for a Rate Cap Determination that Is Properly Calibrated to Digital Banks' Unique Normal Market Area, Thereby Giving Digital Banks the Same Flexibility Afforded to More Traditional Branch Banks

Pegging rate caps to either a single national rate or a geographic-based normal market rate uniquely disadvantages digitally-based bank business models. As the FDIC has acknowledged in its ANPR, "[B]ecause the national rate is an [simple] average for all banks and branches, the largest banks with large numbers of branches have had a disproportional effect on average interest rates. Even as other interest rates began to rise, the average stayed low as the largest banks have been slow to increase interest rates on deposits."[3] Digital banks are thus encumbered by a national rate average that is largely calculated using the lower rates associated with traditional brick and mortar branch banks. This one-size fits all approach could impede innovation in financial services and harm consumers without an identifiable and concomitant regulatory benefit.

Fundamentally, in order to achieve the purpose of the interest rate restrictions, it is critical that the FDIC calculate the proper "average" interest rate before it applies a cap. The rate cap's intent is to prevent less-than-well-capitalized banks from turning to high-risk, very high-cost sources of funding. At the same time, the rate cap conceptually acknowledges a bank's continued need to compete for funding, and allows a bank to do so as long as the rates the bank offers do not "significantly exceed" the average. That is, a bank that offers rates at or near the average when it becomes less than well capitalized may actually *increase* its interest rates in order to remain competitive, provided the increase is within the 75 basis point cap. The rate cap's intent is not to suddenly cram down otherwise market-average rates in a way that renders a bank non-competitive and creates a potential liquidity event. Unfortunately, both the current and proposed methodologies for calculating the national average interest could produce such a punitive result for digital banks today.

The FDIC's current methodology for calculating the rate cap does not accurately reflect the cost of deposits for banks without extensive physical branch networks. In today's rate environment, this causes the FDIC's market average rates to fall significantly below those of the digital deposit segment. Because of the digital nature of our business, our costs of providing deposit accounts to our customers are lower than traditional banks, and we pass those savings on to our customers in the form of higher deposit rates.

[3] 84 Fed. Reg. 2,375.

The proposed calculation of the national rate, like the current calculation, provides a mechanism to determine that a bank's market rate is higher than the national rate, but it is still based on limited geographic factors. The FDIC's current and proposed regulations provide that an IDI's market rate is presumed to be the national rate and that a market "is any readily defined geographic area in which the rates offered by any one insured depository institution soliciting deposits in that area may affect the rates offered by other insured depository institutions operating in the same area."[4] This formulation does not provide sufficient flexibility to reflect the business model of digital banks.

The FDIC should implement a "digital normal market area" rate cap pegged to the median rate offered by the ten largest digital banks as measured by total deposit amount. To determine the top ten digital banks, the FDIC could use data from Schedule RC-E, Item 1.f of the Call Report. This field is the "estimated amount of deposits obtained through the use of deposit listing services that are not brokered deposits." The FDIC could source the rate information directly from the ten largest digital banks' websites. This calculation would be straightforward for the FDIC to administer. Calculating the "digital normal market area" rate using the median, rather than a simple average, would guard against rate outliers skewing the cap through all stages of economic and interest cycles. Alternatively, the FDIC could outsource the gathering of this information to a third-party vendor – similar to how the FDIC currently gathers rate data today when calculating the national rate.

For the spread applied on top of the "digital normal market area" rate average, we suggest that the FDIC could amend the definition of "significantly higher" to 25 basis points. Twenty five basis points would be one-third of the current 75 basis points spread above the national rate that the FDIC uses today and proposes to use in the future. Permitting a bank that is not well capitalized to offer rates that are 25 basis points above the "digital normal market area" rate would provide the bank flexibility to account for introductory or promotional rates, while also preventing less than well-capitalized banks from abusing the "digital normal market area" rate to raise high-risk, volatile deposits.

The frequency of the publication of the "digital normal market area" rate calculation should be increased to better reflect prevailing market conditions. The FDIC proposes to update and publish the national rate cap information on a monthly basis, rather than the current weekly publication schedule. Monthly calculation may not be sufficiently reflective of current market rates. More frequent updating would draw a closer nexus between the prevailing rate environment in the market and the rate caps applied to less than well capitalized banks. As such, we recommend retaining the current weekly calculation and publication schedule for all rates.

Regarding the effective date of any changes, the FDIC proposes that any updated national rate cap that is lower than the previously published national rate would take effect three days after publication. In a competitive market, a change within three days after publication could put firms at a disadvantage to direct competitors. We recommend that the FDIC provide institutions seven days before a rate becomes effective.

[4] 12 CFR 337.6(f).

III. The FDIC Should Amend its Supervisory Manuals and Guidance to Remove Outdated References to "Internet Deposits" as Being Categorically "Rate Sensitive" or "Wholesale" Funding

Existing regulatory guidance unnecessarily stigmatizes banks that offer deposit accounts through digital channels. This guidance reflects an outdated view of the marketplace and does not account for very significant changes in technology, business practices, and consumer behaviors and preferences. For example, the federal banking agencies currently have joint guidance instructing their examiners that "[d]eposits attracted over the Internet…require special monitoring…[because] their inherent risk characteristics are similar to brokered deposits [and] are typically attractive to rate-sensitive customers who may not have significant loyalty to the bank."[5] The FDIC also has sections in its examination manual that reinforce these outdated notions. For instance, the "Liquidity and Funds Management" section of the FDIC's Risk Management Manual of Examination Policies (the "Manual") states that deposits acquired through the internet are examples of "wholesale funds" and that "core deposits" are typically raised through "convenient branch locations, superior customer service, extensive ATM networks, and low or no fee accounts."[6] The Manual instructs FDIC examiners that internet deposits generally "should not be considered stable sources of funds for liquidity purposes."[7]

The Commenting Banks respectfully submit that the above guidance reflects an outdated view of today's digital marketplace for deposits. The interagency guidance was issued in 2001 at a time well before smart-phones or mobile applications. Today's consumers increasingly look to digital channels first to obtain banking products and engage in financial activities. To meet this demand, banks today are able to offer compelling deposit products through the internet with rich feature sets, enhanced convenience, and customer service that rivals, if not exceeds, branch-based tellers. We believe that consumers today are attracted to digital banks for many reasons other than interest rates. As a result, we respectfully request that the FDIC review its existing guidance to remove outdated references and ensure that examiners do not inappropriately stigmatize deposits acquired through digital platforms.

[5] *Joint Agency Advisory on Brokered and Rate-Sensitive Deposits*, May 11, 2001.
[6] *See* FDIC Risk Management Manual of Examination Policies, Section 6.1-8 and 6.1-9.
[7] *Id*. at 6.1-8.

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We appreciate the opportunity to provide our comments and would welcome the opportunity to discuss them further with you during the rulemaking process.

If you have any questions or if we can provide any additional information, please contact Josh Wilsusen, Managing Director and Chief Counsel, Head of Public Policy and Government Relations, Ally Bank at josh.wilsusen@ally.com or 202.572.2158; Brett Loper, Executive Vice President, Global Government Affairs, American Express National Bank at brett.loper@aexp.com or 202.434.0160; Jeff Sowden, Head of Savings Products, Barclays Bank Delaware at jsowden@barclaycardus.com or 302.255.7122; James P. Shanahan, Senior Vice President & Chief Regulatory Counsel, CIT Bank, N.A. at james.shanahan@cit.com or 973.740.5371; and Mark Baum, EVP, General Counsel & Corporate Secretary, TIAA, FSB at mark.baum@tiaabank.com or 904.623.8191.

Sincerely,

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