May 27, 2020

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

Attention: Comments – FDIC 12 CFR Part 327 **- RIN 3064-AF53**, May 20, 2020 Notice of Proposed Rulemaking
Re: Assessments, Mitigating the Deposit Insurance Assessment Effect of Participation in the Paycheck Protection Program (PPP), the PPP Lending Facility, and the Money Market Mutual Fund Liquidity Facility,[i] [ii]

Mr. Feldman:

Valley National Bank (Valley) appreciates the opportunity to comment on the notice of proposed rulemaking (NPR) from the Federal Deposit Insurance Corporation (FDIC) to mitigate the deposit insurance assessment effects of participating in the Paycheck Protection Program (PPP) established by the Small Business Administration (SBA), and the Paycheck Protection Program Lending Facility (PPPLF) and Money Market Mutual Fund Liquidity Facility (MMLF) established by the Board of Governors of the Federal Reserve System.

The NPR's proposed changes would:

- remove the effect of participation in the PPP and PPPLF on various risk measures used to calculate an insured depository institution's assessment rate,
- remove the effect of participation in the PPPLF and MMLF programs on certain adjustments to an IDI's assessment rate,
- provide an offset to an insured depository institution's assessment for the increase to its assessment base attributable to participation in the MMLF and PPPLF, and
- remove the effect of participation in the PPPLF and MMLF programs when classifying insured depository institutions as small, large, or highly complex for assessment purposes.

The FDIC has requested comments on several areas:

Question 1: The FDIC invites comment on its proposal to apply a waterfall approach in excluding PPP loans, which include loans pledged to the PPPLF, from C&I Loans, All Other Loans, and Agricultural Loans in the calculation of an IDI's assessment rate. Is the assumption that all PPP loans are C&I Loans appropriate, or should these loans be distributed across loan categories in another manner? Should the FDIC collect additional data on how PPP loans are categorized in order to more accurately mitigate the deposit insurance assessment effects of these loans? Alternatively, should institutions report PPP loans as a separate loan category instead of including them in C&I Loans or other loan categories, thus providing data that would reduce the need for the FDIC to rely on certain assumptions, reduce the amount of necessary changes to specific risk measures and

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other factors, and potentially more accurately mitigate the deposit insurance assessment effects of an IDI's (Insured Depository Institution) participation in the program? Would this be overly burdensome for institutions?

Question 2: The FDIC invites comment on its proposal to exclude PPP loans from C&I Loans, All Other Loans, and Agricultural Loans in the calculation of an IDI's assessment rate. Is the assumption that all PPP loans are C&I loans appropriate, or should these loans be distributed across loan categories in another manner? If so, how and why? Should the FDIC collect additional data on how PPP loans are categorized?

Valley's comments on Questions 1 and 2:
We believe it is best if the PPP loans have its own separate category, instead of including them in C&I or other loan categories. This would reduce the need for the FDIC to rely on certain assumptions, potentially more accurately mitigate the deposit insurance assessment effects of a bank's participation in the program and would reduce the regulatory burden on banks. Also, according to the NPR, seven additions to the Call Report are being considered within the Federal Financial Institutions Examination Council to accommodate the proposed mitigations.[iii] Valley supports these changes. We recommend that the new reporting items be added to the memoranda items on Schedule RC-C—Loans and Lease Financing Receivables.

Question 3: The FDIC invites comment on advantages and disadvantages of mitigating the effects of participating in the PPP and PPPLF on deposit insurance assessments. How does the approach in the proposed rule support or not support the objectives of the Paycheck Protection Program and the associated liquidity facility?

The NPR includes the following with regard to question 3:
1. Established Small Institutions.
a. Exclusion of Loans Pledged to the PPPLF in Various Risk Measures
b. Exclusion of PPP Loans and Loans Pledged to the PPPLF in the LMI
(details contained within the NPR)

2. Large and Highly Complex Institutions. For IDIs defined as large or highly complex for deposit insurance assessment purposes, the FDIC is proposing to exclude the outstanding balance of loans pledged to the PPPLF and borrowings from the Federal Reserve Banks under the PPPLF from five risk measures used in the scorecard method: the core earnings ratio, the core deposit ratio, the balance sheet liquidity ratio, the average short-term funding ratio and the loss severity measure. For four risk measures—the growth-adjusted portfolio concentration measure, the balance sheet liquidity ratio, the trading asset ratio, and the loss severity measure—the FDIC is proposing to treat the outstanding balance of PPP loans, which includes loans pledged to the PPPLF, as riskless.

Valley's comment:
Valley, like many Banks, has made and continues to make PPP loans to support small businesses in our local communities due to the devastating effect COVID-19 has had and continues to have on small businesses, their employees, and the local communities. The margins on PPP loans are very thin and the resources

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needed to quickly stand up the capabilities to implement and operationalize the PPP program were significant. Valley therefore agrees that banks should not be penalized in the form of higher FDIC assessments for providing this much needed public service.

We appreciate that the FDIC has considered all the elements of the assessment rate formulas for "small," "large," and "highly complex" banks and that the FDIC has proposed modifications to a range of these elements. While Valley is a "large" bank under the FDIC's definitions for deposit insurance assessment purposes, we support the modifications proposed in the NPR for the:

- loan mix index in the formula for assessments for "small" banks;
- core deposits ratio, balance sheet liquidity ratio, loss severity measure, trading asset ratio, and growth-adjusted portfolio concentrations measure (in the concentrations measure) in the assessments formulas for "large" and "highly complex" banks; and
- unsecured debt, depository institution debt, and brokered deposit adjustments for all banks.

The modifications outlined in the NPR would not, however, completely offset the impact of PPP lending on banks' assessments. Rather, many banks would experience very little to no relief. We believe the following three recommendations would more effectively and appropriately limit the impact of PPP loans on bank assessments:

1) recognize the entire quarter-end outstanding balance of PPP loans, not only those pledged to the PPPLF;
2) factor the quarter-end outstanding balance of PPP loans into the leverage ratio used in the assessments formulas; and
3) exclude the PPP loans from the classification of "higher risk assets;"

1) Recognize the entire quarter-end outstanding balance of PPP loans, not only those pledged to the PPPLF.

The most significant issue is that the NPR would not provide relief for the total outstanding balance of PPP loans on a bank's balance sheet. As currently proposed, it generally recognizes only the quarterly average balance of PPP loans pledged against borrowings from the PPPLF.

Like many banks, Valley has not needed to borrow from the PPPLF, as we were proactive in building our liquidity position as the pandemic was in its early stages earlier this year (pre-PPP), and we also funded the PPP loans with deposits. At Valley, once the PPP loans are approved by the SBA, the borrowed funds are deposited in the small business owner's deposit account at Valley. As the borrower needs to cover payroll and other expenses, they draw down the funds.[iv] If banks need to replace this funding source as small businesses draw down their deposits, it can pledge PPP loans to borrow from the PPPLF (up through September 30, 2020). Such replacement funding builds gradually as the PPP-associated deposits are withdrawn, so a bank's average PPPLF borrowing over a quarter can be considerably less than its quarter-end PPP loan balance. However, several provisions in the NPR recognize the former (quarterly average PPPLF borrowing), but not the latter (quarter-end PPP loan balance), which would mitigate only a small portion of the effect of making PPP loans. In addition, it is quite possible that many banks, Valley included, may opt not to borrow through the PPPLF at all given their current funding positions and options. Yet, the banks that

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participated in making these much-needed PPP loans to small businesses experienced elevated balance sheets, impacting several ratios considered in the assessment formulas.

As of May 20, 2020 (latest data available), PPPLF borrowings totaled only $45.1 billion, or 8.8 percent of the current total balance of all PPP loans, which were $511.3 billion as of May 26, 2020.[v] It would seem, then, that the provisions in the NPR would provide relief of only 8.8 percent of the assessment penalty for banks with PPP loans on their books.

The approach outlined in the NPR, in effect, penalizes banks that do not borrow from the PPPLF. Many banks, including Valley, have indicated that they have not needed to participate in the PPPLF because they have sufficient deposits or other funding sources to finance their PPP loans. In addition to deposits from PPP borrowers, deposit inflows from the Economic Impact Payments, and the general "flight to quality" deposit inflows have helped fund PPP loans. Valley, and other Banks, should not be required to pay 35 basis points to borrow funds from the PPPLF in order to get credit in their FDIC assessments for making PPP loans.

The Federal Reserve is providing PPPLF borrowings with PPP loans pledged as collateral, without recourse. Our understanding is that the FDIC considers this feature as reasoning for mitigating the assessments formulas for PPP loans only when used as collateral for PPPLF borrowing. However, PPP loans are 100 percent guaranteed by the SBA, and the full principal amount of the loans and any accrued interest may qualify for loan forgiveness.[vi] We believe un-pledged PPP loans should be recognized with respect to assessments, and not require a second level of federal protection to enable this recognition.

For the reasons noted above, Valley recommends that the final rule be changed to provide full credit for the outstanding balance of PPP loans throughout the assessments calculations, including in the:

- offset to the assessment base for all banks;
- formulas for the base assessment rate for established "small" banks;
- formulas for the base assessment rate for "large" and "highly complex" banks; and
- classification of a bank as "small," "large," or "highly complex."

2) Factor the quarter-end outstanding balance of PPP loans into the leverage ratio used in the assessment rate formulas.

Valley recommends that the entire quarter-end outstanding balance of PPP loans should be utilized to adjust the leverage ratio used in the base assessment rate formulas for all banks. The federal banking regulators now permit adjustment of the leverage ratio for the sake of Prompt Corrective Action based on only the quarterly average of PPP loans pledged against PPPLF borrowing.[vii] However, FDIC assessments serve a different purpose, so a different treatment is appropriate and warranted. This point is important in that the leverage ratio is heavily weighted in the assessment rate formulas.

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3) Exclude the PPP loans from the classification of "higher risk assets"

PPP loans should not be classified as "higher risk assets" in the assessment rate formulas for "large" and "highly complex" banks. Under FDIC rules, a loan to a "high-risk C&I borrower" classifies as a "higher-risk loan," a component of "higher-risk assets."[viii] Therefore, a PPP loan to a "higher-risk C&I borrower" would raise the bank's "higher-risk assets / tier 1 capital and reserves" ratio, and thus potentially its assessment rate.[ix] Even if the PPP borrower is not a "higher-risk C&I borrower," a bank should be saved the steps required to evaluate whether an asset as secure as a PPP loan should classify as "higher-risk." Therefore, we believe the final rule should exclude PPP loans from "higher risk assets" in the assessment rate formulas for "large" and "highly complex" banks.

Question 4: The FDIC invites comment on the advantages and disadvantages of adjusting an IDI's assessment to offset the increase in its assessment base due to participation in the MMLF and PPPLF. How does the approach in the proposed rule support or not support the objectives of the Facilities?

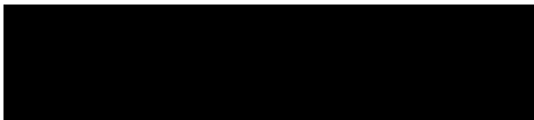
Valley's Comment:
This is addressed in our comments in response to Question 3 above.

Question 5: The FDIC invites comment on the reasonable and possible alternatives described in this proposed rule. Should the FDIC consider other reasonable and possible alternatives?

Valley's Comment:
This is addressed in our comments noted above. In addition, Valley, like other banks, relies on the assessments calculators for planning and budgeting, which is found on www.fdic.gov/deposit/insurance/calculator.html. Valley respectfully requests that revised versions be posted on its website as soon as a rule on mitigating the effects on assessments from participation in the PPP, PPPLF, and MMLF is finalized.

Valley appreciates the opportunity to comment on the NPR. Should you have any questions, please contact the undersigned.

Respectfully submitted,



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[i] Federal Deposit Insurance Corporation, "Assessments, Mitigating the Deposit Insurance Assessment Effect of Participation in the Paycheck Protection Program (PPP), the PPP Lending Facility, and the Money Market Mutual Fund Liquidity Facility: Voluntary Disclosure of Sovereign Exposures," 85 Federal Register 30649, May 20, 2020, www.govinfo.gov/content/pkg/FR-2020-05-20/pdf/2020-10454.pdf.

[ii] Information contained in this letter, in part, was sourced from the American Bankers Association and The Bank Policy Institute's draft Comment Letter addressing this NPR.

[iii] "[T]he agencies have submitted requests for seven additional items on the Call Report (FFIEC 031, FFIEC 041, and FFIEC 051): (1) The outstanding balance of PPP loans; (2) the outstanding balance of loans pledged to the PPPLF as of quarter-end; (3) the quarterly average amount of loans pledged to the PPPLF; (4) the outstanding balance of borrowings from the Federal Reserve Banks under the PPPLF with a remaining maturity of one year or less, as of quarter-end; (5) the outstanding balance of borrowings from the Federal Reserve Banks under the PPPLF with a remaining maturity of greater than one year, as of quarter-end; (6) the outstanding amount of assets purchased from MMFs under the MMLF as of quarter-end; and (7) the quarterly average amount of assets purchased under the MMLF." (NPR, footnote 19 on pages 30651-30652)

[iv] Funds loaned under the PPP are specifically authorized to cover only payroll, rent, mortgage interest, and utilities, at least 75 percent of which must have been used for payroll.

[v] The data on total PPP loans and PPPLF borrowing for banks and non-banks came from Federal Reserve Statistical Release H.4, www.federalreserve.gov/releases/h41/current/h41.htm, and the U.S. Small Business Administration, www.sba.gov/funding-programs/loans/coronavirus-relief-options/paycheck-protection-program.

[vi] U.S. Small Business Administration, "Business Loan Program Temporary Changes; Paycheck Protection Program—Requirements—Extension of Limited Safe Harbor With Respect to Certification Concerning Need for PPP Loan Request," 85 Federal Register 29845, May 19, 2020, page 29846, www.govinfo.gov/content/pkg/FR-2020-05-19/pdf/2020-10649.pdf

[vii] "Regulatory Capital Rule: Paycheck Protection Program Lending Facility and Paycheck Protection Program Loans," 85 *Federal Register* 20387, April 13, 2020.

[viii] 12 CFR 327 Appendix C to Subpart A.

[ix] Other factors could outweigh the effect on assessments of larger "higher-risk assets." For "large" banks, the "concentration measure" in the assessments formula equals the larger of the higher-risk assets ratio and the "growth-adjusted portfolio concentrations" measure. For "highly complex" banks, the assessments formula "concentration measure" factor depends on which is largest among the balances of higher-risk assets, top 20 counterparty exposure, and largest counterparty exposure.

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