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BANK POLICY INSTITUTE

May 27, 2020

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

Attention: Comments

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, RIN 3064-AF53, May 20, 2020[1]

Mr. Feldman:

The American Bankers Association[2] and the Bank Policy Institute[3] (together, "the Associations") appreciate the opportunity to comment on the notice of proposed rulemaking from the Federal Deposit Insurance Corporation ("FDIC") to mitigate the effects on assessments for banks that participate in the Paycheck Protection Program ("PPP") of the U.S. Small Business Administration, as well as in the Federal Reserve's PPP Liquidity Facility ("PPPLF") and Money Market Mutual Fund Liquidity Facility ("MMLF") ("the NPR"). To this end, the NPR would:

- provide an offset to a bank's assessment base for borrowing from the PPPLF and MMLF;

[1] 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," 85 *Federal Register* 30649 (May 20, 2020), www.govinfo.gov/content/pkg/FR-2020-05-20/pdf/2020-10454.pdf.

[2] The American Bankers Association is the voice of the nation's $18½ trillion banking industry, which is composed of small, regional, and large banks that together employ more than two million people, safeguard $14½ trillion in deposits, and extend $10½ trillion in loans.

[3] The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation's small business loans, and are an engine for financial innovation and economic growth.

- modify various elements of the formulas for the base assessment rate for "small," "large," and "highly complex" banks[4] to account for participation in the PPP and PPPLF;
- exclude loans pledged to the PPPLF and assets purchased under the MMLF from the unsecured debt, depository institution debt, and the brokered deposit adjustments; and
- exclude loans pledged to the PPPLF and assets purchased under the MMLF for purposes of classifying a bank as "small," "large," or "highly complex."

The Paycheck Protection Program is a Federal program, authorized under the CARES Act,[5] to address the devastating economic impacts of the COVID-19 pandemic by providing subsidies for small businesses to keep employees on their payrolls. This program is administered primarily through banks, which make forgivable loans to small businesses. Banks have made these loans to support their small business customers and their local communities. These loans do not boost a bank's earnings, as the margins are thin. The Associations therefore agree that banks should not be penalized in the form of higher FDIC assessments for providing this 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 proposed modifications to a range of these elements. In particular, 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 growth-adjusted portfolio concentrations measure) in the assessment formulas for "large" and "highly complex" banks; and
- unsecured debt, depository institution debt, and brokered deposit adjustments for all banks.

However, the proposed modifications would not completely offset the impact of PPP lending on assessments for any bank; in fact, they would provide minimal-to-no relief for most banks. As detailed below, to more effectively limit the impact of PPP loans on assessments, we recommend that the final rule should:

- adjust throughout for the total quarter-end outstanding balance of all PPP loans, not only those pledged to the PPPLF;
- factor the quarter-end outstanding balance of all PPP loans, not just those pledged to the PPPLF, into the leverage ratio used in the assessments formulas;
- allow that PPP loans not be considered as potential "higher risk assets;"
- post revised assessments calculators as soon as possible; and
- include the new Call Report items under "Memoranda" on Schedule RC-C.

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[4] For purposes of FDIC assessments, a "small" bank is generally defined as one with less than $10 billion in total assets; a "highly complex" bank as one with $50 billion or more in total assets and controlled by a parent holding company with $500 billion or more in total assets or is a processing bank or trust company; all others are "large" banks. (12 CFR §327.8(e,f,g))

[5] Coronavirus Aid, Relief, and Economic Security Act, P.L. 116-136, Division A—Small Business Interruption Loans.

The final rule should recognize the entire quarter-end balance of all PPP loans, not just those pledged to the PPPLF.

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

Many banks funded PPP loan operations with deposits. In making a PPP loan, a bank usually deposits the borrowed funds in a deposit account of the small business borrower. The borrower draws down these deposits over time to cover payroll and other expenses.[6] If the bank needs to replace this financing, it can pledge PPP loans against borrowing from the PPPLF. Such replacement funding builds gradually as the PPP-associated deposits are withdrawn, so the 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 impact on assessments from PPP lending.

In demonstration, total borrowing from the PPPLF averaged $17.8 billion for second quarter 2020 through May 20, which was 3.5 percent of the $512.2 billion balance of PPP loans outstanding on that date.[7,8] This suggests that the NPR provisions would relieve no more than 3.5 percent of the assessment penalty for banks with PPP loans on their books.

Moreover, many banks indicate that they have not needed to participate in the PPPLF because they have sufficient deposits to finance their PPP loans. In addition to deposits from PPP borrowers, deposit inflows from the Economic Impact Payments have helped fund the loans. These banks should not be required to pay 35 basis points to borrow nonessential funds from the PPPLF in order to get credit in their FDIC assessments for making PPP loans.

PPPLF borrowing against PPP loan collateral is provided without recourse. We understand that the FDIC views this feature as justification for mitigating the assessments formulas for PPP loans only when used as collateral for PPPLF borrowing. However, "[l]oans under the PPP are 100 percent guaranteed by [the U.S. Small Business Administration], and the full principal amount of

[6] 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.

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

[8] Preliminary results from a survey of banks of all sizes indicates that PPP loans expanded the balance sheets of bank that participated in the program by up to 20 percent, with a mean of 8 percent. Moreover, on average over 83 percent of PPP loans were funded from sources other than borrowing from the PPPLF (71 percent from deposits and securities sales).

the loans and any accrued interest may qualify for loan forgiveness."[9] As a general matter, guarantees by the U.S. Small Business Administration are backed by the full faith and credit of the United States Government. Surely multiple levels of federal protection should not be needed for the FDIC to achieve its stated goal of mitigating assessments for PPP loans, including (not exclusively) those pledged to the PPPLF.

Accordingly, the Associations recommend that the final rule provide full credit for the outstanding balance of all PPP loans throughout assessments calculations, including in the:

- offset to the assessment base for all banks;
- formula for the base assessment rate for established "small" banks for the following:
  - net income before taxes / total assets ratio,
  - nonperforming loans and leases / gross assets ratio,
  - other real estate owned / gross assets ratio,
  - brokered deposits ratio, and
  - one-year asset growth;
- formulas for the base assessment rate for "large" and "highly complex" banks for the core earnings ratio and average short-term funding measure; and
- classification of a bank as "small," "large," or "highly complex."

The entire quarter-end outstanding balance of all PPP loans should factor into the leverage ratio used in the assessment rate formulas.

For the reasons set forth above, as well as for consistent and effective application of approach in the final rule, the Associations recommend that the entire quarter-end outstanding balance of all PPP loans should be taken into account 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 Prompt Corrective Action purposes based on only the quarterly average of PPP loans pledged against PPPLF borrowing.[10] However, FDIC assessments serve a different purpose, so a different treatment is warranted. This point is significant in that the leverage ratio is heavily weighted in the assessment rate formulas.

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[9] 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, 29846 (May 19, 2020), www.govinfo.gov/content/pkg/FR-2020-05-19/pdf/2020-10649.pdf.

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

PPP loans should not classify 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" is classified as a "higher-risk loan," a component of "higher-risk assets."[11] 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.[12] Even if the 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." Accordingly, the final rule should exclude PPP loans from "higher risk assets" in the assessment rate formulas for "large" and "highly complex" banks.

Amended assessments calculators for "small," "large," and "highly complex" banks should be posted at FDIC's soonest convenience.

Banks rely on the assessments calculators on www.fdic.gov/deposit/insurance/calculator.html for planning and budgeting. The Associations respectfully request that revised versions be reposted as soon as a rule on mitigating the effects on assessments from participation in the PPP, PPPLF, and MMLF is finalized.

The new Call Report items should be included under "Memoranda" on Schedule RC-C.

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.[13] The Associations support these changes. We recommend that the new reporting items be added to the memoranda items on Schedule RC-C—Loans and Lease Financing Receivables.

[11] 12 CFR §327 Appendix C to Subpart A.

[12] 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.

[13] "[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." (85 *Federal Register* 30649 (May 20, 2020), 30651-30652, footnote 19)

The NPR contained a few questions regarding the option of reporting PPP loans as their own category on Schedule RC-C, Part I in the Call Report. The Associations do not support this alternative, as many institutions have already established processes to report these loans in existing categories on schedule RC-C. Therefore, reporting PPP loans as a separate loan category on Schedule RC-C would create a significant operational burden for these institution.

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The Associations appreciate the opportunity to comment on the NPR. Please contact the undersigned if there are any questions.

Respectfully submitted,

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