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FINANCIAL SERVICES ROUNDTABLE

January 5, 2016

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

RE: Notice of Proposed Rulemaking on Assessments (12 CFR §327), RIN 3064–AE40[1]

Dear Mr. Feldman:

The American Bankers Association,[2] The Clearing House Association,[3] and the Financial Services Roundtable[4] (the Associations) appreciate the opportunity to respond to the notice of proposed rulemaking from the Federal Deposit Insurance Corporation (FDIC) on a means to implement section 334 of the Dodd-Frank Act (§334).[5] This provision requires the FDIC to (1) raise the minimum reserve ratio for its insurance fund to 1.35 percent of estimated insured deposits (instead of 1.15 percent, as before), (2) assess premiums on banks to reach the 1.35 percent goal by September 30, 2020, and (3) "offset the effect of [the increase in the minimum reserve ratio] on insured depository institutions with total consolidated assets of less than $10,000,000,000."

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1 80 *Federal Register* (215) 68,780, November 6, 2015, posted to www.gpo.gov/fdsys/pkg/FR-2015-11-06/pdf/2015-27287.pdf (proposal).

2 The American Bankers Association is the voice of the nation's $16 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $12 trillion in deposits and extend more than $8½ trillion in loans.

3 Established in 1853, The Clearing House is the oldest banking association and payments company in the United States, and is owned by the world's largest commercial banks. The Clearing House Association L.L.C. is a nonpartisan organization that engages in research, analysis, advocacy and litigation on behalf of its owner banks, focused on financial regulation. Its affiliate, The Clearing House Payments Company L.L.C., owns and operates payments systems that clear almost $2 trillion each day, representing nearly half of all automated clearing house, funds transfer and check-image payments made in the United States.

4 As advocates for a strong financial future, the Financial Services Roundtable represents the largest integrated financial companies providing banking, insurance, payment, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the CEO. FSR member companies provide fuel for America's economic engine, accounting directly for $92.7 trillion in managed assets, $1.2 trillion in revenue, and 2.3 million jobs.

5 The Dodd-Frank Wall Street Reform and Consumer Protection Act, P.L. 111-203, July 21, 2010.

The Associations believe that the proposed mechanism of credits for banks under $10 billion in assets (*small banks*) would be a reasonable means to satisfy the §334 requirement, with some modifications. As to the proposed surcharge assessment scheme for banks over $10 billion (*large banks*), we propose an alternate plan from those offered in the proposal. In brief, we recommend that:

- Surcharge assessments on *large banks* should be set on a fixed schedule to raise the FDIC insurance fund to 1.35 percent of insured deposits by the end of 2019, with a potential shortfall assessment in first quarter 2020 if needed, as provided by Congress.
- A *large bank*'s assessment base for surcharge assessments should not be augmented by adding the assessment base of an affiliated *small bank*.
- In calculating surcharge assessments, the $10 billion assessment base deduction should apply for ***each*** *large bank*, whether or not there is an affiliated *large bank*.
- *Small banks* should be permitted to transfer or use without limit the assessment credits they are allocated for raising the FDIC insurance fund's reserve ratio above 1.15 percent as soon as the fund reaches 1.35 percent, and should not pay assessments on these credits.

Discussion of these recommendations follows.

<u>Surcharge assessments should be established on a fixed schedule to recapitalize the FDIC insurance fund using the full period specified in statute.</u>

Per §334, the FDIC is to assess banks to bring its insurance fund to a 1.35 percent reserve ratio by September 2020. ***The Associations recommend that surcharge assessments be set so as to take full advantage of this time period.*** We note that Congress twice extended the timespan over which the fund is to be recapitalized to the minimum target reserve ratio. After the fund fell dramatically in the last recession, in October 2008 the FDIC established a recapitalization deadline of December 2014. In May 2009, the Helping Families Save Their Homes Act (PL 111–22) §204(b) extended the deadline to December 2016. Then, in July 2010, Dodd-Frank Act §334(d) specified September 30, 2020, as the date when the fund is to be recapitalized to a 1.35 percent reserve ratio. The clear intent of reiterated extension of the deadline was to allow time for banks to recover from the deep recession and build capital to support their soundness and ability to lend. Taking advantage of the full period for surcharge assessments would be consistent with this intent.

The *large banks* have, in fact, retained earnings and built capital; the aggregate tier 1 capital of banks currently over $10 billion in assets is up 77.1 percent from the end of the last recession, bringing their aggregate tier 1 capital-to-assets ratio from 7.9 percent to 9.1 percent. The impact on the availability of credit has not been negligible. At the same time, total bank credit grew only 13.3 percent in the 6¼ years since the last recession, compared to 23.7 percent in the same period following the prior recession and 67.3 percent following the recession before that.[6]

[6] Banks over $10 billion in assets currently hold 76.9 percent of total bank credit. These figures were calculated over second quarter 2009 to third quarter 2015, fourth quarter 2001 to first quarter 2009, and first quarter 1991 to second quarter 1997 from data available on www.fdic.gov.

For this reason, the Associations strongly disagree with the contention in the proposal that surcharge assessments will not significantly impact *large banks*' capital or earnings. *Large banks* have been working hard to bring expenses under control so the higher expenses and deterioration of performance measures will mean less new capital to support credit growth. We therefore urge the FDIC to minimize the annual assessment expense by using the full surcharge period that was reiterated in statute by Congress.[7]

The FDIC projects in the proposal that 4½ basis points (b.p.) annually of surcharge assessments would likely raise the insurance fund's reserve ratio to 1.35 percent in 8 quarters.[8] It therefore seems reasonable that 14 quarters (from third quarter 2016 to fourth quarter 2019) at no more than 2¼ b.p. annually would similarly suffice.

A 2¼ b.p. surcharge would, after the scheduled reduction in the assessment schedule for all banks after the insurance fund reaches 1.15 percent, be roughly equivalent to the current assessment schedule for *large banks*. Therefore, several *large banks* suggest that the current risk-based assessment pricing methodology could be applied to implement surcharge assessments.[9] The impact on expenses would be limited, which in turn would reduce the impact on the banks in terms of services provided. Additionally, maintaining the prevailing assessments structure for *large banks* would provide consistency and predictability for FDIC assessments for *large banks* and continue the benefit to those with lower risk-based assessments.

In particular, ***the Associations recommend that surcharge assessments be integrated into risk-based assessments pricing in a way that maintains the current offset for long-term, unsecured debt***. When the Initial Base Assessment Rate (IBAR) schedule is lowered after the insurance fund reaches 1.15 percent, the benefit of the Unsecured Debt Adjustment will also be reduced.[10] Integrating surcharge assessments into the IBAR schedule can maintain this incentive. Many *large banks* have issued long-term, unsecured debt to take full advantage under the prevailing IBAR schedule, behavior the FDIC has recently encouraged.[11] Implementation of surcharge assessments as recommended here would avoid penalizing them for doing so.

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[7] A survey of *large banks* indicated that a strong majority would prefer the plan outlined above, *i.e.*, surcharge assessments targeting recapitalization of the FDIC insurance fund to a 1.35 percent reserve ratio by September 2020. However, a few would prefer a one-time surcharge to bring the fund to 1.35 percent in the first quarter that surcharge assessments are assessed and a few would prefer the proposed scheme of surcharge assessments at a 4½ b.p. annual rate until the fund reaches 1.35 percent.

[8] Proposal, page 68,781.

[9] The survey of *large banks* indicated that about half would prefer that surcharge assessments be integrated into risk-based assessments pricing.

[10] Since the "unsecured debt adjustment" is limited to half of the Initial Base Assessment Rate, and the range for this rate will be scaled down from 5-35 b.p. at present to 3-30 b.p. after the insurance fund reaches 1.15 percent, some of the potential benefit from outstanding long-term unsecured debt will be lost.

[11] In its Final Rule on Large Bank Pricing, the FDIC stated: "All other things equal, greater amounts of long-term unsecured debt can reduce the FDIC's loss in the event of a failure, thus reducing the risk to the [insurance fund]." (76 *Federal Register* (38) 10,672, February 25, 2011, at page 10,680).

A *large bank*'s assessment base for surcharge assessments should not be augmented with the assessment base of an affiliated *small bank.*

As proposed, the assessment base for surcharge assessments for a *large bank* would be augmented by the assessment base(s) of any affiliated *small bank*(s). ***The Associations believe that this adjustment would abrogate the intent of §334 by imposing de facto assessment surcharges on small banks affiliated with large banks, albeit indirectly by assessing through the larger affiliates.*** In effect, these *small banks* would ***not*** receive ***full*** offsets for their contributions to growth of the insurance fund above 1.15 percent in that they would be forced to contribute to a growing fund reserve ratio through indirect assessment surcharges.

The Associations note that, while §334(d) authorizes the FDIC to "***take such steps as may be necessary***" to bring the bring the insurance fund's reserve ratio to 1.35 percent by September 2020 and §334(e) specifies a treatment for *small banks*, there is no mention in §334 of *large banks* and no authorization for alteration of the FDIC assessment base specified in 12 C.F.R. §327.5. ***We do not see augmentation of large banks' assessment bases with those of smaller affiliates as a "necessary" step that is consistent with statue***.

We further disagree with the premise of this proposed adjustment, that it "would prevent *large banks* from reducing their surcharges (and shifting costs to other *large banks*) either by transferring assets and liabilities to existing or new affiliated *small banks* or by growing the businesses of affiliated *small banks* instead of the *large bank*."[12] Bank affiliates are structured to enhance the business of the banking organization and not to manipulate deposit insurance assessments. In many cases, a *large bank*'s smaller affiliate is dedicated to a single business line or is a "limited purpose bank." Temporary surcharge assessments would not induce bank management to change priorities in this respect – to move assets from the *large bank* into the smaller one or grow assets in the smaller bank instead of the larger one – particularly given the short time frame for such surcharges.

If, despite these arguments, there is to be an adjustment over questionable concern for incremental shifts to smaller affiliates, then any augmentation of a large bank's surcharge assessment base should be limited to no more than the change in the assessment base of any small bank affiliates starting in the quarter when surcharges are first applied.[13] Nonetheless, even these adjustments would penalize some *small banks* and make assessment base adjustments that we believe are not supported in statute.

Each *large bank* should receive the full $10 billion deduction from its surcharge assessment base.

The Associations appreciate the proposal's sensitivity to the impact on *large banks* that are just above $10 billion; ***we agree that a $10 billion deduction from the surcharge assessment base is a reasonable approach.*** However, we do not support apportionment of this deduction among

[12] Proposal, page 68,783.

[13] In measuring the change in an affiliated *small bank*'s assessment base, allowance should be made for normal growth.

affiliated *large banks*, as proposed. As FDIC assessments are computed at the bank entity level, why now should the legal entity structure be ignored for purposes of applying the $10 billion deduction when calculating the assessment base? ***We feel that a full $10 billion deduction should apply for every bank larger than $10 billion.***

As noted above, §334 requires "***such steps as may be necessary***" to bring the insurance fund to 1.35 percent by September 2020. ***The Associations do not see that applying deductions in a way that discriminates against banking organizations with multiple affiliated large banks as "necessary."***

Moreover, this aspect of the proposed surcharge assessment base would increase select *large banks*' liability for conduct long before §334 went into effect. The youngest *large bank* currently affiliated with another *large bank* was chartered more than five years before the Dodd-Frank Act was enacted in July 2010. It is inherently unfair to impose punitive surcharges on affiliated *large banks* by applying the proposed rulemaking authority retroactively.

<u>*Small banks*' assessment credits should not be limited in use or assessed.</u>

Limits on the Use of Credits

As proposed, a *small bank* would not be able to use its assessment credits until the insurance fund's reserve ratio reaches 1.40 percent, and thereafter would be allowed to offset no more than 2 b.p. of assessments annually (while its credits last).[14] ***The Associations see no reason for these limits.***

The proposal argues that these limits would "provide a cushion for the [insurance fund] to remain above 1.35 percent in the event of rapid growth in insured deposits or an unanticipated spike in bank failures, and therefore would reduce the likelihood of triggering the need for a restoration plan."[15] However, the Associations project that the fund will be near $100 billion with near $6.5 billion a year in assessment income by the time it reaches 1.35 percent (more under our proposed surcharge assessment scheme). In comparison, the FDIC projects that the assessment credit pool will be only about $900 million.[16] This amount would make a minimal difference in the fund as it grows above 1.35 percent, especially in that *small banks* represent only 19 percent of the FDIC current assessment base.

More fundamentally, delaying use of credits seems to contradict the intent of §334. The forgone interest the *small banks* could earn if they use their credits immediately after the insurance fund reaches 1.35 percent, instead of getting them back in small increments over three or four years (as per the proposal), would be equivalent to paying interest on these funds. Thus, in effect, the *small banks* would net an incomplete offset for their contributions to the growth of the fund above 1.15 percent.

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[14] Proposal, page 68,785.
[15] *Ibid.*
[16] *Ibid.*

Sales and Transfers of Assessment Credits

As proposed, a *small bank* would be barred from selling or otherwise transferring any part of its assessment credits (except in an acquisition or merger).[17] ***The Associations believe that if a small bank wants to sell or transfer all or part of its balance of assessment credits, perhaps because it could put those funds to use in making loans or providing services, then it should be permitted to do so without limit.*** A few years ago, the FDIC's experience with the transferability of credits in the form of prepaid assessments did not reveal any noteworthy problems with transferability. Moreover, it seems inconsistent that the proposal would look through the organization structure of banking firms with *large bank* subsidiaries but would not permit a *small bank* to transfer assessment credits to an affiliated *small bank*.

Assessments on Assessment Credits

Once credits are parceled out to *small banks*, they could be viewed as assets on the banks' books, and thus by statute part of the FDIC assessment base. It seems incongruous that any bank should pay assessments on perfectly risk-free assets that are, in fact, assessments-to-be-forgone. ***The Associations therefore recommend that the assessments pricing formula for small banks be adjusted such that there is no assessment on assessment credits.***

Conclusion

The Associations appreciate that the FDIC has provided instructions and assessments calculators to allow banks to project their assessments going forward, including with the proposed surcharge assessments. As to surcharge assessments for *large banks*, we recommend that the FDIC allow the full time period specified repeatedly by Congress to bring its insurance fund to a 1.35 percent reserve ratio, that risk-based pricing for surcharge assessments maintains the Unsecured Debt Adjustment incentive at current levels, and that there are no adjustments to surcharge assessment bases for *small* or *large bank* affiliates. For *small banks*, we recommend transfer and use without limit, as well as exclusion from assessments, for the assessment credits to be allocated for raising the fund's reserve ratio above 1.15 percent. We look forward to working with FDIC staff as it finalizes a rule to implement Dodd-Frank Act §334. Please contact the undersigned if you have any questions regarding the Associations' response to the proposal.

Sincerely,

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[17] Proposal, page 68,785.