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The Clearing House®

Monday, May 16, 2011

By electronic delivery to:

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

Dear Mr. Feldman;

The American Bankers Association (ABA)[1] and The Clearing House (TCH)[2] appreciate the opportunity to comment on the issues raised by the Federal Deposit Insurance Corporation's (FDIC) Notice of Proposed Rulemaking (NPR)[3] regarding interest on deposits and deposit insurance coverage (Regulation Q) as mandated under §627 of Title VI[4] of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act).[5]

Specifically, the Dodd-Frank Act repeals §19(i) of the Federal Reserve Act,[6] §18(g) of the Federal Deposit Insurance Act,[7] and part of §5(b)(1)(B) of the Home Owners' Loan Act.[8] The FDIC NPR rescinds Regulation Q implementing regulations applicable to state non-member banks. The FDIC proposes to retain and move the definition of "interest" from 12 C.F.R. 329.1(c) *Interest on Deposits*, to 12 C.F.R. 330.1 *Deposit Insurance Coverage* in order to

[1] The American Bankers Association represents banks of all sizes and charters and is the voice for the nation's $13 trillion banking industry and its two million employees. ABA's extensive resources enhance the success of the nation's banks and strengthen America's economy and communities.
[2] Established in 1853, The Clearing House is the nation's oldest banking association and payments company. It is owned by the world's largest commercial banks, which employ 1.4 million people in the U.S. and hold more than half of all U.S. deposits. The Clearing House is a nonpartisan advocacy organization representing through regulatory comment letters, amicus briefs and white papers the interests of its owner banks on a variety of systemically important banking issues. The Clearing House Payments Company provides payment, clearing, and settlement services to its member banks and other financial institutions, clearing almost $2 trillion daily and representing nearly half of the automated clearinghouse, funds-transfer, and check-image payments made in the U.S. See The Clearing House's web page at www.theclearinghouse.org.
[3] 76 Fed. Reg. 21265 (April 15, 2011).
[4] Public Law 111-203, §627 *noted at* 12 USC 371(a), *Interest-Bearing Transaction Accounts Authorized.*
[5] Public Law 111-203. Codified at 12 U.S.C. 5301.,.
[6] 12 U.S.C. 371a
[7] 12 U.S.C. 1828(g).
[8] 12 U.S.C. 1464(b)(1)(B).

facilitate the implementation of the new assessment rules, and extension of temporary, unlimited deposit insurance coverage for noninterest-bearing transaction accounts. The FDIC also requests comment on whether there are additional definitions that should be retained and moved, such as the exception for premiums from the definition of interest.

Although Regulation Q prohibits the payment of interest on all demand deposits, in practice, the prohibition was limited to forbidding the payment of interest on business checking accounts. In response to Regulation Q's limitations, Negotiable Order of Withdrawal (NOW) and sweep accounts were created to extend interest to individuals and some businesses.[9] Upon the repeal of Regulation Q, banks *may* offer interest-bearing demand deposits, including checking accounts, to businesses and individuals.

By statute, the repeal of Regulation Q is effective automatically July 21, 2011.[10] Due to the operation of a statutory termination, the FDIC does not have the authority to delay or to implement a transitional phase-out of Regulation Q.

Part I: Issues and Recommendations

This comment letter consists of two-parts. Part I responds to the proposal generally and discusses outstanding issues and recommended solutions; Part II responds to the specific questions posed in the NPR.

Call Reports and TFRs Need to be Modified

Before the September 2011 reporting deadline, Call Reports and Thrift Financial Reports (TFR) should be modified for the interest-bearing demand deposit account (DDA) products that will be developed following the repeal of Regulation Q. If Call Reports cannot be updated by the end of 3Q 2011, the Federal Financial Institutions Examination Council should release detailed guidance explaining how to report interest-bearing demand deposits until Call Reports and TFRs can be modified formally. Call Report and TFR instructions need to explain clearly how to report (1) accounts bearing paid interest, and (2) accounts bearing hybrid interest.

Clarity Needed for New Hybrid Products

The term "hybrid product" describes post-Regulation Q demand deposit accounts offering a combination of earnings credits and interest payments. Many institutions are interested in offering these products, but more regulatory clarity is needed. Specifically, banks need to know if hybrid accounts will be considered interest bearing, and how unused earnings credits may be used, particularly if credits may be rolled over monthly or reserved indefinitely for future use.

[9] NOW accounts are available to individuals, sole proprietorships, governmental units, and non-profit organizations. 12 U.S.C. 1832(a). Sweep accounts move funds overnight from non-interest bearing into interest bearing accounts, such as a money market or mutual fund.

[10] 12 U.S.C. 371(b). The statutory repeal of Regulation Q is mandated by the Dodd-Frank Act to occur "1 year after the date of enactment of this Act." The enactment date of the Dodd-Frank Act was July 21, 2010.

FDIC and Federal Reserve Should Host Industry Roundtables Before July 21, 2011
As this comment letter will demonstrate, the immediate need of the banking industry is for post-Regulation Q regulatory clarity. A series of joint FDIC and Federal Reserve roundtables to discuss the Regulation Q repeal might be the most efficient forum to address the need for immediate communication and regulatory certainty. In order to reach a larger banking audience, the roundtables could be accompanied by a Frequently Asked Questions (FAQ) document downloadable from the agency websites offering further clarity. The majority of the roundtable discussions should occur prior to the July 21, 2011, repeal date to provide a timely response to industry comments, questions, and concerns.

Joint Cooperation Among the Regulators Needed
Due to the pending effective date, time is of the essence in gaining clarity and certainty on the issues addressed in this comment letter. To ease the post-Regulation Q transition, it would be helpful if the FDIC and Federal Reserve would work jointly to clarify issues generally, prior to the July 21, 2011, effective date, and modify reporting forms prior to the September 2011 Call Report and TFR deadline.

Banks Need Adequate Time to Prepare for Regulatory Changes
ABA and TCH appreciate the implementation burden placed on the FDIC by the prescribed Dodd-Frank deadlines. The implementation schedule is strict, and will continue to strain the resources of banking agencies and financial institutions. Although the one-year repeal of Regulation Q was well known, the implementing FDIC NPR was released only 96 days before the Dodd-Frank Act mandated transfer date. Looking forward to the next set of statutory deadlines, ABA and TCH respectfully request that the FDIC consider providing financial institutions more time to prepare for new operational and compliance demands.

Due to the repeal of Regulation Q, banks choosing to offer interest bearing demand deposits will have an operational burden to develop new deposit products, update contracts and disclosures, educate customers, and, depending on the applicable FDIC insurance levels, move a substantial volume of customer funds into new deposit products. From a compliance perspective, banks need an improved understanding of the impact of the repeal on demand deposit products, and, very importantly, instructions on how to record interest-bearing demand deposits on quarterly bank reports.

Part II: Responses to Proposed Questions

Preserve the Definition of Interest and Exceptions to the Definition of Interest

ABA and TCH support the proposal to retain and move the definition of "interest," and the exception from the definition of interest for premiums on demand deposits. If these definitions are not retained, their automatic repeal could convert heretofore noninterest-bearing demand deposits into interest-bearing demand deposits, reducing the account's FDIC insurance coverage from unlimited to the $250,000 cap. To avoid this outcome, the preferred solution is to preserve the definition of "interest" and the exception for premiums by migrating these sections from 12 CFR 329.1(c) *Interest on Deposits*, to 12 CFR 330.1 *Deposit Insurance Coverage*.

As noninterest-bearing accounts, business checking accounts under Regulation Q have unlimited FDIC insurance as extended under §343 of the Dodd-Frank Act.[11] If the definitions and exceptions are not retained, as proposed, noninterest-bearing commercial demand deposit accounts offering earnings credits could lose their unlimited FDIC insurance coverage and convert to interest bearing accounts capped at $250,000 in FDIC insurance.[12] If the definitions are retained and moved, as proposed, business customers would have the opportunity to select either an interest bearing account with capped FDIC insurance, or unlimited FDIC protection on a non-interest bearing account. Concurrent with the development of new account options, banks will be obligated to educate customers and to offer disclosures as the new interest-bearing products become available.

Earnings Credits Are Essential

Implementing the repeal of Regulation Q without retaining the definitions as proposed could void the exception for earnings credits, which is rooted in the definition of "interest." Earnings credits are essential because they offer substantial benefits to customers and financial institutions. Without earnings credits, banks would have fewer options for pricing accounts and consumers would have limited deposit options. Customers may elect to receive earnings credits, premiums, or bonuses, in lieu of paid interest depending on their needs and preferences. Anecdotally, business customers are expressing a strong preference for earnings credits and likely will continue to request earnings credits after the Regulation Q repeal.

For banks, earnings credits and hybrid accounts may soften the impact of the increased cost of funds and mitigate the upward spiral effect of "rate chasing." If the industry experiences a high demand for interest-bearing demand deposits in a high interest rate environment, an increased variety of interest options and earning credits would moderate the influence of "rate chasers" and give the bank more pricing tools, which would lessen the bank's reliance on interest rate increases to capture deposits.

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[11]Public Law 111-203, §343 *noted at* 12 U.S.C. 1821(a)(1), *Insurance of Transaction Accounts.*

[12] Unlike consumer accounts that may be eligible for extended FDIC insurance by opening multiple accounts under differing legal titles, commercial customers are limited to $250,000 in FDIC coverage per tax identification number.

Retain the Federal Reserve Library of Regulation Q Interpretive Letters and Staff Opinions

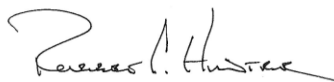
In order to provide greater regulatory certainty, the Federal Reserve's collection of legal opinions under Regulation Q, which have provided valuable guidance to the industry for a number of years, must survive the repeal of Regulation Q. All legal interpretive letters, staff opinions, published rulings, and other Federal Reserve documentation should be preserved to support the proposed FDIC transfer of regulatory language. Additionally, the industry needs the guidance offered by the Federal Reserve Regulation Q materials for product development and as supporting documentation for examination and compliance purposes.

ABA and TCH recommend a transitional period for the retention and management of the library of Federal Reserve Regulation Q materials. As of July 21, 2011, the Regulation Q documentation should be retained for a period of 18-months or more. During the initial 18-month retention period, the library should be available electronically and fully searchable. For examination purposes, the FDIC should incorporate the Federal Reserve principles in these rulings into a Financial Institution Letter (FIL). After 18 months and the creation of the FIL, the library should be maintained in some format for historical and research purposes.

Existing earnings credit programs developed according to the Federal Reserve standard set forth in interpretive letters and staff opinion should be grandfathered. The basis and validity of grandfathered programs should not be subject to new examiner scrutiny following the repeal of Regulation Q.

ABA and TCH appreciate the opportunity to comment on this proposed rulemaking. Please contact the undersigned with questions. Thank you for considering our comments and recommendations.

Sincerely,



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