May 7, 2019

Submitted Electronically

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

Re: Unsafe and Unsound Banking Practices: Brokered Deposits and Interest Rate Restrictions RIN 3064-AE94

Dear Mr. Feldman,

The Wisconsin Bankers Association (WBA) is the largest financial trade association in Wisconsin, representing approximately 230 state and nationally chartered banks, savings and loan associations, and savings banks. WBA appreciates the opportunity to comment on the Federal Deposit Insurance Corporation's (FDIC) advance notice of proposed rulemaking on brokered deposits (ANPR). WBA welcomes and supports FDIC's decision to undertake a comprehensive review of the regulatory approach to brokered deposits.

Summary

The rules, written over 30 years ago, today result in overly broad determinations as to who is a deposit broker, which impedes financial institution innovation through modern technologies, business models, and products. By taking this opportunity to refine "deposit broker" to a more workable definition, and modernize FDIC's interest rate cap calculation method, the rules can serve their Congressional purpose while still permitting bank growth, innovation, and flexibility in consumer products.

Section 29 of the Federal Deposit Insurance Act (Section 29) was enacted by Congress in 1989, as part of the Financial Institutions Reform, Recovery, and Enforcement Act. Section 29 sets restrictions on the acceptance of brokered deposits by institutions with weakened capital positions. Congress intended to prevent troubled institutions from holding funds placed by third-parties whose primary business is "placing deposits or facilitating the placement of deposits of third parties" with insured depository institutions. Since 1989, FDIC has issued a multitude of interpretations in the form of advisory opinions, FAQs, and other guidance. These interpretations expand who is considered a deposit broker, applying restrictions well beyond Congressional intent.

Congress adopted Section 29 in connection with the savings and loan crisis of the 1980s, after emerging electronic technologies made brokered deposits possible. Many savings and loans relied on funding through a new financial product developed in the 1960s: the certificate of deposit. Certificates of deposit were bundled for investors by third parties, which became known as brokered deposits. Brokered deposits were then new products, considered unstable and

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highly rate sensitive. Ultimately, institutions that depended on this type of funding were more expensive for the federal deposit insurance agencies to resolve in the event of failure.

Initial concern centered around brokered deposits contributing to irresponsible asset growth at some institutions. Section 29 was intended to make resolution of failed banks less costly by restricting weak institutions from holding brokered deposits. FDIC sought to regulate brokered deposits by limiting the deposit insurance available for such deposits. The regulation, first proposed in 1983, was ultimately enjoined by the courts on grounds that the rule exceeded agency authority. Congress adapted the FDIC's language but significantly restricted the scope of application. Despite this enjoiner and the narrowing of the provision's scope by Congress, FDIC has continued to rely on concepts contained within the earlier rule. FDIC expanded who is considered a deposit broker, narrowly interpreted exceptions, and applied restrictions beyond the focus of Congress. Specifically, this has resulted in inappropriate classification of certain entities as deposit brokers, such as: social media platforms, fintech partners (such as apps/application programming interfaces), bank affiliates and subsidiaries, and homeowners associations.

A fundamental role of banks is to provide financial services including deposit taking, lending, access to payments system, wealth management, trust and custody services and cash management services. Modern technology, including an increasing diversity of financial affiliations, and the creation of and growth in online and mobile banking, allows banks to offer these services, gather stable deposits and obtain access to potential depositors via new mechanisms.

Definition of "Deposit Broker"

WBA members are eager to meet customer needs by playing this role. In order to make this possible, it is imperative that FDIC improve and modernize its framework to focus on the original purpose of Section 29 and ensure that banks are not penalized for engaging in practices that are well within the bounds of a bank's normal course of business, including responding to evolving customer preferences and enhancing diversification and resilience in bank funding. For this to be possible, the definition of "deposit broker" and, by extension, application of what is a "brokered deposit" must evolve.

FDIC's current interpretation of deposit broker includes any third party, being, generally, "any person" engaged in "placing deposits...of third parties," and draws no further distinction. Because this interpretation hinges on the involvement of any third party, many modern deposits are scooped into this definition, despite being some of the most stable. Penalizing these deposits is harmful both to banks and their customers. In order to ensure that neither banks nor their customers are disadvantaged by an overly broad classification of deposits as brokered, WBA urges FDIC to limit the classification of an entity as a "deposit broker" to persons that contract to place deposits of unaffiliated third parties with banks or who contract with troubled insured depository institutions for the purpose of selling interests in their deposits to third parties.

Furthermore, FDIC must consider the importance of carving out certain deposits as not "brokered." For example, relationship deposits, which would include those generated from subsidiaries and affiliates of a bank, and other deposits involving a direct, continuing relationship between a customer and an insured depository institution should not be considered "brokered." WBA has found that these deposits are among the most stable. Such deposits should be expressly excluded from consideration as "brokered," even if an unaffiliated third-

party is involved in the origination of the deposit or maintains an ongoing relationship with the depositor independent of the deposit relationship. WBA has found little evidence that relationship deposits gathered through the normal course of providing banking services through affiliates or marketing partners pose enhanced risk to safety and soundness or the deposit insurance fund.

Brokered Deposit Rate Caps

In addition to setting restrictions on brokered deposits, Section 29 directs the FDIC to calculate a national rate cap on the interest rates weaker institutions may offer on deposits. The cap is established by adding 75 basis points to the "national rate." The national rate is currently established by taking a "simple average of rates paid by all insured depository institutions and branches for which data are available." Because banks with the most branches drive the calculation of the average rate, the current rate does not accurately reflect the cost of deposits for community banks, and others, that do not have extensive branch networks. As a result, the FDIC's rate can be (and currently is) significantly below market in a rising rate environment. It is also WBA's understanding that the rate caps do not factor in credit unions who are direct competitors of our members, operating in the same market space.

As a practical example, Ally Bank currently shows $115 billion in deposits as of March 31, 2019. Their current online savings account rate is 2.20% APY on all balance tiers. They only show one branch. Marcus by Goldman Sachs offers a savings account at 2.25%. Goldman Sachs Bank USA reported $145 billion in deposits from 2 branches. Under the weekly national rates and rate caps as of April 29, 2019, the rate cap for savings products was 0.85%. These Banks would not be effectively evaluated in an average rate paid based on their limited branch network. For many WBA banks, if they were to have a product similar to Ally or Marcus, those funds would be considered volatile funds during an FDIC examination because the rate was over the FDIC's national rate caps. The strict regulatory definitions do not factor in the overall relationship with the client. Banks now have the ability to market their products nationwide via digital platforms, so the use of branches to calculate rate caps to evaluate a volatile liability needs to change.

Many WBA member banks utilize wholesale lending, including brokered deposits, extensively and prudently manage the overall risks of such funding very well. Through these banks' capital and liquidity risk management tools, their concentration on the asset and liability side of their balance sheet, and regular liquidity stress testing, many of these banks maintain capital ratios well in excess of the definitions of well capitalized. Furthermore, at least one of these banks has further enhanced its risk management practices on capital by capital stress testing engaging a third party to assist in conducting capital stress testing.

The rates that banks choose to offer on deposits are determined by reference to a variety of factors across multiple tenors and products, including their competitors' rates, and various benchmarks including Treasury rates, Federal Home Loan Bank (FHLB) advances, swap rates, and money market rates, among others. However, the FDIC's methodology does not currently employ or consider these common benchmarks or indexes to set the national rate cap.

In order to identify outlier interest rates, as directed by the statute, we recommend that FDIC investigate the use of robust, transparent, and widely used benchmarks to determine a market interest rate, with an appropriate and dynamic add-on to establish a threshold for rates that are tolerably above market. For example, as a base rate FDIC could use the top ten rates posted on bankrate.com, a median of FHLB advance rates or a composite rate of widely understood and accessible benchmarks, or a combination thereof. The add-on to the base rate should be

dynamic to ensure the FDIC's national rate is well above that of the deposit market rate. WBA recognizes the difficulty of creating a rate that remains robust through all stages of the economic and interest rate cycles. We recommend that the FDIC allow banks to use their local FHLB advance rate, plus the FDIC's add-on, as an alternative to the national rates. The FHLB rates are a dynamic reflection of the regional market cost of funds and would likely be an accurate gauge of the market through the cycle. An accurate FDIC rate, with rate cap, should land sufficiently above normal market rates so as to identify only outlier deposit pricing, including deposit specials.

An artificially low rate is problematic for well-capitalized and weaker banks alike. Because examiners use the national rate cap as a proxy for higher risk deposits, even well capitalized banks are often discouraged from raising or holding deposits with a rate higher than the national rate cap. For weaker institutions, a non-competitive rate means that these banks have a reduced ability to improve their condition, as they are impaired in their ability to raise funds to sustain their assets. Moreover, as with other factors and items within the FDIC's brokered deposit framework, it is unclear how the 75 basis point add-on was derived, whether it allows for a sufficiently high level result during all phases of the interest rate and business cycles, or if it should be dynamic though the cycles.

Conclusion

WBA strongly suggests FDIC consider in its proposed rulemaking: narrowing the definition of deposit broker and, by extension, application of what is a brokered deposit; and revising FDIC's rate cap calculation method to reflect modern economic and rate trends.

WBA is grateful for the opportunity to comment on FDIC's consideration of modernizing brokered deposit regulations. We appreciate your consideration of these comments.

Sincerely,

Rose Oswald Poels
President/CEO