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March 13, 2007

Mr. Robert E. Feldman
Executive Secretary
ATTN: Comments/Legal ESS
550 17th Street, NW
Washington, DC 20426

RE: Federal Deposit Insurance Corporation; RIN 3064-AC98; Large-Bank Deposit Insurance Determination Modernization Proposal; 12 CFR Chapter III; 71 Federal Register 74857, December 13, 2006

Dear Mr. Feldman:

The American Bankers Association ("ABA") appreciates this opportunity to comment on the Federal Deposit Insurance Corporation's ("FDIC") advance notice of proposed rulemaking ("2006 ANPR") on proposed approaches to determine the insurance status of each depositor in the event of a depository institution failure.

The ABA submits these comments on behalf of the more than two million men and women who work in the nation's banks. ABA brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional, and money center banks and holding companies, as well as savings associations, trust companies, savings banks, and bankers banks – makes ABA the largest banking trade association in the country.

At the outset we wish to commend the FDIC for the open and inclusive process it has followed thus far in this project. While we have concerns with the substance of the 2006 ANPR as noted below, we very much appreciate the FDIC's willingness to engage the industry in ways to achieve the agency's objectives.

In our letter we make the following points:

- The 2006 ANPR would result in covered banks incurring real and substantial costs in return for no benefit to themselves and benefits to the FDIC that likely never will be realized.
- The FDIC should not proceed with this rulemaking without further research and consideration and only once the benefits significantly exceed the costs. As a major component in that exercise, the agency should minimize the costs to the industry to the maximum extent feasible. This

might be achieved, for instance, through implementation thresholds and FDIC development of software.

- Banks should not be required to tell their customers about the insurance status of a new deposit account when it is opened.
- FDIC insurance premiums should not be tied to a bank's development of such an insured deposit monitoring system, since the feasibility and value of such systems are as yet untested.
- To the extent that the FDIC chooses to include specialized institutions with fewer than 250,000 deposit accounts within the scope of its proposed rulemaking, it should develop a flexible and proportionate approach that is consistent with such institutions' existing operational framework.

Background

2005 Advance Notice of Proposed Rulemaking

In December 2005, the FDIC published an ANPR ("2005 ANPR") seeking comment on three options to address the FDIC's concerns that the existing deposit insurance determination process, by its very nature, imposes significant delays when applied to large and complex financial institutions. The 2005 ANPR targeted those financial institutions with more than 250,000 deposit accounts and total domestic deposits of at least $2 billion. The FDIC estimated in 2005 that such a proposal would apply to 145 financial institutions.

The options as proposed in 2005 would: 1) require financial institutions to maintain depositor data employing a unique identifier for each account on a continuing basis with the capability to place temporary holds on accounts as needed; 2) require financial institutions to maintain a program modeled after Option 1 except that it would be limited to information the financial institution "currently possesses" and would not require a unique identifier; and 3) require additional differentiation in accounts for the largest 10 or 20 institutions.

The ABA joined with America's Community Bankers and the Financial Services Roundtable ("Associations") in a March 13, 2006, letter to the FDIC in response to the 2005 ANPR. In that letter, the Associations recognized the value of "prudent systems to prepare for and respond to the failure of any size institution . . . ." However, the Associations concluded that imposing such a system as reflected in the FDIC's 2005 ANPR would impose high costs on affected financial institutions without commensurate benefit to the FDIC. In addition, the Associations questioned the advisability of pursuing "an expensive solution in search of a very low probability problem." The Associations advised that "The FDIC might be better served if it were to develop a mechanism to assist it in future large bank deposit determinations triggered when a bank reaches problem bank status."

2006 ANPR

The FDIC's 2006 ANPR further refines the FDIC's perspective on the process while adding an expanded scope of coverage for financial institutions in concert with greater compliance complexity.

In the 2006 ANPR, the FDIC proposes three coverage categories. "Tier 1 Covered Institutions" would include the largest, most complex institutions among those having a least 250,000 deposit accounts and more than $2 billion in domestic accounts. "Tier 2 Covered Institutions" would include those meeting the above tests but determined to have "lesser complexity." In addition, Tier 2 Covered Institutions would include as a separate category those financial institutions having at least $20 billion in domestic assets and $2 billion in domestic deposits without regard to number of accounts. "Non-Covered Institutions" would include those not meeting the above tests; such institutions would be exempt from any requirements as identified under the 2006 ANPR.

In terms of requirements, both Tier 1 and Tier 2 institutions would have many of the same requirements, including automated provisional holds and standardized data structure. Tier 1 institutions, however, would also be required to have a unique depositor identification for each depositor.

Discussion

1. The FDIC should perform a cost-benefit analysis that addresses the current limitations of the FDIC resolution process, the costs likely to be imposed on the industry, and alternative ways to achieve the FDIC's goals. The ABA has supported, and continues to support, the idea that no bank should be viewed as too big to fail. We understand the need for the FDIC to have in place workable procedures designed to maintain liquidity and confidence in the banking system. However, while enhancing the process of handling a failed bank is a laudable objective, the FDIC must balance whatever gains it believes could be achieved against the very real costs that would be imposed on the covered institutions.

The 2006 ANPR provides little analysis of precisely what problems the FDIC is attempting to solve. We understand that a large bank failure could require the FDIC to make deposit insurance determinations rapidly for hundreds of thousands or millions of accounts. What is less clear is whether the best way to position the FDIC to do this is to change the FDIC's systems, the systems of covered banks, or both. While the largest failure to date involved approximately 90,000 accounts, the 2006 ANPR does not explain what the shortcomings are in the current system that make a failed bank with more accounts problematic. Perhaps an analysis of those shortcomings would inform the decision about how best to tailor the solution.

The 2006 ANPR would require banks to absorb costs for software development, application of software to existing bank systems, employee training, periodic maintenance and mandatory testing. These costs are not inconsequential. Development and validation of the proposed systems would not be simple add-ons to existing deposit account systems. To begin with, most of the institutions with whom we have spoken have customized their systems to the point where the system developer cannot simply install a patch. Moreover, for each institution it would be an involved process to adjust its system to be able to impose provisional holds.

Any costs to private industry must be matched by a demonstrated public benefit. Cost estimates provided by our members ranged from $2 million to $6 million per institution for initial compliance, testing, and training, plus additional testing and validation costs of approximately $500,000 per year. These are rough estimates, of course, given that the ANPR, by design, did not provide enough specifications for a bank to know precisely what it would spend.

What is known, however, is that these real costs would be incurred for systems that have little likelihood of being used. As we advised in our letter to the FDIC about the 2005 ANPR, the recent history of deposit insurance and banking reform legislation in the last twenty some years suggests that the likelihood of a large bank failure has declined, and that careful consideration must be given to the costs to individual institutions of the approach advocated by the FDIC. This concern is as valid today as it was in 2005.

Implementation of important regulatory reforms, together with the continued refinement of the bank examination process through technology and enhanced examiner oversight, have demonstrably reduced the incidence of bank failures, and we see little prospect for major changes in the likelihood of failures. Many of the banks covered by the 2006 ANPR have examiners who are resident in those banks and are involved on a day-to-day basis in overseeing them. Engaging in a time-consuming deposit insurance identification process with a declining likelihood of ever needing to employ such a process is an expensive exercise that should not be engaged in without demonstrated justification. Thus, the ABA urges the FDIC not to move forward with this project unless the various costs to banks can be reduced to a minimum and those costs are outweighed by demonstrated benefits.

The 2006 ANPR, in its discussion of the likely values of the variables "Y" and "Z," refers to FDIC analysis of historical loss data for large institutions. The ABA encourages the FDIC to publish an analysis of the losses to the FDIC arising from payouts of uninsured funds resulting from depositors having more than one account. Such information likely would help inform the discussion about the costs and benefits of various alternatives.

The FDIC, as it considers the costs and benefits of the rule and ways to mitigate the costs, must also keep in mind the limited resources currently available to even the largest banks and the competing demands for those resources. Changes to risk-based capital rules, the rules governing FDIC insurance premium assessments, and a host of other regulatory initiatives – on top of the demands of running a bank in a safe and sound manner – will require resources that will not be available to implementing a new system that will do nothing to produce additional resources.

2. The FDIC should minimize the costs to the covered institutions as much as possible. The ABA believes that there are steps that can be taken to mitigate the likely costs of the proposed program, though we believe that even with implementation of these measures the costs will continue to outweigh the benefits of the proposal.

a. The FDIC should consider thresholds for implementation. The FDIC should fully consider the use of supervisory triggers that would require an insured depository institution to implement the rule only once the institution's condition deteriorates to a specified level. Not only would this avoid imposing significant costs unnecessarily, it would create additional incentives for a bank to operate in a safe and sound manner. While any rule along the lines described in the 2006 ANPR will require a lengthy implementation period, we believe it is incumbent on the FDIC to explore whether there are factors (a) that are highly correlated with bank failures and (b) that appear sufficiently in advance of failure to permit a bank to implement a system like what the FDIC is considering.

The 2006 ANPR, in noting that covered institutions are more likely to fail due to liquidity reasons prior to becoming critically undercapitalized, appears to be premised on the assumption that a covered bank is susceptible of failing too quickly to put the improved deposit determination system in place. We note that it is unlikely that liquidity itself would cause a bank to fail, given the wide array of private and public sources of liquidity available to banks today. Rather, elements of *insolvency* lead to *irresolvable* liquidity problems; these elements of insolvency are nearly always discernable over time, particularly for larger banks with many analysts observing and publicly commenting on a bank's performance.

Having said that, the FDIC is not limited to a bank being critically undercapitalized as the sole measure to trigger application of an insured deposit determination program. The FDIC could, instead, impose the rule only on covered banks that become undercapitalized, are downgraded to a CAMELS 3, or otherwise fail to meet objective supervisory criteria that create a demonstrably stronger likelihood of failure. The rule should not be imposed until it is clear that whatever led to the downgrade is not likely to be corrected within a short period of time. Moreover, there should be a clear correlation between the trigger used and heightened risk of failure.

A bank that is experiencing troubles typically will go through a number of steps well in advance of failing, including capital infusions, changes in policies and management, and other means by which to address a problem. Thus, it seems likely that warning signs will be available sufficiently in advance of any real threat of failure to implement whatever systems will be required. The FDIC has not provided examples of any bank that has failed since the adoption of the Federal Deposit Insurance Corporation Improvement Act and the implementation of prompt corrective action rules. This suggests that the FDIC could design a system that could be implemented after a triggering event but sufficiently before failure to permit implementation of the improved system envisioned by the FDIC.

b. The FDIC should develop and provide software to covered banks. The FDIC should explore opportunities to support the covered banks during the developmental and testing stages of the process. For instance, the FDIC should fully consider the possibility of developing software designed to provide a basic, uniform platform that all covered banks could use to implement the rule. The FDIC also could dedicate staff to provide technical assistance to banks covered by the proposal. With this software and level of support, banks could map the software provided by the FDIC to their systems. This would reduce the costs to the banking industry, provide the FDIC with a better understanding of each bank's existing systems and their strengths and limitations, enhance the ability of the FDIC to work with different types of institutions, and promote the use of a consistent platform at all covered banks that would benefit the FDIC in testing and resolution situations. After all, the proposal is, in effect, a prestaging of tools useful to the FDIC in handling resolution of failed banks rather than a resource to help healthy banks serve the day-to-day needs of their customers.

c. The rule should not require aggregation of accounts. The ABA opposes a deposit insurance determination system that requires banks to aggregate their deposit accounts to determine FDIC risk exposure. Aggregation not only dramatically increases the banks' costs of implementation, but it is so complex that many institutions would find it problematic to develop a workable system.

For many of the banks affected by the proposal, there are thousands of accounts opened and closed on any given day. Successful aggregation requires the cooperation of each person opening or closing an account to identify other accounts within the same institution. Account opening procedures would have to be changed to obtain this information, staff would have to be trained, and customers would need to understand the reason for the additional time and detail associated with the inquiry. All of this would result in enormous burdens on covered institutions.

Moreover, certain customers prefer for a variety of legal, business, and other personal reasons that their accounts not be connected. There must be a compelling policy reason to override such customer preferences. We submit that the speculative benefits the proposal might bring about fail to provide that reason.

d. The rule should not require unique identifiers. The ABA also opposes the introduction of a mandated unique identifier to any deposit insurance determination system. Banks have universally advised the ABA that such identifier would be prohibitively expensive to implement and would create the customer choice concerns noted above. If unique identifiers were to be required as part of the account opening procedure, extensive training of staff would be required, costs to the consumer would increase, and the account opening process would become significantly more cumbersome. As with the aggregation requirement discussed above, any requirement to have unique depositor identifiers would be enormously burdensome.

e. The FDIC should provide numerical values instead of variables. The 2006 ANPR suggests a system whereby banks would be required to place provisional holds on all accounts with over "X" dollars and then be able to put a hold of either "Y" or "Z" percent, depending on the size of the account. The FDIC would, under the 2006 ANPR approach, provide the numerical values of X, Y, and Z on the day a bank fails. It would be preferable for the FDIC to provide the actual dollar and percentage thresholds in the rule instead of requiring a system that must accommodate whatever figure is provided by the FDIC only when the bank is closed. Our members inform us that the programming is likely to be easier with known values than it would be if a covered bank had to program in the flexibility to use a range of numbers that would only become certain when the institution is at the point of failure.

f. The FDIC must provide adequate implementation time and flexibility. Regardless of the approach taken, the FDIC must ensure that there is adequate time for implementing any final regulation that results from this rulemaking process. This would be the equivalent in many respects of integrating new systems acquired through a merger. Covered institutions will need time to develop and apply whatever software is necessary for successful compliance with the regulation or customize software provided by the FDIC to their own requirements. They also will need time to test the software throughout the implementation process. Employees will need to be trained to ensure successful implementation of the proposal as finalized. This process is time consuming and expensive. To complete this effort, banks will likely need to reassign staff from their usual responsibilities to this project. No matter how much the FDIC can assist banks in their implementation efforts, this will not be a simple process.

The FDIC also should build into any rule sufficient flexibility for a bank to implement the rule in accordance with a schedule that minimizes burden to a given bank. Banks have different schedules for integrating new software and processes, and any final rule should accommodate

those differences. ABA members with whom we have conferred have identified 18 months as the absolute minimum amount of time that would be required to implement a proposal along the lines discussed in the 2006 ANPR. If the FDIC were to design software that could be used industry-wide, this perhaps would shorten the time required, but covered institutions still would need a significant length of time to map the software to their accounts and then test it and train personnel to use and service it.

g. Ongoing testing should be required only in certain circumstances, and then only as needed. ABA member banks have advised that testing will be an expensive undertaking not only in terms of out-of-pocket costs but also in terms of staff time to prepare for and execute each test. As previously suggested, we believe the rule should not be imposed until a bank crosses a predetermined supervisory threshold, such as becoming undercapitalized or downgraded to a CAMELS 3. Moreover, ongoing testing should not be required until a bank crosses such a threshold. Given the extremely low probability that the systems will be used and given the costs of testing, the ABA urges the FDIC to require testing only when there is a genuine possibility of the systems being used.

Once a bank crosses the threshold where testing becomes more relevant, even then testing should not be required more frequently than is absolutely necessary to ensure continued functionality. In addition, the FDIC should provide adequate notice to each bank of when the FDIC expects the testing to occur so that the testing can be scheduled contemporaneously with a bank's normal testing of its systems. According to some institutions, there is not enough time to do testing (including their own) between when accounts are closed late at night and opened again early the next morning. They advise that testing must be done over holiday weekends to avoid interference with customer access to their accounts.

3. Account opening procedures should not require bank personnel to opine on insured account status. Banks should not have to make determinations about the insurance status of each new deposit account and notify customers of the account status whenever a new deposit account is opened. Such determinations are more appropriately the responsibility of the FDIC. The training and compliance costs associated with any modifications to banks' account opening procedures would be enormous.

Perhaps of greater significance, any modification has the potential to affect customer relations negatively. This is especially so if the account opening process is lengthened and the customer, after hearing a discussion about insurance status, is left with the impression that the bank at which he or she has just entrusted his or her money is a candidate for failure. It is not in anyone's best interest to require regulatory disclosures that in their language could have the effect of undermining confidence in the banking system.

4. This rulemaking should have no relationship to FDIC assessments. In a separate notice of proposed rulemaking ("NPR"), the FDIC has proposed a procedure to adjust its deposit insurance premium assessment on banks with over $10 billion of assets.[1] One element of that NPR is a provision to consider a bank's insured deposit monitoring system.[2] ABA objects to this

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[1] Proposed Assessment Rate Adjustment Guidelines for Large Institutions and Insured Foreign Branches in Risk Category I, 72 Fed. Reg. 7878 (Feb. 21, 2007) (www.fdic.gov/regulations/laws/federal/2007/07noticeadjustment.pdf).

[2] Id. at 7880.

provision. As pointed out here, the benefits of such systems have not been demonstrated, whereas the implementation costs are high and unrelated to bank soundness. No benchmarks have been established to determine whether a bank has developed its insured deposit monitoring systems to the FDIC's satisfaction. Therefore, assessments should not be tied in any way to a bank's insured deposit monitoring system, and the assessment system should not be used as a back-door means to compel banks to develop such systems.

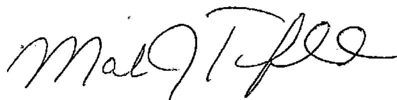
5. The FDIC should create a flexible and proportionate deposit insurance determination process for specialized institutions with fewer than 250,000 deposit accounts. In contrast to its original 2005 ANPR, the FDIC now proposes to include within the scope of the large bank deposit insurance determination process specialized institutions with fewer than 250,000 deposit accounts that have more than $2 billion in domestic deposits and more than $20 billion in domestic assets. The ABA is unconvinced that there is a well-defined need to include such institutions within the scope of the FDIC's proposed rulemaking. These institutions have materially different business, operational, and informational profiles. Moreover, they may present comparatively minor exposure of loss to the FDIC. To accommodate these differences, the ABA recommends the development of a flexible and proportionate approach, consistent with the data and processes already used by specialized banking institutions in the conduct of their day-to-day operations, rather than the establishment of a narrow "one size fits all" approach.

Conclusion

This letter outlines a few of the issues raised by the 2006 ANPR. Whether the issue is the aggregation of accounts, the use of a unique identifier or the testing of the system necessitated by a final regulation, the costs on covered banks are likely to be enormous. Such costs should be imposed only if the FDIC determines that they are outweighed by the benefits to be obtained.

The ABA appreciates the measured approach the FDIC has taken to ensure that the concepts underlying any deposit insurance determination proposal are fully vetted within the banking industry. The FDIC's issuance of a second ANPR on this subject and its willingness to meet with bankers to explain these concepts further demonstrates the commitment the FDIC has made to working with banks affected by the proposal. The ABA encourages the FDIC to continue this dialogue with the banking industry.

Sincerely,



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