R&T DEPOSIT SOLUTIONS

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November 20, 2024

Mr. James P. Sheesley
Assistant Executive Secretary
Attention: Comments — RIN 3064-AF99
Federal Deposit Insurance Corporation
550 17th Street N.W.
Washington, D.C. 20429

Re: Comment on Notice of Proposed Rulemaking on Brokered Deposits Restrictions (RIN 3064-AF99)

Dear Mr. Sheesley,

Reich & Tang Deposit Networks ("R&T") appreciates the opportunity to provide input to the Federal Deposit Insurance Corporation ("FDIC") on the Notice of Proposed Rulemaking on *Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions*, published on August 23, 2024 (the "Proposal").[1]

R&T was founded in 1974 and operates a leading sweep program network, providing services to more than 400 participating financial institutions. Through the administration of this network, R&T provides access to stable funding for banks and credit unions of all sizes.

We deeply value the FDIC's mission and role in upholding public confidence and ensuring financial stability through deposit insurance. The FDIC's emblem and the assurance of being "Backed by the Full Faith and Credit of the United States Government" are enduring symbols of the strength and resilience of our financial system.

As the banking industry has evolved from the traditional brick-and-mortar model to a more digital and networked landscape, R&T supports the FDIC's efforts to modernize deposit insurance rules to better reflect this new reality, particularly in light of the increasing participation of non-bank entities.

R&T believes, however, that many of the changes detailed in the Proposal are premature given that the FDIC recently revised the rule on brokered deposits (the "Rule") in 2020. These recent revisions were stress-tested in a series of bank failures, and were helpful in providing stability to the U.S. banking system.

[1] Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions, 89 Fed. Reg. 68244 (proposed Aug. 23, 2024) (to be codified at 12 C.F.R. pt. 303 and 337.

Before the FDIC makes significant revisions to the framework it established in 2020, we encourage careful study of the potential consequences from such changes to ensure that changes are made with following key considerations in mind which we discuss further below:

- Addressing depositor behavior with respect to specific classifications of deposits, as evidenced by recent bank failures; and
- The stabilizing impact of reciprocal deposits in reducing risk.

Given that the Proposal appears to lack consideration of the above criteria, we recommend that the FDIC monitor the market with these key considerations in mind before adopting any further revisions to the current Rule**.** This is particularly important in light of the expected change in leadership at the FDIC; new personnel should have the opportunity to consider any potential changes to the FDIC's regulatory framework, including changes that have been proposed but not yet finalized.

We also appreciate several components of the Proposal. For example, the FDIC's proposal to allow banks that receive a brokered deposit waiver to regain agent institution[2] status once they are deemed "well-capitalized" and "well-rated" will reduce confusion and provide greater certainty for banks and their customers. We would recommend that the FDIC retain these elements in future revisions to the brokered deposits regime.

I. Key Considerations Requiring Further Review

Current Material Gaps in Data on Depositor Behavior

The bank failures that occurred in 2023 underscore the critical need for better data on depositor behavior -- not only based on deposit category classification, but importantly whether consumers were focused on whether their deposits were insured or uninsured. The Proposal cites such examples from "recent events" and "recent experience"[3] but does not provide any relevant data indicating how depositor behavior may have been affected, if at all, by specific classifications of deposits—as brokered or core, insured or uninsured.

Consistent with its recent request for information on deposits,[4] R&T agrees with the FDIC that the collection and analysis of such data is critical. Only after such data is available to the FDIC and an analysis is performed should the agency seek to revise the existing brokered deposits framework.

For example, in the case of Silicon Valley Bank, the bank experienced a rapid withdrawal of large *uninsured* deposits that were also classified as *non-brokered* and were deemed to be

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[2] *See* Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions, 89 Fed. Reg. at 68249.

[3] *See id*. at 68250 – 68251.

[4] Request for Information on Deposits, 89 Fed. Reg. 63946, 63948 (Aug. 6, 2024) (the "RFI") (stating, that IDIs "do not report comprehensive data on the composition of insured and uninsured deposits").

"core", thus challenging long-held assumptions about the stability of core deposits. Other recent failures like that of First Republic and Signature have shown that the simplistic nature of the designation "core" vs "noncore" fails to capture the behavior of depositors during times of stress.

It is notable that the Proposal does not provide any analysis of the role that brokered deposits did—or did not—have in the large deposit outflows that occurred at many banks in early 2023. Nor does it analyze the stabilizing effect it had for certain banks over that same time period who needed to shore up funding.

It has been well reported that the bank failures in 2023 were caused in large part by pre-existing solvency and asset quality concerns, which were amplified by social media, a highly networked and concentrated depositor base, and advancements in technology. When concerns about SVB and then Signature Bank were raised, depositors instantly spread concerns about a bank run through social media, and were able, via technology, to withdraw funds at a rapid pace. This unusual confluence of factors impacting SVB and Signature Bank, while protecting other insured depository institutions that were rumored to be heading towards insolvency highlights the critical need for additional data to better understand the relationship between deposit category classification, insured and uninsured deposits, and the combined effect on depositor behavior.

As it acknowledged in the RFI on deposits, FDIC possesses limited information on the structure and stability of deposit categories such as uninsured or brokered. We believe the RFI is not only a good step towards closing this data gap, but is critical to informing the FDIC's proposed revisions to the brokered deposits framework.

The Stabilizing Impact of Reciprocal Deposits

As observed by both R&T and the FDIC, reciprocal deposits have proven to be a critical stabilizer during times of crisis. In considering amendments to the Rule, R&T urges the FDIC to afford greater weight to the role of reciprocal deposits in reducing risk for all banks.

Specifically, in the wake of the 2023 banking turmoil, R&T saw a surge in demand for our *Demand Deposit Marketplace*® (DDM®) program, enabling banks to diversify their deposits and to reassure customers that all their deposits were fully insured by spreading deposits throughout the 400+ participating institutions that make up the R&T network.

Likewise, the FDIC has acknowledged the stability of reciprocal deposits. In particular, in promulgating the Proposal, the FDIC references its 2011 study on core deposits,[5] in which the FDIC describes the following characteristics of brokered deposits: (i) deposits that can be gathered quickly in large quantities and used to fund risky assets or investments; and (ii) deposits that are not based on a customer relationship and can be easily withdrawn.

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[5] FDIC, Study on Core Deposits and Brokered Deposits (2011); https://www.fdic.gov/sites/default/files/2024-03/coredeposit-study.pdf.

The FDIC identified the same characteristics in its 2020 Final Rule to support a limited exemption for these arrangements from the brokered deposit rules by recognizing that reciprocal deposits may be a more stable funding source for healthy banks.

Research from the Federal Reserve Banks of Cleveland and Dallas has reinforced the risk-reducing nature of reciprocal deposits by increasing the amount of deposit insurance available to individual depositors.[6] So, too, has the FDIC championed reciprocal deposits as carrying less risk than brokered deposits. In its 2009 Assessments Rule, the FDIC acknowledged that "reciprocal deposits may be a more stable source of funding for healthy banks than other types of brokered deposits and may not be as readily used to fund rapid asset growth."[7]

The 2023 challenges to the banking system demonstrate that reciprocal deposits added stability to the deposit system, but the implementation of certain aspects of the Proposal could undermine the stability these deposits provide. For example, the Proposal, penalizes banks that fail to be well-rated or well-capitalized that choose to increase their reciprocal deposit usage. As proposed, such institutions would be forced to reclassify the entire balance reciprocal deposits as brokered deposits, rather than just the amounts over the 25 percent limit.

Such proposed treatment serves as a strong deterrent for using reciprocal deposits because banks face the risk of disclosing a potentially large increase in brokered deposits and signaling to market participants that the bank is no longer rated a CAMELS 1 or 2, which has long been viewed as confidential supervisory information. While we recognize the FDIC's intent to simplify the brokered deposit definition, we encourage a more nuanced approach. We ask that the FDIC, as part of the implementation of the RFI, evaluate whether the recent evidence on the role of reciprocal deposits justifies a higher exemption threshold.

I. Potential Harm of Accelerated Changes to Deposit Regulations

The Proposal introduces significant changes to the treatment of sweep programs, including limiting the types of qualifying entities, changing the threshold for the "primary purpose test" from 25% to 10%, requiring firms to reapply for FDIC approval, and altering the denominator in the test from "customer assets under *administration*" to "customer assets under *management*."

We believe the Proposal seeks to implement too many changes simultaneously, adding complexity and burden to banks benefiting from this additional funding source. This approach may have unintended consequences on broader funding markets, which may be difficult monitor and assess. Accordingly, we recommend that before adopting revisions to the existing brokered deposit regime, the FDIC should monitor the impacts of each of the proposed changes in isolation and base the proposal on empirical findings.

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[6] Fed. Rsrv. Bank of Dallas, Reciprocal Deposit Networks Provide Means to Exceed FDIC's $250,000 Account Cap (2023) (updated Sept. 6, 2024), https://www.dallasfed.org/research/economics/2023/1128 (finding that reciprocal programs played a significant role in stabilizing midsized banks, helping them avoid insolvency and weather the storm of the 2023 U.S. banking crisis); Fed. Rsrv Bank of Cleveland, Reciprocal Deposits and the Banking Turmoil of 2023 (2024) https://www.clevelandfed.org/publications/economic-commentary/2024/ec-202414-reciprocal-deposits-and-banking-turmoil-2023.

[7] Assessments, 74 Fed. Reg. 9525, 9532 (Mar. 4, 2009) (to be codified at 12. C.F.R. pt. 327).

Sudden, sweeping changes to rules as fundamental as those dealing with deposits—the lifeblood of community bank funding— without a full data and analysis could have serious unintended consequences. These changes may force community banks to make unplanned adjustments to their core business models, leading to significant operational, legal, and compliance costs, potentially exacerbating the earnings pressure many community banks already face and ultimately reducing competition and local community support.

We, respectfully request that the FDIC consider whether this Proposal could require banks to rapidly restructure their balance sheets and operations, which could have a destabilizing effect on the broader market.

I. Conclusion

The Proposal raises several important issues that warrant thoughtful consideration and, in particular, careful study as to depositor behavior and the ongoing role of reciprocal deposits. R&T stands ready to assist the FDIC in further discussions and analysis, particularly in relation to the role of reciprocal deposits and cash sweep programs.

R&T is of the view that any amendments to the Rule undertaken without further review, and the opportunity for new agency personnel to consider such changes, would be premature and could create significant challenges for banks. We believe that a balanced and informed operate within it.

Sincerely,

[redacted]
Joseph Jerkovich (Nov 20, 2024 15:34 EST)

Joseph Jerkovich
President and Chief Executive Officer
Reich & Tang Deposit Networks, LLC (d/b/a R&T Deposit Solutions)