January 22, 2010

Jennifer J. Johnson
Secretary
Board of Governors
Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, DC 20551

Re: Docket No. R-1381, Regulation D Amendments Authorizing Establishment of Term Deposits

Dear Ms. Johnson:

We appreciate the opportunity to comment on the proposed amendments to Regulation D, Reserve Requirements of Depository Institutions, authorizing the establishment of term deposits.

Our organization, United Bankers' Bank (UBB), is headquartered in Bloomington, Minnesota and provides a comprehensive suite of correspondent banking services to community banks in a 13 state market area primarily located in the upper Midwest. We were chartered in 1975 as the nation's first bankers' bank, a bank owned solely by other financial institutions. Our history and experience in this area provide us with a unique perspective on correspondent banking.

While the effects of any new regulatory measure are always difficult to assess, UBB sees more negative impact resulting from the term deposit program than positive, and questions the underlying need for the proposal given other monetary control tools the Federal Reserve System ("Reserve System") has available.

Term Deposit Program Impact

UBB's overriding concern regarding the proposed term deposit program is the potential for increased competition between the Reserve System, other federal government agencies or GSE's, and the private sector banking system. This competition could take different forms:

1. **Decrease the availability and increase the rates on brokered deposits (CD's).**
   If banks have the option of placing investible funds in a zero risk weighted, fully guaranteed product through the Reserve Bank that is paying a competitive interest rate, they will do so. Because the Reserve System is a quasi government agency, there may be no dollar limit that the investing institution may have or consider with a Reserve Bank term deposit. Operationally for the investing bank, the Reserve Bank product may be

easier to manage with its funds in one safe, secure place. Interest rates on comparable alternative instruments offered by private industry will have to increase to compete with the rate and security being paid by the Reserve System. This also results in an unfair competitive advantage to the Reserve System. While higher rates are beneficial to the owner of funds, they are negative to the purchaser of such funds in the private marketplace. Financial institutions may find funding either more expensive or availability more limited, thus significantly impacting their bottom line. This effect is considerable, especially in the current economic environment.

2. **Decrease the availability and increase the rates on Fed Funds**.
Many correspondent banks, community banks, Federal Home Loan Bank, bankers' banks, and others depend on Fed Funds as an important source of funding. The Reserve System's proposed term deposit program could negatively affect the availability of Fed Funds and their cost if banks with excess funds find a more attractive product to invest in through the Reserve Bank. In a sharply rising rate environment, the private market rate on Fed Funds could increase quickly impacting interest rate margins and thereby adversely impacting the safety and soundness of many financial institutions.

3. **Competition with governmental or government sponsored agencies for funding**.
Many other government agencies or government sponsored entities rely on open-market funding for their various financing programs. The term deposit program would compete with these other agencies. Government could be competing with itself, forcing up borrowing costs for all.

4. **Direct competition with correspondent banks particularly when combined with other measures that the Reserve System has either proposed or has in some stage of formulation.**
Over the course of the past year several proposals have been initiated either by the Reserve System (or other federal regulatory authorities) that would place the Reserve System in a stronger and perhaps advantageous competitive position with the private sector. Those initiatives include the proposal to broaden how the private sector adjustment factor (PSAF) is calculated, introduction of excess balance accounts (EBA's), the Correspondent Risk Guidance Letter, and most recently, the proposed term deposit program. The Reserve System establishes many of the rules under which banks must operate. The Reserve System, through its Federal Reserve Banks, competes with the private sector correspondent banks through its operational services, and to some extent, through its limited credit services. Furthermore, the Reserve System also ensures that bank's comply with its rules and applies penalties if they do not. In short, the Reserve System sets rules, competes with those under its rules, and changes the rules where it deems appropriate, or as subject to broader congressional review.

UBB questions whether a more powerful Reserve System with increased regulatory authority as well as additional monetary tools is accretive to the important balance between governmental oversight of the private sector and hampering the private sector's ability to provide the financial resources that the economy requires. As an example, the term deposit program could impact economic recovery through minimizing the total pool of investible funds in the banking system by diverting a portion of those funds away from lending programs into “safe-haven” accounts at the Reserve Bank.

Despite major concerns, if the Reserve System determines that it will offer the term deposit program, UBB thinks it vital to allow correspondent banks to aggregate and/or act as agent for community banks participating in the term deposit program. A potential model would be how correspondent banks worked with the Reserve Banks allowing EBA access for their customers.

The Reserve System specifically requested comment on three questions (if term deposits are offered):

1. Limitations on the maximum amount of term deposits that an institution may hold. *The Reserve System may wish to consider a percentage of total capital such as 5%.*
2. What maturity or maturities would eligible institutions recommend as appropriate for term deposits? *The Reserve System might wish to mirror the debt offerings of the United States Treasury. However, there is a question of whether the Reserve System’s term deposit program would actually compete with Treasury Department debt offerings. Could one of the consequences of the term deposit program be a case of one government entity creating higher borrowing costs for another government agency, or the entire U.S. Government/Treasury?*
3. Are there basic terms and structures for term deposits other than those described in this notice that should be considered? *How the Reserve System determines the interest rate for different tiers of term deposit products is vital. If the Reserve System pays too much in comparison to the private market, disintermediation could result. What measures would the Reserve System take to ensure that it does not unfairly compete with private industry as well as the GSE’s? Has the Reserve System considered a PSAF adjustment for the term deposit program?*

While there would clearly be some benefits of the proposed term deposit program, UBB believes that the issues identified in this letter outweigh potential program advantages when viewed within the broader context of the role of government and private sector banking services.

Sincerely,

William C. Rosacker
President
United Bankers’ Bank
Bloomington, Minnesota