Promontory Interfinancial Network

Promontory Interfinancial Network, LLC
1515 North Courthouse Road
Suite 1200
Arlington, Virginia 22201-2909

T 703-292-3400
F 703-528-5700

www.promnetwork.com

April 3, 2015

Board of Governors of the Federal Reserve System
20th Street & Constitution Avenue, N.W.
Washington, D.C. 20551
Attention: Robert deV. Frierson, Secretary

Re: Risk-Based Capital Guidelines: Implementation of Capital Requirements for Global Systemically Important Bank Holding Companies (Docket No. R-1505; RIN 7100 AE-16)

Ladies and Gentlemen:

I am writing on behalf of Promontory Interfinancial Network, LLC ("*PIN*")[1] to comment on the proposal by the Board of Governors of the Federal Reserve System to establish a risk-based capital surcharge for the largest, most interconnected U.S.-based bank holding companies (the "*Proposal*").[2] The Proposal builds on the international standard adopted by the Basel Committee on Banking Supervision, but modifies it by including a "*method 2*" that, among other things, replaces the Basel Committee's substitutability indicator with a short-term wholesale funding ("*STWF*") score. Under method 2, other things being equal, a higher STWF score results in a higher surcharge.[3]

A principal component in calculating the STWF score for a calendar year is the daily average of STWF deposits during the previous calendar year. Although the STWF score reflects

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1 Founded in 2002, PIN provides funding, liquidity management and relationship-building solutions to the bank and brokerage industries. PIN offers services that include the Insured Network Deposits® service (IND®), which is a brokered sweep deposit service drawing funds from both non-affiliates and affiliates of receiving banks, the Certificate of Deposit Account Registry Service® (CDARS®), which is a reciprocal brokered deposit service for time deposits, and the Insured Cash Sweep® service (ICS®), which is a reciprocal brokered deposit service for non-time deposits.

2 79 Fed. Reg. 75473 (Dec. 18, 2014). Acronyms and capitalized terms used in this letter and not separately defined are used with their commonly recognized meanings.

3 The Federal Reserve notes, in the introduction to the Proposal, that "in most instances, a [globally systemically important banking organization ("*GSIB*")] would be subject to the surcharge resulting from method 2" and not method 1, because the method 2 surcharge would be greater. 79 Fed. Reg. at 75480.

designated weightings for remaining maturity,[4] the Proposal applies the same weightings to all types of unsecured (and often uninsured) wholesale funding provided by non-financial sector entities ("*Unsecured Wholesale Funding*") and all types of brokered deposits and brokered sweep deposits provided by a retail customer or counterparty ("*Retail Brokered Deposits*").[5]

PIN's comments in this letter respond to the Federal Reserve's Question 30: "Should brokered deposits and brokered sweep deposits provided by a retail customer or counterparty be excluded from a GSIB's short-term wholesale funding amount?"[6] We also address the related question whether fully-insured non-retail reciprocal deposits should be excluded from the STWF amount. In PIN's view, the Federal Reserve should exclude from the STWF amount fully-insured reciprocal brokered deposits, whether or not from retail customers, and fully-insured retail brokered sweep deposits from retail customers ("*Insured Reciprocal and Retail Sweep Deposits*"). At the very least, if Insured Reciprocal and Retail Sweep Deposits are not excluded, the Federal Reserve should adjust their weightings to come closer to reflecting their demonstrated stability.

Discussion

The Proposal acknowledges that short-term wholesale funding normally provides benefits, but states that, during periods of stress, "reliance on short-term wholesale funding can leave firms vulnerable to runs that undermine financial stability."[7] In seeking to address vulnerability to runs, the Proposal treats all types of Unsecured Wholesale Funding and all types of Retail Brokered Deposits as if they all presented the same run risk. As the banking agencies have acknowledged, however, and as the empirical evidence shows, Insured Reciprocal and Retail Sweep Deposits are markedly different from, and more stable than, other types of deposits in the STWF amount, which includes deposits that are uninsured and deposits that otherwise lack the stability-promoting characteristics that Insured Reciprocal and Retail Sweep Deposits display.

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4 The weightings are 50% if the remaining maturity is 30 days or less, 25% if the remaining maturity is 31 to 90 days, 10% if the remaining maturity is 91 to 180 days, and 0% if the remaining maturity is 181 to 365 days. 79 Fed. Reg. at 75488.

5 *See id.*

6 *Id.*

7 79 Fed. Reg. at 75474.

By treating Insured Reciprocal and Retail Sweep Deposits as if they presented the same run risk as uninsured STWF deposits, the Proposal assumes – contrary to the entire 82-year history of the FDIC – that the presence of deposit insurance has no effect on vulnerability to runs. Indeed, the Proposal expressly declares its indifference to the presence of deposit insurance, making the blanket statement that Retail Brokered Deposits, which may or may not be insured, are volatile "notwithstanding the presence of deposit insurance."[8] The Proposal also disregards the additional characteristics, such as (among others) the relationship-based nature of reciprocal arrangements and the transactional nature of brokerage accounts in sweep arrangements, that also make Insured Reciprocal and Retail Sweep Deposits stable.

Moreover, the Proposal's approach not only lacks an empirical basis, but cannot be squared with the final liquidity coverage ratio rule (the "*LCR Rule*") that the federal banking agencies, including the Federal Reserve, adopted just a few months before the Proposal was released.[9] The LCR Rule establishes outflow rates for various types of liabilities that go to exactly the same point – concern with run risk in times of stress – that the Proposal states it is designed to address.[10] Unlike the Proposal, however, the LCR Rule recognizes that run risks for all wholesale funding and all brokered deposits are not the same. The LCR Rule therefore assigns different outflow rates to different types of deposits depending on among other things, whether the deposits are insured, whether they are wholesale or retail deposits, and whether they are transactional, reciprocal, or sweep deposits.

Whereas the LCR Rule assigns an outflow rate as high as 100% to some retail brokered deposits,[11] the outflow rate for insured retail reciprocal brokered deposits is 10%,[12] the outflow rate for insured retail brokered sweep deposits from affiliates is 10%,[13] and the outflow rate for insured retail

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8 79 Fed. Reg. at 75487.

9 79 Fed. Reg 61440 (Oct. 10, 2014).

10 The outflow rates in the LCR Rule and the STWF score are both liquidity metrics designed to account for run-risk associated with different types of liabilities.

11 LRC Rule § 32(g)(1).

12 LCR Rule § 32(g)(5). The outflow rate for insured non-retail reciprocal deposits is 40%. *See* LCR Rule §§ 32(h)(2).

13 LCR Rule § 32(g)(7).

brokered sweep deposits from non-affiliates is 25%.[14] The outflow rates in the LCR Rule for uninsured deposits of these same three types, which are significantly higher, indicate that the presence of insurance alone reduces the run risk of otherwise *identical* deposits by between 37.5% and 75%.[15] The Proposal completely disregards this powerful effect of insurance on run risk, as well as the available data and the other favorable substantive characteristics of Insured Reciprocal and Retail Sweep Deposits that, as the LCR Rule also acknowledges, reduce the vulnerability of such deposits to runs.

Available Data

Annex 1 and Annex 2 present data on a variety of aspects of the performance of deposits arising, respectively, from PIN's CDARS and ICS services (as the primary examples of insured reciprocal deposit services) and from PIN's IND service (as the primary example of an insured retail sweep service). As reflected in Annexes 1 and 2, deposits placed through such services demonstrate exceedingly high levels of stability, even in times of stress.

First, with respect to CDARS and ICS and referring to Annex 1:

- As shown in Figure 1, CDARS reciprocal deposits display exceedingly high reinvestment rates, consistently and even in times of stress, for both retail and non-retail reciprocal deposits. From Q1 2007 to Q4 2014, which included the most recent financial crisis in its entirety, the quarterly CDARS reciprocal reinvestment rate averaged 81.0%. For 2014, average reinvestment rates were 88.0% for individuals, 87.7% for businesses, 73.9% for public entities, and 87.0% for non-profits.

- As shown in Figure 2, CDARS reciprocal deposits also display exceedingly high reinvestment rates not only for CDARS reciprocal deposits with original terms of 91-180 days, which the Proposal weights at 10%, but also for those with original terms of up to 90 days, which the Proposal weights at 25-50%. Indeed, for January 2014 to March 2015, the average monthly CDARS reciprocal reinvestment rate for original terms of up to 90 days was 89%, which was even higher than rate for original terms of 91-180 days.

- As shown in Figure 3, CDARS reciprocal early withdrawal rates are extremely low for both retail and non-retail reciprocal deposits. From Q1 2007 to Q4 2014, the CDARS early withdrawal rate averaged less than 1% of overall balances on a quarterly basis. For

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14 LCR Rule § 32(g)(8).

15 *See* LCR Rule §§ 32(g)(5), 32(g)(6) (10% rate for fully-insured retail reciprocal brokered deposits becomes 25% if the deposits are not fully-insured); LCR Rule §§ 32(g)(7), 32(g)(9) (10% rate for insured retail brokered sweep deposits from affiliates becomes 40% if the deposits are not fully-insured); LCR Rule §§ 32(g)(8), 32(g)(9) (25% rate for fully-insured retail brokered sweep deposits from non-affiliates becomes 40% if the deposits are not fully-insured insured).

2014, average early withdrawal rates were 1.00% for individuals, 0.79% for businesses, 0.13% for public entities and 0.59% for non-profits.

- As shown in Figure 4, CDARS reciprocal early withdrawal rates are also extremely low for CDARS reciprocal deposits with remaining maturities of up to 90 days, as well as for those with remaining maturities of 91-120 days. For January 2014 through March 2015, the monthly early withdrawal rates for CDARS reciprocal deposits with remaining maturities in these two cohorts both averaged less than 0.1% of balances for the cohort.

- As shown in Figure 5, ICS reciprocal deposits are also extremely stable, as shown by uniformly positive month-to-month balance changes for every month since inception, even after early ramp-up growth. In 2014 and again in the first three months of 2015, the average monthly change in ICS reciprocal deposits was +2.5%.

- As shown in Figure 6, the ICS reciprocal account closure rate is consistently very low across retail and wholesale customer classes and has always been lower than the ICS account opening rate. For 2014, average closure rates were 2.7% for individuals, 1.7% for businesses, 1.4% for public entities and 1.3% for non-profits, and the account opening rate averaged 4.0%.

Second, with respect to IND and referring to Annex 2:

- As shown in Figure 1, IND sweep deposit balances have actually increased, rather than having decreased, during crisis periods, reflecting customer perceptions of the safety of fully-insured sweep deposits as compared to alternatives.

- As shown in Figure 2, since January 2007, the percentage month-to-month change in IND deposit balances, consistently and in times of stress, has been positive, without material decline.

- As shown in Figure 3, since January 2007, the percentage change in daily IND balances has remained largely within +/- 0.5%, and the single largest daily outflow represented only 1.3% of program balances.

Substantive Characteristics

In the preamble to the LCR Rules, the Federal Reserve and other federal banking agencies identified the key characteristic, in addition to insurance, that contributes to the stability of fully-insured reciprocal brokered deposits. The agencies observed: "Reciprocal brokered deposits generally have been observed to be more stable than typical brokered deposits because each institution within the deposit placement network typically has an established relationship with the retail customer or counterparty making the initial over-the-insurance-limit deposit that necessitates placing the deposit

through the network."[16] Reciprocal deposits are also more stable because the member of the network with which the deposits originate (*i.e.*, at which the customer has the initial account) sets the interest rate on the funds it places with other network members.[17] As the data cited above reflect, non-retail reciprocal deposits just as clearly display the positive effects of these stability-promoting characteristics.

In the case of fully-insured retail brokered sweep deposits, key characteristics that promote stability include, in addition to the presence of insurance:

- The customer funds swept to banks arise out of a relationship between a retail customer and a financial institution – typically a broker-dealer at which the customer maintains a brokerage account, likely to be a long-term relationship like the customer's relationship with its bank and, also like bank relationships, in many cases including other services.

- Brokerage accounts are inherently 'transactional." There are typically multiple aspects to the brokerage account relationship, including not only the use of the account for securities transactions, but also its use for transactions such as direct deposit, bill pay, and checking.

- The customer chooses the broker, and the broker sweeps the funds to banks with which it has contracted. In sweep programs such as IND, the broker identifies available banks that are acceptable to the customer. The broker is contractually obligated to fulfill the terms of its agreements with banks.

- The combination of small per account balances – which are fully insured – and the large number of accounts and customers in each broker-dealer's program contributes to the extraordinary stability of funds swept by a broker to individual banks across time periods, including during periods of stress.[18]

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16 79 Fed. Reg. at 61493.

17 *See* the definition of the term "*reciprocal deposits*" in Section 327.8(q) of the FDIC's Regulations, 12 C.F.R. §327.8(q) ("... each member of the network sets the interest rate to be paid on the entire amount of funds it places with other network members..."). In reciprocal deposit programs, that member is customarily referred to as the "*relationship bank*" because that bank has the relationship with the depositor providing the funds. Banks that receive funds placed through such a program are referred to as "*issuing banks*" or "*destination banks*." Funds are placed at destination banks in amounts below the FDIC standard maximum deposit insurance amount (currently $250,000) so that they will be insured under the FDIC's flow-through deposit insurance rules.

18 The average per-account cash balance that is swept is relatively modest—on average during the years 2008 to 2014 for IND, approximately $12,000 (although recent market trends have increased customer holdings of cash and this average has modestly increased to approximately $14,000 at the end of 2014). Across all broker-dealers, there are approximately 8 million depositors with over 42 million individual bank accounts for IND at year-end 2014.

- Unlike traditional brokered deposits, customer funds are being swept to banks for convenience and FDIC insurance coverage, not to implement a retail customer's search for yield. When customers are searching for yield, they use the same brokerage accounts involved to purchase securities.

Recommendation and Conclusion

For the reasons stated in this letter, we urge the Federal Reserve to exclude Insured Reciprocal and Retail Sweep Deposits from the STWF amount. If such deposits are included at all, the weightings for them should be substantially reduced in keeping with the LCR Rule outflow rates and the data discussed above.

The Proposal assigns weightings of 50% if the remaining maturity is 30 days or less, 25% if the remaining maturity is 31 to 90 days, 10% if the remaining maturity is 91 to 180 days, and 0% if the remaining maturity is 181 to 365 days.[19] As discussed above, however, the data show that Insured Reciprocal and Retail Sweep Deposits with remaining maturities of 90 days or less or with no maturities, which the Proposal weights at 25-50%, are at least as stable as those with remaining maturities of 91 to 180 days or more, which the Proposal weights at only 10%. Accordingly, if Insured Reciprocal and Retail Sweep Deposits are included in the STWF amount at all, their maximum weighting should be 10%, even when they have remaining maturities of 90 days or less or no maturities.

On a number of occasions, most recently in connection with the LCR Rule, we and others have provided documentation of the stability of Insured Reciprocal and Retail Sweep Deposits. Although, in our view, the evidence we have identified supports even more favorable treatment of such deposits, the LCR Rule acknowledges that different types of wholesale and brokered deposits present very different run risks, as reflected in the comparative outflow rates discussed above. The Federal Reserve and other banking agencies should adhere to the LCR Rule's recognition of this fact.

Proceeding otherwise on the reflexive assumption that all wholesale or brokered deposits are volatile, in addition to being unsupported by the evidence, would be counterproductive. If the final rule includes Insured Reciprocal and Retail Sweep Deposits in the STWF amount, and especially if it does so with the same weightings as less stable types of deposits in that amount, the rule will create competitive distortions rather than preventing them. Treating Insured Reciprocal and Retail Sweep

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19 *Supra* note 4.

Deposits the same as less stable types of STWF deposits devalues the relative stability of Insured Reciprocal and Retail Sweep Deposits. As a result, to the extent such a rule does not push deposits out of the banking system altogether, it overvalues less stable deposits, which can only work against the goals that the rule seeks to accomplish.

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Thank you for consideration of our comments. Should you wish to discuss them further, please contact the undersigned at (703) 292-3333 (mjacobsen@promnetwork.com).

Sincerely,

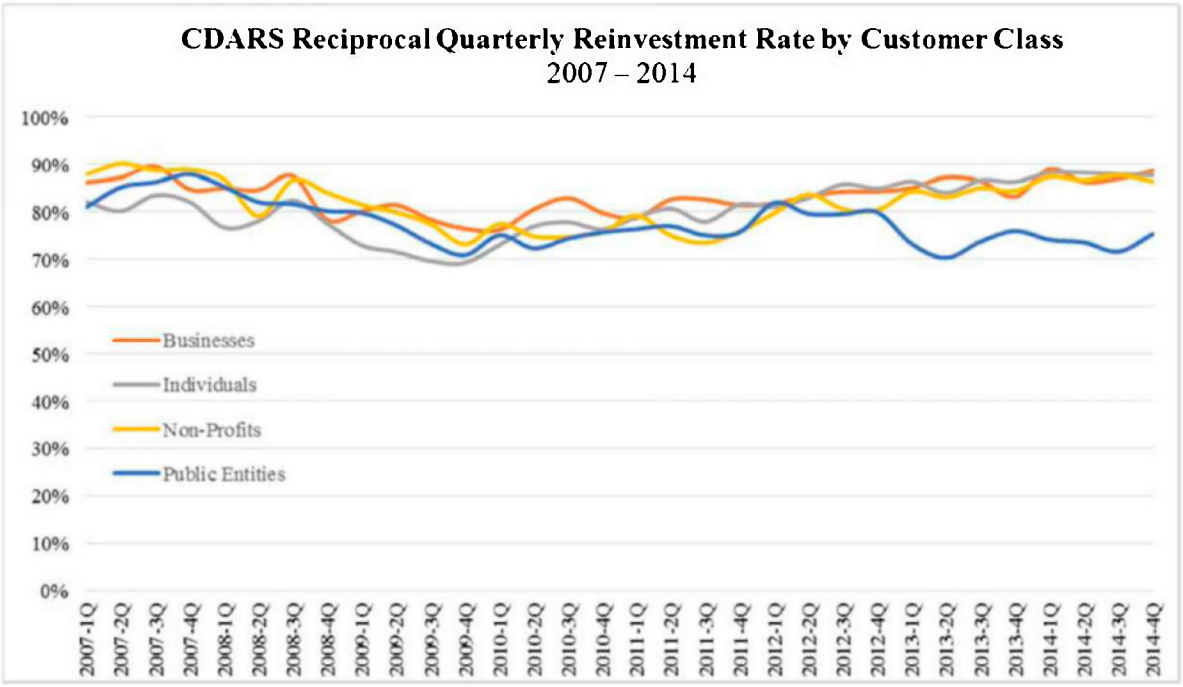
Mark P. Jacobsen
President and Chief Executive Officer

DATA AND STATISTICAL TABLES FOR PROMONTORY'S RECIPROCAL SERVICES (CDARS AND ICS)

1. **CDARS reciprocal deposits display exceedingly high reinvestment rates, consistently and even in times of stress, for both retail and non-retail reciprocal deposits.**

Figure shows reinvestment rates for CDARS reciprocal deposits on a quarterly basis from Q1 2007 to Q4 2014. Reinvestment rates for both retail and wholesale customer classes were exceedingly high throughout this period, which included the most recent financial crisis in its entirety. For the entire period, the quarterly CDARS reciprocal reinvestment rate averaged 81.0%. For 2014, average reinvestment rates were 88.0% for individuals, 87.7% for businesses, 73.9% for public entities and 87.0% for non-profits.[1]

Figure 1



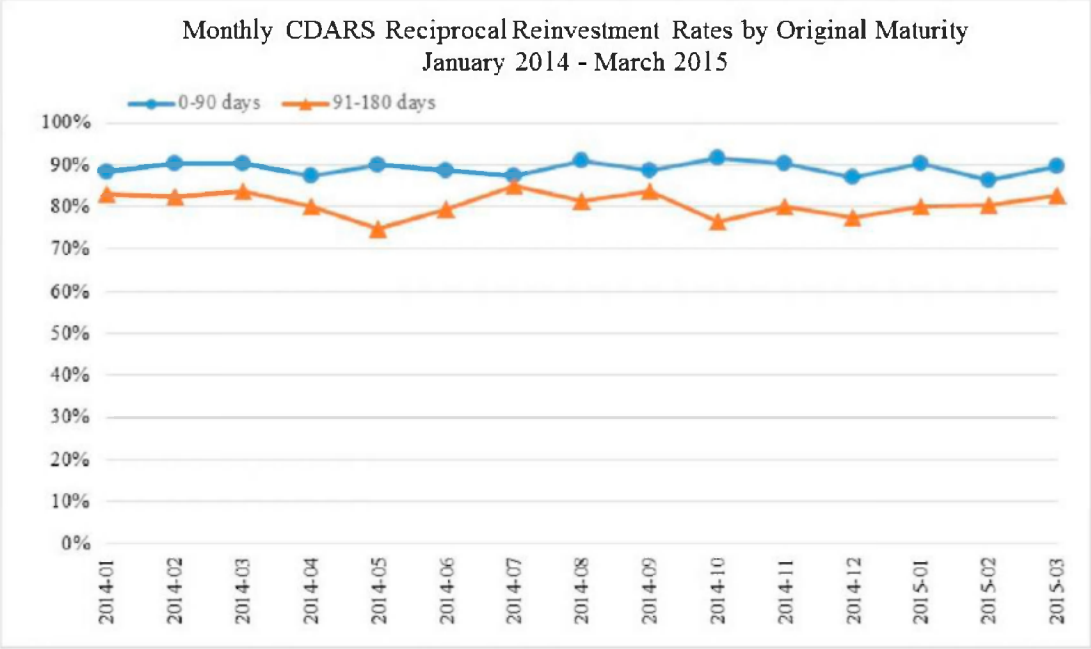
Source: Promontory Interfinancial Network

[1] CDARS reciprocal deposits are held by the following customer classes: Businesses – 28%, Individuals – 22%, Non-Profits – 14%, and Public Entities – 36%. Although banks can also place their own funds, their overall share of reciprocal deposits is *de minimis*.

2. CDARS reciprocal reinvestment rates are even higher for original maturities of up to 90 days than for original maturities of 91-180 days.

Figure 2 shows, for January 2014 through March 2015, monthly reinvestment rates for CDARS reciprocal deposits with original maturities of up to 90 days, which the Proposal weights at 25-50%, and for deposits with original maturities of 91-180 days, which the Proposal weights at only 10%.[2] As reflected in Figure 2, the reciprocal deposits in the up-to-90 days cohort had even higher reinvestment rates, averaging 89%, than those in the 91-180 days cohort, which averaged 81%.

Figure 2



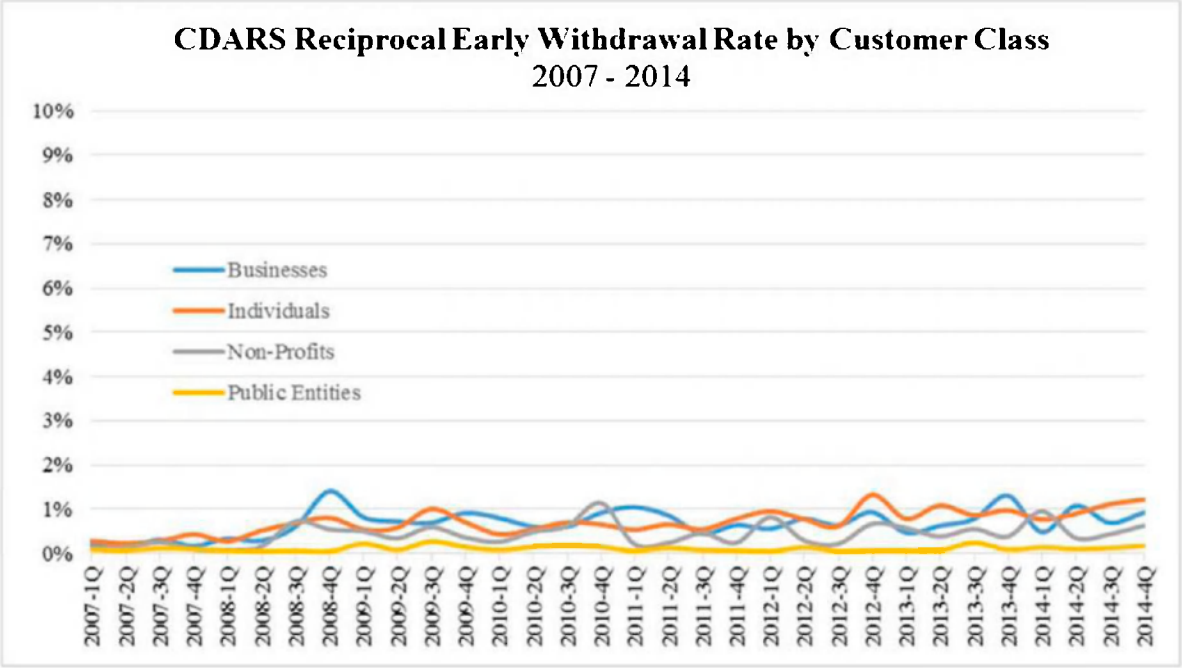
Source: Promontory Interfinancial Network

3. CDARS reciprocal early withdrawal rates are extremely low for both retail and non-retail reciprocal deposits.

Figure 3 shows early withdrawal rates for CDARS reciprocal deposits on a quarterly basis from Q1 2007 to Q4 2014. Over that period, the CDARS reciprocal early withdrawal rate averaged less than 1% on a quarterly basis. Early withdrawal rates throughout the period were extremely low across all customer classes. For 2014, average early withdrawal rates were 1.00% for individuals, 0.79% for businesses, 0.13% for public entities and 0.59% for non-profits.

[2] The CDARS reciprocal monthly reinvestment rate for a maturity cohort is (i) the maturing amount for deposits with original maturities in the specified range that matured that month and were reinvested as a percentage of (ii) the maturing amount for all deposits with original maturities in the specified range that matured that month.

Figure 3



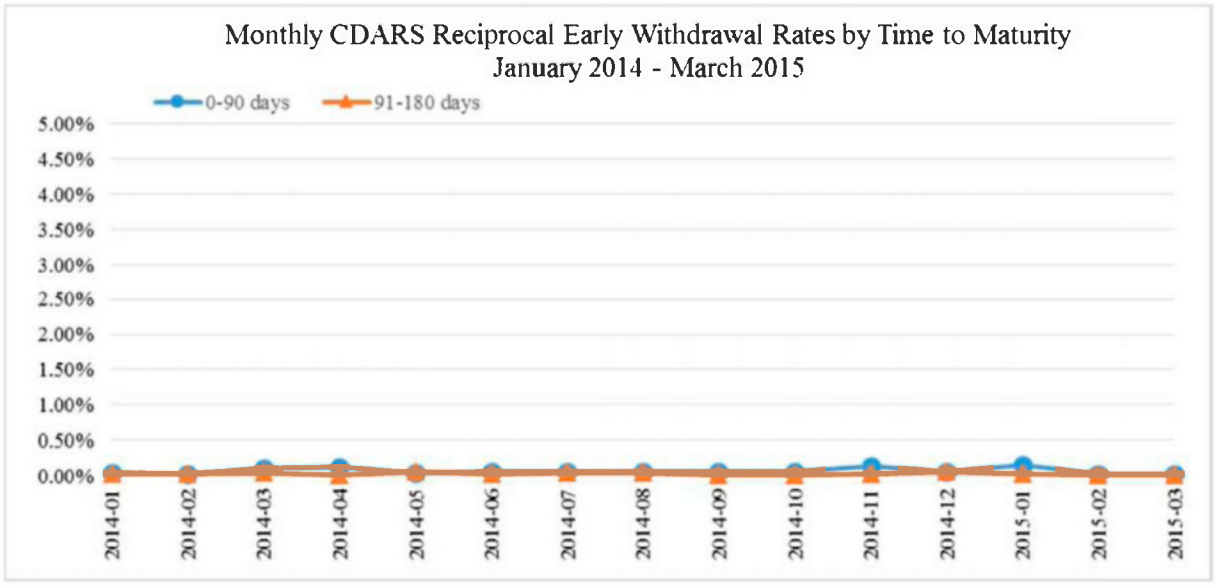
Source: Promontory Interfinancial Network

4. CDARS reciprocal early withdrawal rates are well below 0.1% of the cohort both for remaining maturities of 90 days or less and for remaining maturities of 91-180 days.

Figure 4 shows, for January 2014 through March 2015, monthly early withdrawal rates for CDARS reciprocal deposits with remaining maturities of up to 90 days and for those with remaining maturities of 91-180 days.[3] As reflected in Figure 4, the deposits in both cohorts had monthly early withdrawal rates of less than 0.1% of deposits in the cohort. The up-to-90 days cohort averaged a 0.07% monthly early withdrawal rate, and the 91-180 days cohort averaged a 0.03% monthly early withdrawal rate.

[3] The CDARS reciprocal monthly early withdrawal rate for a maturity cohort is the average of CDARS reciprocal weekly early withdrawal rates for the cohort in the month. The CDARS reciprocal weekly early withdrawal rate for a maturity cohort is (i) the sum of early withdrawals with a time to maturity in the specified range that week as a percentage of (ii) the outstanding CDARS Reciprocal balances with a time to maturity in the specified range as the beginning of that week. For the purpose of this analysis, weeks begin on Thursdays.

Figure 4



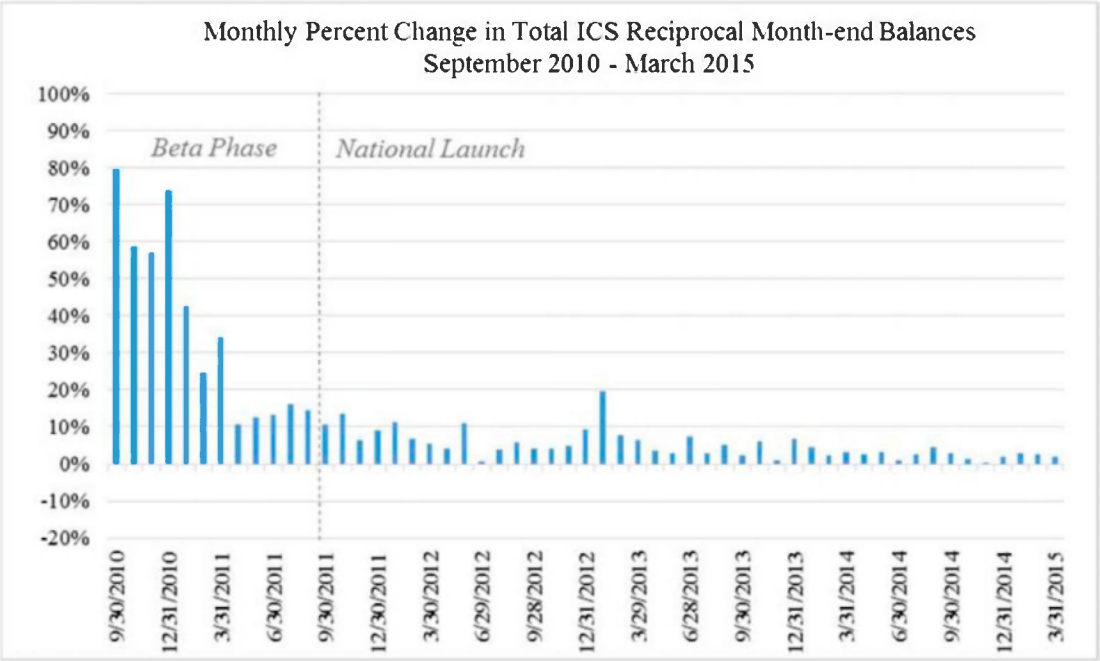
Source: Promontory Interfinancial Network

In addition, in 431 weekly observations since 2007, the up-to-90 days and 91-180 days cohorts have represented highly stable percentages of total CDARS reciprocal outstanding balances. The up-to-90 days cohort has represented an average of 45% of total CDARS reciprocal outstandings, with a standard deviation of 3%, and the 91-180 days cohort has represented an average of 24% of total CDARS reciprocal outstandings, with a standard deviation of 1%.

5. **ICS reciprocal deposits are also highly stable, as shown by uniformly positive month-to-month balance changes, even after early ramp-up growth.**

Figure 5 shows, for ICS reciprocal month-end balances, the average monthly change since inception of the service. As shown in Figure 5, these balances have shown positive month-to-month changes in every month, even after the early ramp-up growth. In 2014 and again in the first three months of 2015, the average monthly change in ICS reciprocal deposits was 2.5%.

Figure 5



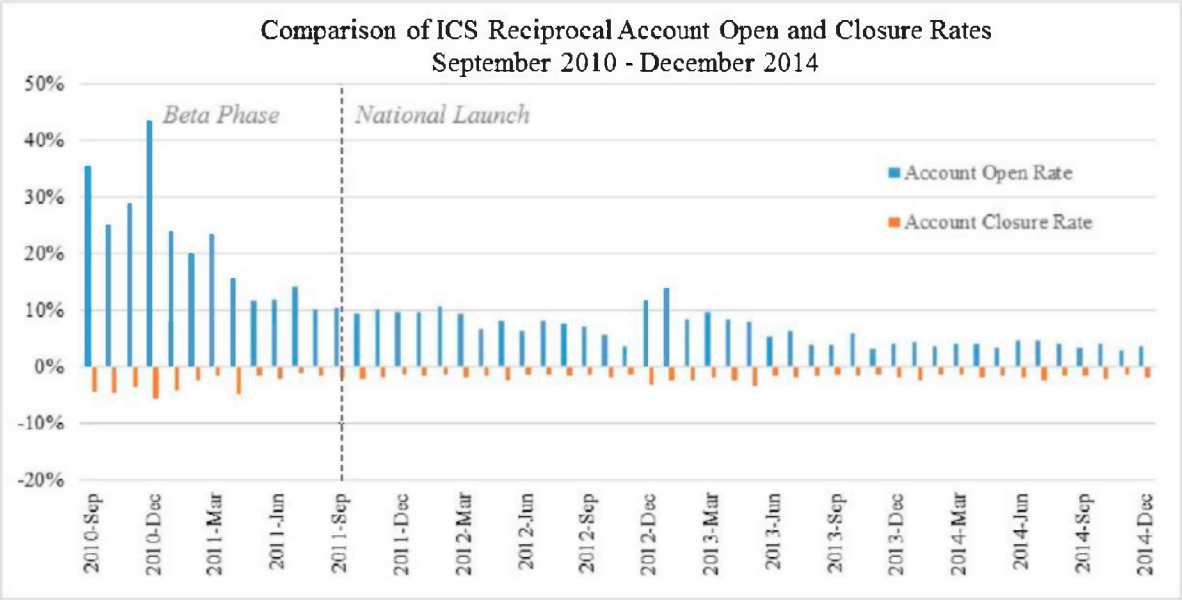
Source: Promontory Interfinancial Network

6. The ICS reciprocal account closure rate is extremely low across retail and wholesale customer classes and has always been lower than the account opening rate.

Figure 6 shows the ICS reciprocal account opening and closure rates since the inception of the service.[4] For 2014, average closure rates were 2.7% for individuals, 1.7% for businesses, 1.4% for public entities, and 1.3% for non-profits. Since inception, the monthly reciprocal account closure rate has always been lower than the monthly reciprocal account opening rate, which in 2014 averaged 4.0%.

[4] The ICS reciprocal account closure rate for a given month, expressed as a negative percentage in Figure 6, is the number of reciprocal accounts closed during the month as a percentage of the total number of reciprocal accounts at the beginning of the month. The number of reciprocal accounts closed during the month is the number of non-zero-balance reciprocal accounts withdrawn to zero dollars during the month and not returned to a non-zero-balance within 91 days. The ICS reciprocal account opening rate for a given month is the number of accounts opened during the month as a percentage of the total number of reciprocal accounts at the beginning of the month.

Figure 6



Source: Promontory Interfinancial Network

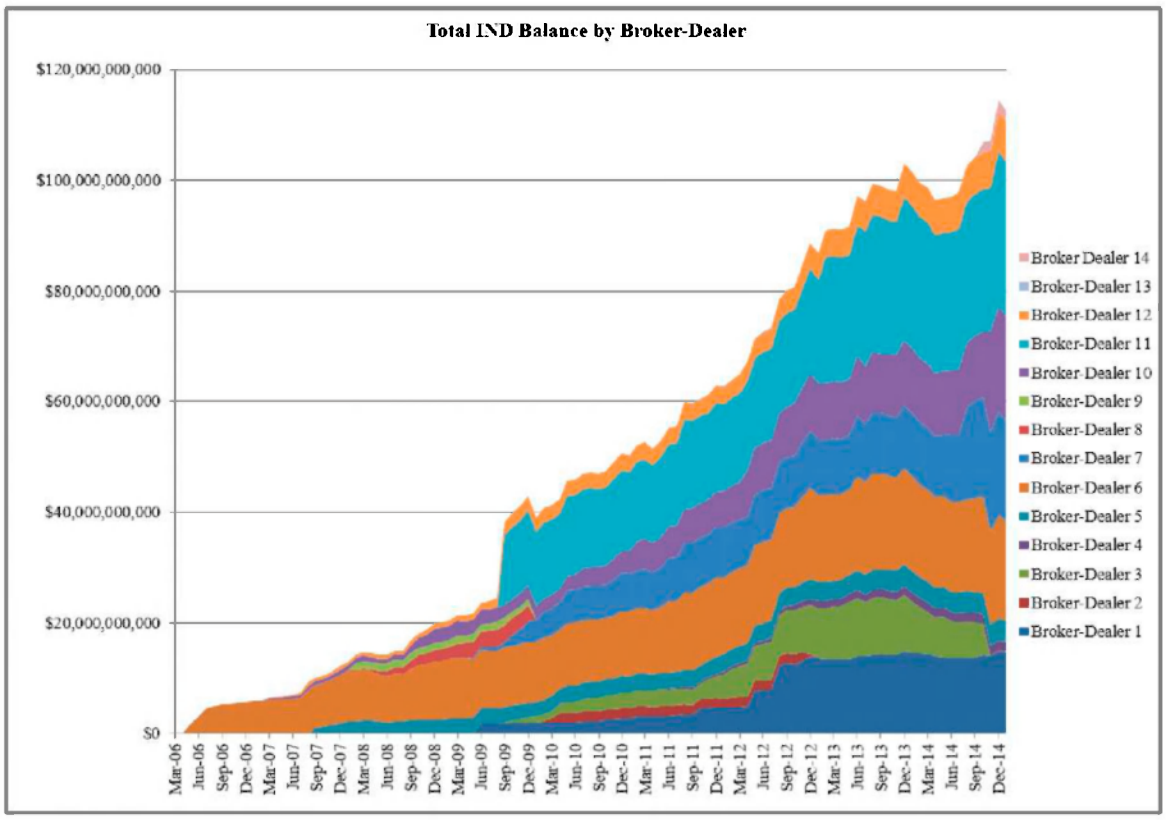
Annex 2

DATA AND STATISTICAL TABLES FOR PROMONTORY'S
RETAIL SWEEP SERVICE (IND)

1. IND balances by broker have steadily risen in value, without material decline.

Broker-dealer sweep deposits have provided a stable source of funding for decades. As shown in Figure 1, IND balances since inception have shown consistent and sustained growth. IND currently supports the sweeping of over $110 billion from broker-dealers into nearly 105 depository institutions.

Figure 1

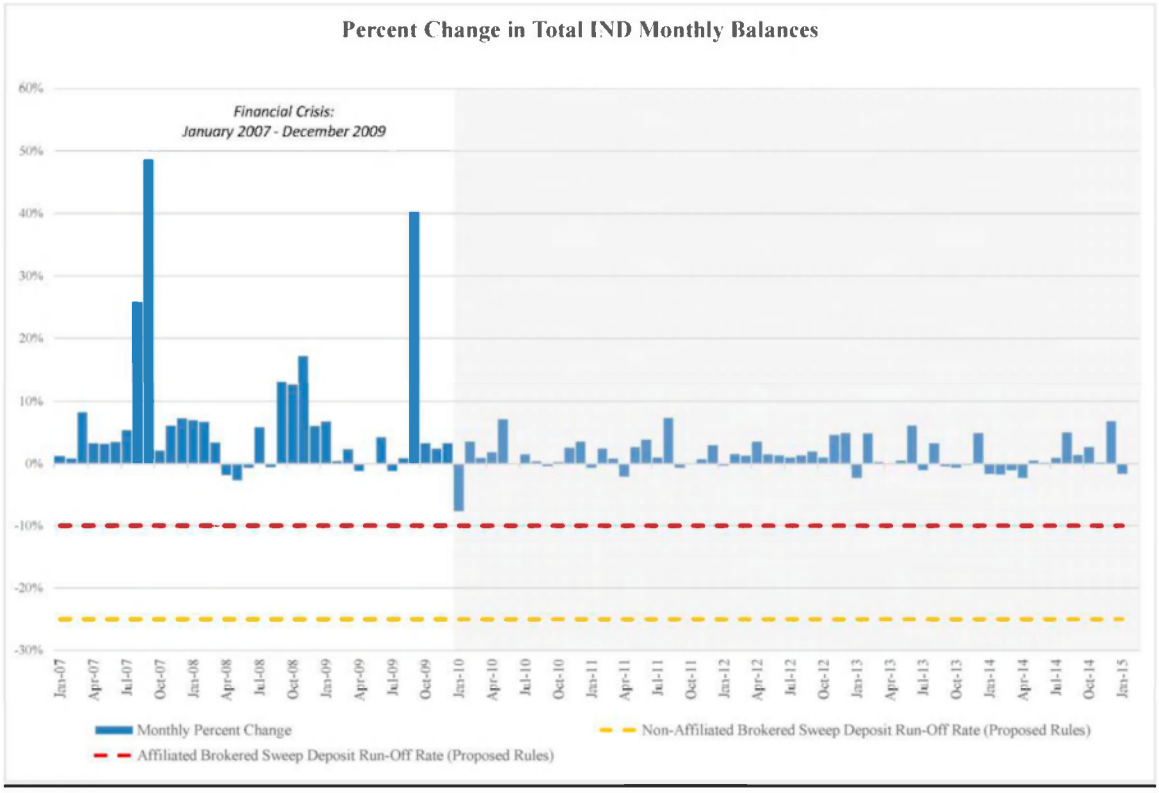


Source: Promontory Interfinancial Network

2. During the 2007-2009 financial crisis, IND balances increased in 30 of the 36 months, and the largest month-to-month decrease was less than 3%.

Figure 2 below shows the results of a deposit change analysis examining month-to-month changes in retail customers' IND deposits during and after the 2007-2009 financial crisis.[1] The outstanding balance of deposits increased in 30 of the 36 months of the financial crisis, and when the outstanding balance decreased at all, the decrease was minimal. The highest month-to-month outflow during that period, 2.6%, was significantly below the LCR's 10% outflow rate for affiliated sweep deposits and far below the LCR's 25% outflow rate for unaffiliated sweep deposits.[2]

Figure 2



Source: Promontory Interfinancial Network

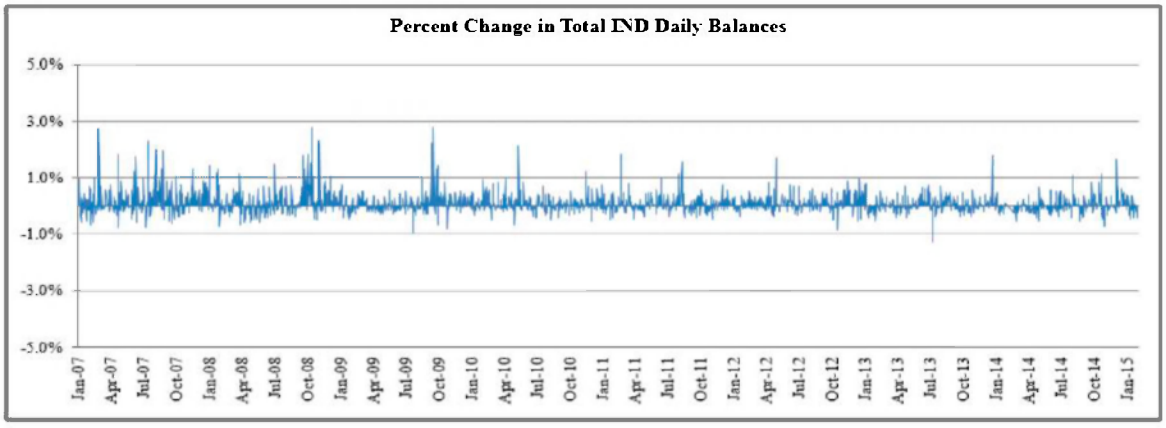
[1] The change in outstanding balance was calculated on the basis of total month-end deposits, including deposits from customer accounts that existed at the beginning of the month as well as new customer accounts that came into the bank over the course of the month.

[2] Month-to-month balances also remained highly stable after the 2007-2009 financial crisis. The only significant month-to-month outflows from 2010 to the present have resulted from changes in program participation (such as a bank leaving the program or requesting lower balances or a broker providing its balances a bank through a different provider) unrelated to run risk. Even with such changes, month-to-month outflows never reached the LCR Rule's 10% outflow rate for affiliated sweep deposits, much less the 25% outflow rate for unaffiliated sweep deposits.

3. IND balances show very low day-over-day volatility.

As shown in Figure 3, since January 2007, the percentage change in daily IND balances has remained largely within +/- 0.5%, and the single largest daily outflow represented only 1.3% of program balances.[3]

Figure 3



Source: Promontory Interfinancial Network

[3] Daily outflows resulting from changes in program participation unrelated to run risk are excluded from Figure 3 (but monthly outflows resulting from such changes are included in Figure 2).