



Testimony of

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On behalf of the  
**Independent Community Bankers of America**

Before the

United States House of Representatives  
Committee Financial Services  
Subcommittee on Financial Institutions and Consumer Credit

Hearing on

**“Examining Legislative Proposals to Address Consumer  
Access to Mainstream Banking Services”**

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Washington, D.C.

## **Opening**

Chairman Neugebauer, Ranking Member Clay, and members of the Subcommittee, my name is Ronald D. Paul and I am Chairman and CEO of EagleBank, a \$6.4 billion asset community bank headquartered in Bethesda, Maryland. I'm pleased to testify today on behalf of the Independent Community Bankers of America (ICBA) and the nearly 6,000 community banks we represent. Thank you for convening today's hearing on "Examining Legislative Proposals to Address Consumer Access to Mainstream Banking Services."

We are pleased to offer our support for several of the bills before the Subcommittee today that will provide security for bank depositors, help community banks remain competitive with larger banks, and provide them with resources to better serve their communities. You have an opportunity to enact legislation that will have a meaningful impact in our communities before the close of the 114<sup>th</sup> Congress, and I strongly encourage you to do so.

EagleBank has 430 employees and serves 12,000 customers through 21 branch offices in the Washington, D.C. metropolitan area. We specialize in commercial lending to small and medium sized businesses, though we also serve consumers. EagleBank is also active in real estate lending and is the leading community bank SBA lender in the Washington, D.C. region. EagleBank is deeply engrained in the markets we serve. We believe that to successfully serve a community, a bank must be part of the community. Our employees live, work, volunteer, raise their families, and school their children in the Washington area. Our management decision makers are accessible by the residents, businesses, institutions, and civic organizations that make up the community.

Consistent with this philosophy, we also believe that deposits raised in a community should be deployed in that community, not transferred to markets in another region of the country.

Bills before this Subcommittee today, H.R. 4116, H.R. 5660, and H.R. 6162, will help keep deposits in the community. These bills, and H.R. 4116 in particular, will be the focus of my remarks. The common theme of these bills is that the FDIC's classification of deposits must better reflect their true characteristics. Rational, fact-based deposit classification will help community banks fund more lending to keep pace with the strengthening economic recovery. ICBA supports these bills for the reasons discussed below.

### **H.R. 4116**

Introduced by Representatives Gwen Moore and Thomas Emmer, H.R. 4116 would promote the use of reciprocal deposits as a stable source of funding to support community lending.

Reciprocal deposits allow a depositor to receive FDIC deposit insurance on deposits that exceed the \$250,000 insurance limit without the inconvenience of depositing funds in different banks. A bank distributes the amount of a deposit that exceeds the \$250,000 insurance limit through a network of banks and receives reciprocal deposits back from other banks in the network. The customer enjoys the convenience of continuing their relationship with one local bank, with only one account to keep track of, and receiving the benefit of full deposit insurance. To the customer, this is a seamless experience. The bank gets the benefit of obtaining a large deposit from a local customer, funds that can be put to work in its community. These funds might otherwise go to a large bank outside the community or to a money market fund.

EagleBank uses reciprocal deposits to serve local customers – local governments, foundations, businesses, law firms, and individuals. Many of these entities have charters, bylaws, or legal mandates that require deposits to be insured or be held at minimal risk of loss. Their accounts include checking accounts, money market accounts and certificates of deposit. Our customers take great interest in where they place their deposits and how they are utilized. They have affirmatively chosen to use a locally-based community bank precisely due to their recognition of our role in their local economy. Serving these customers and ensuring that their deposits are fully insured is critical to our business model. Reciprocal deposits are a significant source of funds that support our lending to local small businesses, as well as consumer and commercial mortgages. This lending activity fuels the growth of local businesses, creating jobs and stimulating growth in the regional economy. Without deposits, we cannot continue our lending activity which in part fuels the local economy.

I would particularly like to highlight that many local governments in the Washington area recognize this and keep reciprocal deposits in local banks. EagleBank participates in formal programs with several of them whereby we track loan activity and job creation associated with their deposits. Without the insurance available on reciprocal deposits these types of programs would not be feasible. Our use of reciprocal deposits is typical of many other community banks. Some 3,000 banks – nearly all of them community banks – participate in reciprocal deposit networks.

The problem is that the FDIC currently considers reciprocal deposits to be “brokered deposits,” putting them in the same category with deposits solicited from third party, money center brokers or other firms outside of our market. In a brokered deposit, the depositor is not a customer of the bank, has no relationship with the bank, and probably does not reside in the same community. A brokered deposit merely seeks the highest interest rate.

Brokered deposits are disfavored and discouraged by the FDIC because they are not considered to be a stable source of funding. They are, potentially, “hot money” ready to flee the bank at the first sign of distress or to chase a higher interest rate. “Core deposits,” by contrast, are “sticky,” more likely to stay with the bank over the long term because the depositor is a local customer, has a long-standing relationship with the bank, and may

also have a loan facility or use other bank services. We and many impartial economists and financial analysts believe reciprocal deposits are core deposits.

Reciprocal deposits have none of the characteristics of brokered deposits that warrant the limitations the FDIC has imposed. They are not hot money. A 2014 joint study by the FDIC, the OCC, and the Federal Reserve acknowledges as much, finding that: “Reciprocal brokered deposits generally have been observed to be more stable than typical brokered deposits because each institution within the deposit placement network has an established relationship with the retail customer.” Further support for the stability and value of reciprocal deposits is found in a 2011 study by Alan Blinder, the Princeton academic and former Vice Chair of the Federal Reserve, and Arun Shastri who conclude: “Our analysis shows that while greater use of certain brokered deposits appears to increase the risk of failure, greater use of CDARS Reciprocal Deposits (the most widely used type of reciprocal deposits) probably decreases it.” This authoritative and impartial analysis is fully consistent with our experience with reciprocal deposits at EagleBank. They are a stable and dependable source of funding and behave exactly like EagleBank’s other core deposits.

H.R. 4116 would address the above-stated concerns by amending Section 29 of the Federal Deposit Insurance Act, which imposes limits on the use of brokered deposits, to provide a limited exception for reciprocal deposits. H.R. 4116 includes carefully crafted limitations, or safeguards, which include (i) a limit on the amount of reciprocal deposits a bank may hold under the exception – the lesser of \$10 billion or 20 percent of its total liabilities; and (ii) a requirement that the bank either have a rating of outstanding or good and be well-capitalized, obtain a waiver from the FDIC, or limit its holdings of reciprocals to the amount it has previously held. H.R. 4116 also includes other provisions that give the FDIC full discretion to address safety and soundness concerns that arise from the use of reciprocal deposits.

The limitation on reciprocal deposit holdings noted above will ensure the bill is focused, as it should be, on reciprocal deposits used by community banks. This is appropriate in our view, and not only from the stand point of safety and soundness. One of the most important roles played by reciprocal deposits is helping community banks compete for deposits with larger banks. The largest banks have a definite advantage in soliciting deposits that exceed the insurance limit because of the perception – validated during the financial crisis – that they are too-big-to-fail and that they and their depositors will be propped up by the government if they become destabilized in order to avert a broad, systemic collapse. Unfortunately, size alone is used as a proxy for safety. This is also the reason why community banks pay approximately 40 percent more for deposits than the largest banks.

The too-big-to-fail perception has led to a large and increasing concentration of deposits among the largest banks. Today, the 37 banks that exceed \$50 billion in assets control 66 percent of all domestic deposits. The concentration of deposits both contributes to and results from industry consolidation. There are approximately 2,000 fewer banks today

than there were before the financial crisis. Consolidation and concentration increases systemic risk and reduces competition in pricing and consumer choice.

Reciprocal deposits help to neutralize the megabank advantage in attracting deposits by providing a way for community banks to provide insurance coverage for their larger deposits. By so doing, reciprocal deposits stave off deposit concentration and industry consolidation. They enhance the viability of community banks and thereby strengthen the marketplace for consumers and businesses.

For all of the above reasons, ICBA and I believe there is a compelling public interest for the swift enactment of H.R. 4116 before the close of the 114<sup>th</sup> Congress.

### **H.R. 5660 & H.R. 6162**

ICBA also supports the “Retail Checking Account Protection Act of 2016” (H.R. 5660), sponsored by Representatives Roger Williams and Gwen Moore, for many of the same reasons that we support H.R. 4116. H.R. 5660 would exclude from the definition of brokered deposit deposits opened or held by retail customers of a bank. The stability of these deposits, as is true of reciprocal deposits, is due to the established relationship between the depositor and the bank.

The “Protect Prepaid Accounts Act of 2016” (H.R. 6162), sponsored by Representative Scott Tipton, would provide that prepaid funds deposited in an insured depository institution are not brokered deposits. Both H.R. 5660 and H.R. 6162 address limitations on deposits imposed by the FDIC that are inappropriate, counterproductive, and harmful to community banks and the communities they serve.

### **Closing**

Thank you again for the opportunity to testify before this Subcommittee and for raising the profile of the important bills noted above. We are very pleased with their bipartisan support and hope that they can be swiftly enacted. It’s past time to remove the unwarranted stigma attached to reciprocal deposits, any deposits held by retail customers, and prepaid accounts.