



# *FedFin Client Report*

---

Thursday, July 20, 2023

## **Senate Banking Kicks Deposit-Insurance Reform Down the Road**

**Client Report: DEPOSITINSURANCE121**

### **Executive Summary**

In the wake of today's Senate Banking deposit-insurance reform hearing, it seems certain that there will be no legislation in the near term and most likely in this Congress to increase FDIC-insurance thresholds. Although the FDIC recommended a new approach to transaction accounts in its policy review following recent bank failures ([see Client Report DEPOSITINSURANCE119](#)), Senators on both sides of the aisle demurred. Chairman Brown (D-OH) made it clear that any change in FDIC-coverage limits is conditioned on final, tougher bank regulations, essentially telling banks that successfully opposing new rules means keeping FDIC coverage as is. Ranking Member Scott (R-SC) is no fan of new rules, but he also said that review of FDIC coverage should only follow significant improvements in bank supervision likely in his view to moot the need for higher deposit protection. Sen. Scott was also emphatic that higher thresholds would need to come with higher premiums that could adversely affect bank competitiveness and credit availability. Undeterred, Sen. Vance (R-OH) has introduced legislation to end deposit-insurance coverage limits for community banks. Senators on both sides of the aisle focused instead on ensuring community-bank relief from pending special assessments ([see FSM Report DEPOSITINSURANCE120](#)) and, for Sen. Warren (D-MA), urging higher premiums for "TBTF" banks.

### **Analysis**

#### ***Opening Statements***

Chairman Brown took issue with megabank depositor flight and banking system concentration, arguing that the largest banks should bear a greater burden in any special assessment. He also boosted clawback legislation ([see FSM Report COMPENSATION37](#)) and argued for stronger capital and liquidity standards, stress tests, and supervision as preconditions for more FDIC protection. Ranking Member Scott emphasized tradeoffs to any deposit insurance reform involving expanded coverage, highlighting higher fees and reduced credit. He also suggested that any reforms to the system should consider supervisory failures as well as emerging digital run risk.

---

Federal Financial Analytics, Inc.  
2101 L Street, NW – Suite 300, Washington, D.C. 20037  
Phone (202) 589-0880  
E-mail: [info@fedfin.com](mailto:info@fedfin.com) [www.fedfin.com](http://www.fedfin.com)

© 2023. Federal Financial Analytics, Inc. All rights reserved.

## Testimony

Emily DiVito of the Roosevelt Institute laid out three deposit insurance reform options: leaving the current regime untouched, expanding coverage for certain accounts, and providing unlimited coverage. Testifying for the ICBA, Thomas Fraser of First Mutual Holding Co. urged Congress to focus on consumer protection and banking system stability, as well as accounting for unintended consequences of policy changes such as those to the “the implicit guarantee.” Andrew Olmem of Mayer Brown boosted the FDIC’s targeted approach to deposit insurance reform and argued that Congress should focus on digital run risks.

## Q&A

- **Higher Coverage Thresholds:** Chairman Brown and Ranking Member Scott asked about the benefits and detriments of expanding deposit insurance coverage for all demand deposits; Ms. DiVito said doing so would reduce the likelihood of bank runs and enhance financial stability, and that moral hazard associated with this approach could be offset by higher capital and liquidity requirements. Mr. Olmem argued that, while greater coverage could stem bank runs, higher costs and moral hazard are serious concerns. Ranking Member Scott also asked about the merits of bifurcating deposit insurance for commercial and individual accounts; Mr. Olmem said that the current deposit insurance system works well for most Americans, but said the approach could instill market discipline. Sen. Menendez (D-NJ) argued that tailoring coverage by account type must be done carefully to prevent moral hazard. He also raised concerns that increasing coverage thresholds would exacerbate large-bank deposit concentration; Ms. DiVito argued that raising coverage limits would better enable smaller banks to compete. Sen. Warren (D-MA) argued that the FDIC coverage limit should be raised and that doing so would benefit community banks by reducing incentives for depositor flight; Ms. DiVito agreed. Sen. Warren also argued that any reforms to the deposit insurance system must be accompanied by tougher oversight to prevent banks from engaging in riskier behavior.
- **Digital Run Risk:** Ranking Member Scott emphasized the dangers of digital bank runs and argued that regulatory changes must be contemplated to protect the financial system. Sen. Warner (D-VA) noted that no capital requirements can be high enough to prevent internet-driven runs.
- **Shadow Bank Migration:** Sens. Brown and Cortez Masto (D-NV) pointed to the risks arising from shadow bank deposit migration; Mr. Fraser said that, while fintechs are important to financial services innovation, they fall outside the regulatory perimeter and customers must be aware. Sen. Cortez Masto argued that consumer protection and financial stability should apply equally to banks and nonbanks.
- **Banking System Diversity:** Sen. Vance argued that maintaining a three-tiered banking system is critical. Chairman Brown as well as Sens. Menendez and Warren also emphasized the role of community banks, while Sen. Smith (D-MN) commended the FDIC for excluding small banks from its special assessment.

- **FDIC Premium Levels:** Sen. Warren argued that the biggest banks have an “implicit guarantee” and should therefore pay larger DIF premiums.
- **Private Sector Solutions:** Sen. Warner asked how existing informal exchanges between banks allowing for greater depositor protection could be strengthened; Mr. Fraser said the practice is generally safe and does not burden the system. Sen. Cortez-Masto highlighted that deposit swaps facilitated through companies like IntraFi could reduce run risk and may have even prevented SVB’s collapse, asking witnesses for their views on the appropriate role for cash dispersal; Mr. Fraser agreed the facility could be part of a private sector solution and that services like IntraFi can help with liquidity planning.
- **Discount Window:** Arguing that greater use of the Fed’s discount window would bolster liquidity and reduce run risk, Sen. Warner asked how banks could be encouraged to do so without incurring stigma; Mr. Fraser and Mr. Olmem agreed that removing stigma from Fed liquidity facilities is important.