

## Special Analysis

### Impact of “Big-Bank Tax” on all other banks

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#### Implications

- A tax on “big banks” is de facto a “tax” (higher cost) on all banks.
- There is 70 percent likelihood that all other banks will raise their deposit rates if “big banks” opt to raise capital through retail deposit in order to avoid the “big-bank tax”.
- The “big-bank tax” will indirectly “tax” smaller banks by increasing their cost of funds to stay competitive with the bigger banks.

#### Overview

In January of 2010, the administration proposed a 15-basis-point “big bank tax”, which would be levied against bank assets minus Tier 1 capital and domestic deposits. The proposal targets about 34 (See Exhibit A) of the largest commercial banks – those with \$50 billion or more in assets. The proposed “big bank tax” will be on wholesale funding, which means that this type of funding will become more expensive for the banks.

One possible way of decreasing the exposure to the “big-bank tax” is by increasing the amount of retail deposits; both brokered and direct deposits. However, in order to raise additional capital quickly, “big banks” will have to be more competitive in their deposit rates, which means higher deposit interest rates.

#### Purpose

The purpose of this analysis is to examine the impact that the “big-bank tax” will have on retail deposits rates. The impact is going to be measured in terms of the likelihood and the extent smaller banks are going to increase their deposit rates in response to more aggressive deposit pricing by the “big banks”.

#### Analysis

- We calculated the average APY of standard CDs with terms of 3, 6, 9, 12, 24, 30, 36, 48 and 60 months of the 34 “big banks” for the period of January 1, to December 31, 2009.
- We calculated the average APY of standard CDs with terms of 3, 6, 9, 12, 24, 30, 36, 48 and 60 months of banks that are smaller than the “big banks” for the period of January 1, to December 31, 2009.
- We established the average APY of the “big banks” as the independent variable, and the average APY of the smaller banks as the dependent variable.

- We conducted a time-series analysis to examine the lag time of the APY changes between the “big banks” and the smaller banks.

### **Findings**

- We found that the 70 percent of the variance in the average APY of the smaller banks can be explained by the variance in the average APY of the “big banks” (Table 1).
- We found that the linear relationship between the average APY of the “big banks” and the average APY of the smaller banks is very strong (Beta .834) and very significant (Alpha < 0.01)
- We found that smaller banks follow the rate changes of the “big banks” within a one week lag time from the rate-change occurrence (Figure 1).
- We found that smaller banks price higher than “big banks” at an average of 34 bps, and a range of 0.8 to 62 bps.

### **Discussion**

The “big-bank tax” is very likely to have unintended consequences. A tax on the wholesale funding of “big banks” will force them to raise needed capital through the retail deposit market. However, in order to raise large amounts of capital in a short time, the “big banks” will have to be more aggressive in their deposit pricing, which means higher interest rates.

This analysis shows that there is a 70 percent probability that all other banks will follow the lead of the “big banks”, and raise their deposit interest rates within one week in order to protect their market share and deposits from shifting to the “big banks”. As a result, the smaller banks, which are not being taxed directly, will incur a higher cost of funds expense, which they could have avoided if they did not have to respond to the rate increase by the “big banks”.

**Table 1**  
Linear relationship between CD average APY of “big banks” and smaller banks

#### **Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.834 <sup>a</sup>	.696	.690	.10368

a. Predictors: (Constant), Big banks CD Avg. APY

#### **ANOVA<sup>b</sup>**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	1.253	1	1.253	116.592	.000 <sup>a</sup>
	Residual	.548	51	.011		
	Total	1.802	52			

a. Predictors: (Constant), Big banks CD Avg. APY

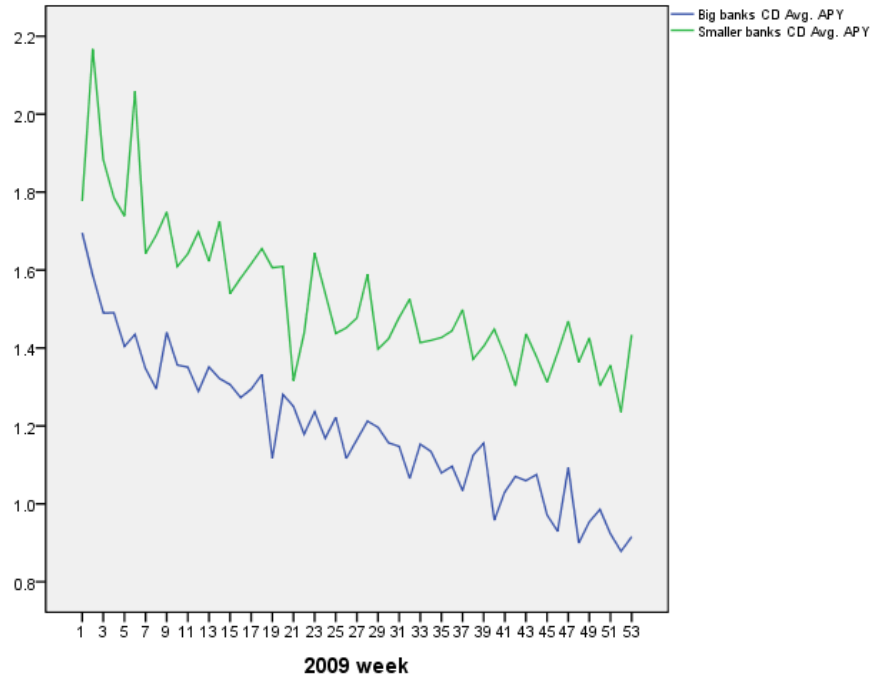
b. Dependent Variable: Smaller banks CD Avg. APY

#### **Coefficients<sup>a</sup>**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.522	.095		5.497	.000
	Big banks CD Avg. APY	.851	.079	.834	10.798	.000

a. Dependent Variable: Smaller banks CD Avg. APY

**Figure 1**  
Time-series analysis of CD APY of “Big banks” vs. smaller banks



**Exhibit A**  
List of the 34 largest commercial banks (\$50 billion and over in assets)

Institution Name	City	State	Total Assets(\$000)
JPMorgan Chase Bank, National Association	Columbus	OH	1,669,868,000
Bank of America, National Association	Charlotte	NC	1,460,147,344
Citibank, National Association	Las Vegas	NV	1,186,754,000
Wells Fargo Bank, National Association	Sioux Falls	SD	547,690,000
Wachovia Bank, National Association	Charlotte	NC	518,389,000
U.S. Bank National Association	Cincinnati	OH	259,942,982
HSBC Bank USA, National Association	Mc Lean	VA	168,262,874
The Bank of New York Mellon	New York	NY	166,539,000
SunTrust Bank	Atlanta	GA	166,171,009
State Street Bank and Trust Company	Boston	MA	160,208,203
Branch Banking and Trust Company	Winston Salem	NC	159,145,841
FIA Card Services, National Association	Wilmington	DE	153,359,090
PNC Bank, National Association	Pittsburgh	PA	146,901,593
Regions Bank	Birmingham	AL	135,594,440
Capital One, National Association	McLean	VA	126,533,761
RBS Citizens, National Association	Providence	RI	118,883,026
Goldman Sachs Bank USA	New York	NY	114,868,000
Fifth Third Bank	Cincinnati	OH	109,196,321
TD Bank, National Association	Wilmington	DE	108,026,470
Citibank (South Dakota), N.A.	Sioux Falls	SD	98,752,082
Keybank National Association	Cleveland	OH	93,760,366
ING Bank, fsb	Wilmington	DE	89,682,361
Chase Bank USA, National Association	Newark	DE	87,833,441
Union Bank, National Association	San Francisco	CA	77,732,748
Sovereign Bank	Wyomissing	PA	73,207,271
Manufacturers and Traders Trust Company	Buffalo	NY	67,807,600
Compass Bank	Birmingham	AL	67,759,513
Morgan Stanley Bank, National Association	Salt Lake City	UT	65,487,000
The Northern Trust Company	Chicago	IL	64,932,863
Bank of the West	San Francisco	CA	63,583,868
Comerica Bank	Dallas	TX	59,448,930
Hudson City Savings Bank	Paramus	NJ	58,684,560
Ally Bank	Midvale	UT	52,512,982
The Huntington National Bank	Columbus	OH	51,988,299
M&I Marshall and Ilsley Bank	Milwaukee	WI	51,571,329

Source: FDIC 12/31/2009.