



December 12, 2019

**MEMORANDUM TO:** The Board of Directors

**FROM:** Doreen R. Eberley  
Director, Division Risk Management Supervision

**SUBJECT:** Notice of Proposed Rulemaking – Brokered Deposits Restrictions

### RECOMMENDATION

Staff recommends that the FDIC Board of Directors (the Board) authorize publication of the attached notice of proposed rulemaking (NPR or proposed rule) with a 60-day comment period.

### SUMMARY

Through this NPR, the FDIC would invite comment on proposed revisions to its regulations relating to the brokered deposits restrictions that apply to less than well capitalized insured depository institutions. The proposed rule, informed by comments received pursuant to an Advance Notice of Proposed Rulemaking (ANPR) issued on December 18, 2018, would create a new framework for analyzing certain terms for purposes of the brokered deposit restrictions, including “facilitation” and “primary purpose.” The proposed rule would also establish an application process and related reporting requirements with respect to the primary purpose exception.

### BACKGROUND

#### A. Statutory and Regulatory Framework

Section 337.6 of the FDIC’s Rules and Regulations implements and closely tracks the statutory text of Section 29 of the FDI Act, particularly with respect to the definition of “deposit broker” and its exceptions.<sup>1</sup> Section 29 does not directly define a “brokered deposit,” rather, it defines a “deposit broker” for purposes of the restrictions.<sup>2</sup>

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<sup>1</sup> See 12 CFR 337.6.

<sup>2</sup> See 12 U.S.C. 1831f.

Concur:

Nicholas J. Podsiadly  
General Counsel

Section 29 and the FDIC's implementing regulation define the term "deposit broker" to include:

1. any person engaged in the business of placing deposits, or facilitating the placement of deposits, of third parties with insured depository institutions or the business of placing deposits with insured depository institutions for the purpose of selling interests in those deposits to third parties; and
2. an agent or trustee who establishes a deposit account to facilitate a business arrangement with an insured depository institution to use the proceeds of the account to fund a prearranged loan.

This definition is subject to nine statutory exceptions, all of which are also set forth in the regulations, and one additional regulatory exception previously established by the FDIC.

#### B. Issues Raised by Commenters in the ANPR

The ANPR sought comments on brokered deposits and the interest rate restrictions applicable to less than well capitalized banks. In response to the ANPR, the FDIC received more than 130 comments from individuals, banking organizations, non-profits, as well as industry and trade groups, representing banks, insurance companies, and the broader financial services industry. Of the total comments, more than 100 related to brokered deposits.

Many commenters argued that brokered deposits represent safe, stable sources of funding, particularly for smaller banks and rural banks that may have difficulty obtaining deposits through traditional channels. Commenters also expressed the view that FDIC staff interpretations have broadened the scope of the definition of "deposit broker" so that most, if not all, transactions involving a third party are considered to be brokered. Given technological innovations and changes to the way in which customers conduct their banking activities, these commenters suggested that the FDIC modernize its regulations to account for these new types of relationships and products.

Other commenters suggested that many transactions involving third parties that today are considered to be brokered should not be brokered, unless it is clear that the transaction is being effected for the purpose of increasing deposit insurance as opposed to having some alternative purpose.

While the majority of commenters sought to constrict the definition of "brokered deposit," one organization argued against reduction in scope, expressing the view that brokered deposits have already received permissive regulatory treatment.

#### **Summary of Proposed Rule**

The intent of the proposed changes would be to modernize the FDIC's brokered deposit regulations to reflect technological changes and innovations. In the NPR, the FDIC would state that it recognizes that the definition of "deposit broker," and its corresponding staff interpretations, may not be as relevant given the deposit placement arrangements that exist in the market today. Currently, banks collaborate with third parties, including financial technology companies, for a variety of business purposes including access to deposits. Moreover, banks are increasingly relying on new technologies to engage and interact with their customers, and it appears that this trend will continue given rapid technological evolution. Through these

proposed changes, the FDIC would seek to balance the need to promote safe and sound practices while ensuring that the classification of a deposit as brokered appropriately reflects changes in the banking landscape since 1989, when the law on brokered deposits was first enacted.

#### A. Deposit Broker Definition

A person meets the “deposit broker” definition under Section 29 of the FDI Act if it is “engaged in the business of placing deposits, or facilitating the placement of deposits, of third parties with insured depository institutions or the business of placing deposits with insured depository institutions for the purpose of selling interests in those deposits to third parties.” In addition, an agent or trustee meets the “deposit broker” definition when establishing a deposit account to facilitate a business arrangement with an insured depository institution to use the proceeds of the account to fund a prearranged loan.

##### 1. Engaged in the business of placing deposits

The statutory definition of “deposit broker” includes a person engaged in the business of placing deposits on behalf of a third party (i.e., a depositor) at insured depository institutions. In the NPR, the FDIC would propose to view a person to be *engaged in the business of placing deposits* if that person has a business relationship with its customers, and as part of that relationship, places deposits on behalf of the customer (e.g., acting as custodian or agent for the underlying depositor).

##### 2. Engaged in the business of facilitating the placement of deposits

The statutory definition of “deposit broker” also includes a person engaged in the business of facilitating the placement of deposits on behalf of a third party with insured depository institutions. In contrast to the first prong of the definition, the “facilitation” prong refers to activities where the person does not directly place deposits on behalf of its customers with an insured depository institution. Historically, the term “facilitating the placement of deposits” has been interpreted by staff at the FDIC to include actions taken by third parties to connect insured depository institutions with potential depositors.

The proliferation of various online marketing and advertising channels have provided new ways for insured depository institutions to attract deposits from different parts of the country. In an effort to ensure that the term brokered deposit appropriately reflects the banking landscape, and to ensure that the FDIC’s regulations promote safe and sound practices, staff recommends that the FDIC propose defining the activities that result in a person being “engaged in the business of facilitating the placement” of third party deposits at an insured depository institution.

Under the proposed rule, a person would meet the “facilitating the placement of deposits” prong of the “deposit broker” definition by, while engaged in business, engaging in any one, or more than one, of the following activities:

- The person directly or indirectly shares any third party information with the insured depository institution;
- The person has legal authority, contractual or otherwise, to close the account or move the third party’s funds to another insured depository institution;

- The person provides assistance or is involved in setting rates, fees, terms, or conditions for the deposit account; or
- The person is acting, directly or indirectly, with respect to the placement of deposits, as an intermediary between a third party that is placing deposits on behalf of a depositor and an insured depository institution, other than in a purely administrative capacity.

The proposed “facilitation” definition is intended to capture activities that indicate that the person takes an active role in the opening of an account or maintains a level of influence or control over the deposit account even after the account is open. The NPR states that it is the FDIC’s view that a level of control or influence indicates that the deposit relationship is between the depositor and the person rather than the depositor and the insured depository institution.

The proposal would define “facilitating the placement of deposits” to include acting as an intermediary between another person that is placing deposits on behalf of a depositor and an insured depository institution, other than in a purely administrative capacity. Administrative functions would include, for example, any reporting or bookkeeping assistance provided to the person placing its customer deposits with insured depository institutions. Administrative functions would not include, for example, assisting in decision-making or steering persons (including the underlying depositors) to particular insured depository institutions.

### 3. Selling Interests in Deposits to Third Parties

The third prong of the “deposit broker” definition includes a person “engaged in ... the business of placing deposits with insured depository institutions for the purpose of selling interest in those deposits to third parties.” This part of the definition specifically captures the brokered certificates of deposit (CD) market (referred to herein as “brokered CDs”). These are deposit placement arrangements where brokered CDs are issued in wholesale amounts by a bank and sold through a registered broker-dealer to investors, typically in amounts that would result in investors’ interests in those deposits being fully insured by the FDIC. The brokers subdivide the bank-issued “master CD” and alter the terms of the original CD before selling the new CDs to its brokerage customers. These brokered CDs are (in most cases) held in book-entry form at the Depository Trust Corporation (“DTC”) and use the CUSIP system for identification and trading in a primary and secondary market.

Deposits placed through this market have always been marketed and classified as brokered deposits and are specifically captured by this part of the deposit broker definition. Staff recommends not proposing any changes to the brokered classification of such deposits.

#### B. Exceptions to the Deposit Broker Definition

Section 29 provides nine statutory exceptions to the definition of deposit broker, all of which are also set forth in the regulations, and, as noted earlier, the FDIC added one additional regulatory exception. Through this rulemaking, the FDIC would propose amending two exceptions – (1) the exception for insured depository institutions, with respect to funds placed with that depository institution (the “IDI exception”) and (2) the exception for an agent or nominee whose primary purpose is not the placement of funds with depository institutions (the “primary purpose exception”).

##### 1. Bank Operating Subsidiaries and the IDI Exception

Section 29 of the FDI Act expressly excludes from the definition of “deposit broker” an insured depository institution, with respect to funds placed with that depository institution. This exception is known as the “IDI Exception.”<sup>3</sup> Under the IDI Exception, an IDI is not considered to be a deposit broker when it (or its employees) places funds at the bank.

The proposal states that the FDIC recognizes that this exception currently is limited to IDIs only, and not their subsidiaries. The IDI Exception currently applies, for example, in the case of a division of an IDI that places deposits exclusively with the parent IDI, but does not apply if a separately incorporated subsidiary of the IDI places deposits exclusively with the parent. The FDIC also recognizes that a wholly owned operating subsidiary that meets certain criteria can be considered similar to a division of an IDI for certain purposes.

There is little practical difference between deposits placed at an IDI by a division of the IDI versus deposits placed by a wholly owned subsidiary of the IDI. Therefore, staff recommends that the FDIC propose that the IDI exception be available to wholly-owned operating subsidiaries provided that such a subsidiary meets the following criteria:

- The subsidiary is a wholly owned operating subsidiary of the IDI, meaning that the IDI owns 100% of the subsidiary’s outstanding stock;
- The subsidiary places deposits of retail customers exclusively with the parent IDI; and
- The subsidiary engages only in activities permissible for the parent IDI.

## 2. Primary Purpose Exception

### a. General Overview and Background

The statute provides that the primary purpose exception applies to “an agent or nominee whose primary purpose is not the placement of funds with depository institutions.”<sup>4</sup> Generally, if a person is engaged in the business of placing or facilitating the placement of deposits for its customers at insured depository institutions, it meets the “deposit broker” definition. However, if the person meets the primary purpose exception, then the person is excepted from the definition of “deposit broker” and any deposits that it places with insured depository institutions are not brokered deposits.

### b. Proposal

Under the proposed rule, application of the primary purpose exception would be based on the business relationship between the agent or nominee and its customers. Since Section 29 was first enacted, there have been a number of different agents and nominees that have sought views on the applicability of the primary purpose exception, and this proposed amendment to the primary purpose exception would expand the number of entities that meet the exception.

### c. Business Relationships Deemed to Meet the Primary Purpose Exception Subject to the Application Process

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<sup>3</sup> 12 U.S.C. 1831f(g)(2)(A).

<sup>4</sup> 12 U.S.C. 1831f(g)(2)(I).

## 1. Deposit Placements of Less Than 25 Percent of Customer Assets Under Management by a Third Party

Through this rulemaking, the primary purpose of an agent's or nominee's business relationship with its customers would not be considered to be the placement of funds, subject to an application process, if less than 25 percent of the total assets that the agent or nominee has under management for its customers, in a particular business line, is placed at insured depository institutions. The NPR proposes that if 75 percent or more of customer assets under management by the third party is not being placed at depository institutions, for a particular business line, the third party has demonstrated that the primary purpose of that business line is not the placement of funds at depository institutions. An agent or nominee that seeks to avail itself of the primary purpose exception based on this standard would be required to submit an application, as discussed below.

In determining the amount of customer assets under management by an agent or nominee, for a particular business line, the FDIC would measure the total market value of all the financial assets (including cash balances) that the agent or nominee manages on behalf of its customers that participate in a particular business line.

The NPR would state that the FDIC believes that establishing a transparent, bright-line test would be beneficial for all parties.

## 2. Deposit Placements that Enable Transactions

Subject to an application process, the primary purpose of an agent's or nominee's business relationship with its customers would not be considered to be the placement of funds if the agent or nominee places depositors' funds into transactional accounts for the purpose of enabling payments. Under the proposal, if an agent or nominee places 100 percent of its customer funds into transaction accounts at depository institutions and no fees, interest, or other remuneration is provided to the depositor, then it would meet the primary purpose exception of enabling payments, subject to providing information as part of an application process. In such a case, staff recommends that the FDIC conclude that the primary purpose of the agent's or nominee's business is to enable payments, and not for the placement of deposits.

If the agent or nominee, or the depository institution, pays any sort of interest or fee, or provides any remuneration, (e.g., nominal interest paid to the deposit account), then the FDIC would more closely scrutinize the agent's or nominee's business to determine whether the primary purpose is truly to enable payments. In such a case, the FDIC would consider a number of factors, including the volume of transactions in customer accounts, and the interest, fees, or other remuneration provided, in determining the applicability of the primary purpose exception.

An agent or nominee that seeks to avail itself of the primary purpose exception on this basis would be required to submit an application.

### d. Other Business Relationships That May Meet the Primary Purpose Exception

In the NPR, the FDIC would propose that agents or nominees that do not fit within the business arrangements detailed above also be eligible for the primary purpose exception, subject to an

application process. The FDIC would consider a number of factors in determining whether the primary purpose of the agent's or nominee's business relationship with its customers is not the placement of funds with insured depository institutions. For example, one factor the FDIC would review is the revenue structure for the agent or nominee. Another factor that the FDIC would consider would be whether the agent's or nominee's marketing activities to prospective depositors are aimed at opening a deposit account or to provide some other service, and if there is some other service, whether the opening of the deposit account is incidental to that other service.

Persons that meet the deposit broker definition because they are "facilitating the placement" of deposits would also be eligible for the primary purpose exception under this basis.

Ultimately, the FDIC's review of whether an agent or nominee meets the primary purpose exception would be a case-by-case review and depend upon a consideration of factors as detailed in the NPR, as well as the information presented by the applicant as to why it should meet the primary purpose exception.

#### e. Business Relationships That Do Not Meet the Primary Purpose Exception

Staff recommends that the FDIC not grant a primary purpose exception for a person's placement of brokered CDs for the reasons set forth previously. For purposes of establishing the person's primary purpose, the person's placement of brokered CDs would be considered a discrete and independent business line from other deposit placement businesses, and so the primary purpose for that particular business line would always be the placement of deposits at depository institutions. Additionally, the primary purpose exception would not apply where a third party's primary purpose for its business relationship with its customers is to place (or assist in the placement of) funds into deposit accounts to "encourage savings," "maximize yield," or "provide deposit insurance" or any similar purpose.

#### f. Applicability of Prior FDIC Staff Advisory Opinions

In the NPR, the FDIC would recognize that some insured depository institutions may have met the primary purpose exception based on a previous FDIC staff advisory opinion. The NPR states that, as part of this rulemaking process, the FDIC intends to evaluate existing staff opinions to identify those that are no longer relevant or applicable based on any revisions made to the brokered deposit regulations. The FDIC plans, as part of any final rule, to codify staff opinions of general applicability that continue to be relevant, and to rescind any staff opinions that are superseded or obsolete.

#### g. Evaluation of Business Lines

In evaluating whether the primary purpose applies, staff recommends that the FDIC analyze specific business lines. Otherwise, any agent or nominee engaged in the brokering of deposits could evade the statutory restrictions by adding or combining its brokering business with other businesses such that the deposit broker business is no longer its primary purpose. In the proposal, the term business line would refer to the business relationships an agent or nominee has with a group of customers for whom the business places or facilitates the placement of deposits.

## h. Application Process for the Primary Purpose Exception

### 1. General Overview of the Application Process

Under the proposal, the FDIC would establish an application process, through Part 303 of the FDIC Rules and Regulations, under which any agent or nominee that seeks to avail itself of the primary purpose exception, or an insured depository institution acting on behalf of an agent or nominee, could request that the FDIC consider certain deposits as nonbrokered as a result of the primary purpose exception. If an application from the agent or nominee is approved, deposits placed or facilitated by that party would be considered nonbrokered. While an IDI may apply on behalf of a third party, the FDIC anticipates that agents or nominees are likely to apply on their own behalf, given that much of the information required for an application would be in possession of the agent or nominee (and not the IDI).

Applicants would receive a written determination from the FDIC within 120 days of receipt of a complete application. The FDIC intends to provide expedited processing for certain simple and straightforward applications.

### 2. Application Contents

An applicant would need to submit certain information, depending on the basis on which the primary purpose exception is being sought. For example, applicants that seek the primary purpose exception based on enabling transactions would need to provide, among other things, the contracts with customers and with the depository institutions in which the third party is placing deposits showing that all of its customer deposits are in transaction accounts. The applicant would also need to submit information on the amount of interest, fees, or remuneration being provided or paid for the transaction accounts.

As another example, third parties that place more than 25 percent of total assets under management for their customers, for a particular business line, into deposit accounts at insured depository institutions, would have to include, among other things, a description of the deposit placement arrangement between all entities involved.

The FDIC would be permitted to request additional information at any time during the review of an application to render the application complete and initiate its review.

### 3. Ongoing Reporting and Monitoring

The FDIC will describe reporting requirements as part of its written approval for a primary purpose exception. Agents or nominees that meet the primary purpose exception, or an IDI that applies on behalf of the agent or nominee, would need to provide reports to the FDIC, and if applicable, in the case of IDIs, to its primary federal regulator. IDIs would also be responsible for monitoring nonbank third parties' eligibility for the primary purpose exception. When establishing a contractual relationship with a nonbank third party for the placement of deposits that may be classified as nonbrokered due to the primary purpose exception, an IDI may wish to consider the reporting and monitoring requirements described here.

#### 4. Modification and Withdrawals

The NPR indicates that at any time after approval, the FDIC may, with notice and as appropriate, require additional information to ensure that the approval is still appropriate, or to verify the accuracy of the information that was provided by a third party to an IDI or submitted to the FDIC. In addition, the FDIC would be able to require that the applicant reapply for approval, or impose additional conditions on the approval. Finally, the FDIC would have the ability to withdraw a previously granted approval.

##### C. Brokered Deposits and Assessments

The proposed interpretations of the brokered deposit definition and its exceptions would result in some deposits currently reported as brokered deposits no longer being so reported. The proposed rule notes that, in a future rulemaking, the FDIC plans to consider modifications to the assessment rule in light of any changes made to the brokered deposit regulation.

##### D. Reporting of Certain Deposits on Call Reports

The NPR states that, after a final rule is adopted, the FDIC will consider requiring reporting of deposits that are excluded from being reported as brokered deposits because of the application of the primary purpose exception. The FDIC will monitor this information to assess the risk factors associated with the deposits and determine assessment implications, if any.

##### E. Treatment of Non-Maturity Deposits for Purposes of the Brokered Deposits Restrictions

Through the proposal, the FDIC is considering an interpretation under which non-maturity brokered deposits would be viewed as “accepted” for the brokered deposits restrictions at the time any new non-maturity deposits are placed at an institution by or through a deposit broker.

##### F. Additional Supervisory Matters

Under this proposal, numerous categories of deposits that are currently considered brokered would instead be nonbrokered. The FDIC will continue to take such supervisory efforts as may be necessary to ensure that banks are operating in a safe and sound manner. Nothing in this proposal is intended to limit the FDIC’s ability to review or take supervisory action with respect to funding-related matters, including funding concentrations, that may affect the safety and soundness of individual banks or the industry generally.

##### G. Alternatives

The NPR states that the FDIC considered a number of alternative approaches, including taking more incremental approaches through which more limited changes would be made. However, the FDIC ultimately determined that the best course of action was to take a fresh, holistic look at the regulations and interpretations, and propose a new framework that reflects technological and other changes in the banking industry over the past three decades and is consistent with the law.

## REQUEST FOR COMMENTS

The FDIC would seek comment on all aspects of the rule and in response to a series of specific questions.

## CONCLUSION

The proposed rule is intended to modernize FDIC's brokered deposit regulations in a manner that reflects technological innovation in the banking industry. FDIC staff recommends that the Board approve the NPR for publication in the Federal Register.

### Staff contacts:

#### *Legal Division*

Vivek Khare, Counsel, (202) 898-6847

Kate Marks, Counsel, (202) 898-3896

#### *RMS*

Rae-Ann Miller, Associate Director, (202) 898-3898