

November 10, 2016

TO: Board of Directors

FROM: Bret D. Edwards 
Director
Division of Resolutions and Receiverships

Charles Yi 
General Counsel

SUBJECT: Final Rule: Recordkeeping for Timely Deposit Insurance Determination

RECOMMENDATION

Staff recommends that the Board adopt, and approve for publication in the *Federal Register*, a final rule regarding recordkeeping by insured depository institutions (“IDIs”) with a large number of deposit accounts in order to facilitate a timely deposit insurance determination in the event of failure (“Final Rule”). The Final Rule requires any IDI with two million or more deposit accounts (“covered institution”) to configure its information technology system (“IT system”) to be capable of calculating, within 24 hours after failure, the deposit insurance available to each owner of funds on deposit in accordance with the deposit insurance rules set forth in 12 CFR part 330. The Final Rule also prescribes recordkeeping requirements that are needed for prompt deposit insurance determination by the FDIC using a covered institution’s IT system while also recognizing the existing recordkeeping requirements set forth in the FDIC’s deposit insurance rules.

DISCUSSION

1. Background

The Federal Deposit Insurance Act (“FDI Act”) instructs the FDIC to pay deposit

insurance “as soon as possible” following the failure of an IDI.¹ Prompt payment of deposit insurance not only maintains public confidence in the banking system but also preserves franchise value, thus decreasing cost to the Deposit Insurance Fund.

Deposit insurance coverage is based on the ownership rights and capacities in which deposit accounts are maintained at IDIs. The FDIC relies on an IDI’s deposit account records to determine deposit ownership. The FDIC’s deposit insurance rules provide, however, that if the deposit account records disclose the existence of a relationship which might provide a basis for additional insurance (i.e., for accounts held by a trustee, agent, nominee, guardian, executor or custodian), the details of the relationship and ownership interests may be ascertained either from the IDI’s records or from records maintained by the depositor or by some person or entity that has undertaken to maintain these records for the depositor.² In a typical IDI failure, the FDIC can pay deposit insurance by the next business day when the IDI’s deposit account records contain sufficient information regarding ownership rights and capacities. With respect to deposit accounts for which records have been maintained by the depositor or the depositor’s designee, the FDIC will pay deposit insurance as promptly as possible when these records are provided to the FDIC.

Because the failure of a very large IDI, as measured by number of deposit accounts, has the potential for serious adverse effects, such as a substantial volume of returned items, the prompt payment of deposit insurance could be critical in such a case. Yet, some of the largest IDIs have millions of deposit accounts, presenting the problem of scalability in processing so many accounts for deposit insurance determinations. In addition, the continued growth in the number of deposit accounts at larger banks and the number and complexity of deposit systems or

¹ 12 U.S.C. § 1821(f)(1).

² See 12 CFR § 330.5(b)(2).

platforms in many of these banks would likely exacerbate the difficulty of making deposit insurance determinations promptly. Staff concluded that requiring large banks with millions of deposit accounts to configure their IT systems and to maintain sufficient deposit account information to facilitate the FDIC's deposit insurance determination process was the best approach to address the problem.

On April 28, 2015, the FDIC published in the *Federal Register* an Advance Notice of Proposed Rulemaking ("ANPR") seeking comment on whether IDIs that have a large number of deposit accounts should be required to develop the capability to calculate the insured and uninsured amounts for each depositor at the end of any business day and to maintain more accurate and complete data on each depositor's ownership interest by right and capacity. After considering comments received on the ANPR, the FDIC published in the *Federal Register* on February 26, 2016, a Notice of Proposed Rulemaking ("NPR") seeking comment on a proposal to require IDIs with two million or more deposit accounts within two years to configure their IT systems to be capable of calculating deposit insurance coverage within 24 hours after failure, and to collect and maintain all necessary data to perform this calculation for all deposit accounts ("Proposed Rule"). The Proposed Rule would have required covered institutions to collect and maintain ownership right and capacity information with respect to all deposit accounts, notwithstanding the existing recordkeeping described in the FDIC's deposit insurance rules, which in some instances recognizes that ownership right and capacity information may be kept in records maintained by the depositor or the depositor's designee.

2. *Comments on the Proposed Rule*

The FDIC received ten substantive comments on the Proposed Rule, submitted by banks, industry and professional associations, and private firms. FDIC staff also had meetings or

conference calls with insured depository institutions and industry representatives related to the comments received. In general, the comments: questioned whether any rulemaking was needed, including questioning the likelihood that any of the covered institutions would fail; identified perceived deficiencies in the FDIC's analysis of the costs and benefits of the proposal; offered obstacles to compliance with the proposal and suggested alternative approaches or revisions to make the proposal more workable; and indicated possible adverse effects of the proposal.

More specifically, some commenters asserted that the Proposed Rule was unnecessary because covered institutions are unlikely to fail and if one does, then the FDIC is likely to arrange for the payment of all deposits in full. In response, staff believes that the recent financial crisis demonstrated that large IDIs, which are more dependent on credit-sensitive funding, can fail and are more likely to suffer a rapid, liquidity-induced failure. While a number of post-crisis reforms have resulted in a more resilient banking system with the expectation of fewer failures, these reforms have not been tested in a crisis. In addition, the FDIC may be less likely to find a purchaser for a very large IDI, jeopardizing the ability to arrange the full payment of all deposits. By facilitating prompt payment of insured deposits at any large bank, the Final Rule should enable the FDIC to meet the least-cost test and to avoid invoking the systemic risk exception.

Commenters also asserted that the FDIC should upgrade its own IT system to handle deposit insurance determinations. This would still require a protracted process of transmission and processing of massive amounts of deposit data from the institution to the FDIC's IT system, which would exacerbate the risk of delayed payment of deposit insurance. On the other hand, requiring a covered institution to configure its IT system to calculate deposit insurance should obviate this problem.

Commenters also asserted that the FDIC did not appropriately balance the benefits and costs of the Proposed Rule. After reviewing its assumptions and the most recent information available, staff has concluded that its analysis of the rule's costs and benefits is appropriate and defensible.

In describing obstacles to compliance with the proposal, commenters stated that the outreach to depositors and recordkeepers that would be required to obtain information about ownership rights and capacities for certain deposit accounts would be expensive, take an inordinate amount of time, and cause disruption and confusion. Commenters also described instances in which fiduciaries may be legally prohibited by privacy and confidentiality concerns from disclosing the necessary information prior to an actual failure. Commenters therefore recommended certain changes to make this aspect of the proposal more workable. The foremost recommendation was that an exception from the information collection requirements be made for several classes of deposit accounts (such as deposits involving trusts and other fiduciary relationships and brokered CD and sweep accounts) where it would not be feasible, practical, or possible to collect the information needed for deposit insurance determination. Staff has revised the Final Rule to address these commenters' concerns.

Under the Final Rule, covered institutions should be able to satisfy the rule's general recordkeeping requirements of assigning one or more unique identifiers and the appropriate ownership right and capacity codes with respect to certain deposit accounts for which the institution is already required to have the necessary information in its deposit account records. Where the FDIC's deposit insurance rules in part 330 recognize that ownership information may be found outside the IDI in records maintained by the depositor or the depositor's designee, the covered institution may satisfy alternative recordkeeping requirements by assigning a unique

identifier to the account holder only and using a “pending” code when ownership right and capacity information is not maintained at the IDI. This alternative recordkeeping is consistent with the recordkeeping rules set forth in part 330. The Final Rule’s bifurcated recordkeeping arrangement is intended to eliminate the need for covered institutions to reach out to depositors and recordkeepers to collect and maintain ownership information for deposit accounts for which the information is kept in records maintained by the depositor or the depositor’s designee. This approach will eliminate the need for the rule to make exceptions from the general recordkeeping requirements for certain classes of deposit accounts and should provide a satisfactory alternative to the commenters’ recommendation for class exceptions.

Among the adverse effects predicted for the Proposed Rule was the possibility that community banks that participate in deposit placement networks would be disadvantaged by any requirement that they provide confidential information about their depository customers to competing banks. Staff believes that the bifurcated recordkeeping arrangement discussed above, which recognizes the existing deposit insurance rules on recordkeeping, will protect community banks from having to disclose this information.

Anticipating that covered institutions would have to collect and maintain comprehensive information collection for all deposit accounts, commenters believed that covered institutions would need at least four years, with possible extensions, to implement the IT and recordkeeping requirements of the Proposed Rule.

3. The Final Rule

The Final Rule differs from the Proposed Rule in the following significant respects:

- The Final Rule provides for a three-year compliance period instead of the two-year compliance period set forth in the Proposed Rule. In light of the modifications made in

the Final Rule with respect to recordkeeping, staff believes that a three-year time frame for compliance is feasible.

- As discussed, unlike the Proposed Rule's requirement that a covered institution collect and maintain ownership right and capacity information for all of its deposit accounts, the Final Rule requires that covered institutions implement the general recordkeeping requirements only with respect to deposit accounts for which the institution should already have the necessary information in light of current statutory and regulatory recordkeeping requirements for IDIs. A covered institution may implement alternative recordkeeping requirements with respect to deposit accounts for which the necessary information resides outside the covered institution in records maintained by the depositor or the depositor's designee, as provided in 12 C.F.R. Part 330.
- To address the potential problem of a large volume of returned items, the Final Rule provides that, for accounts with deposits insured on a "pass-through" basis, if such accounts have transactional features, a covered institution must certify that all information regarding beneficial owners that is necessary to calculate deposit insurance coverage will be submitted to the FDIC in time for the deposit insurance calculation to be performed within 24 hours after the appointment of the FDIC as receiver. Consistent with the stated purpose of this rulemaking, this requirement should ensure the prompt payment of deposit insurance for the owners of these deposits and avoid the ripple effects that could result if transactions involving funds from these deposit accounts were not processed in a timely manner, including a loss of public confidence. The Final Rule provides, however, that this certification requirement does not apply with respect to mortgage servicing accounts, lawyers trust accounts, real estate trust accounts, or

accounts held by employee benefit plans. Staff understands from the comments received on the Proposed Rule that there is a less urgent need for access to insured deposits in these types of accounts than in other deposit accounts with transactional features.

- The Proposed Rule’s exception provision, which set forth certain criteria for obtaining an exception from the recordkeeping requirements, has been replaced in the Final Rule by a procedure whereby a covered institution may submit a request for an exception from any of the requirements imposed by the rule if circumstances exist that would make it impracticable or overly burdensome to meet the requirement(s). In addition, the Proposed Rule would have required a covered institution that had been granted an exception from the recordkeeping requirements for a particular deposit account to advise its customer that, in the event of failure, the payment of deposit insurance might be delayed. That requirement has been deleted in the Final Rule.

The Final Rule, which is described in further detail in the attached “Final Rule” document for publication in the *Federal Register*, will apply to any IDI that has two million or more deposit accounts. Because the FDIC anticipates using a failed covered institution’s IT system to calculate deposit insurance coverage, each covered institution is required to configure its IT system to be capable of accurately calculating the deposit insurance available for each deposit account in accordance with the FDIC’s deposit insurance rules set forth in 12 CFR Part 330 should the covered institution fail. The IT system must be able to perform the deposit insurance calculation and adjust account balances within 24 hours after the appointment of the FDIC as receiver or, for certain accounts, after the FDIC has received additional information.

The Final Rule imposes certain recordkeeping requirements on covered institutions that would be necessary for accurate calculation of deposit insurance coverage. Generally, a covered

institution must assign and maintain in its deposit account records for each deposit account a unique identifier for each account holder, beneficial owner of the deposit (if the account holder is not the beneficial owner), and grantor and beneficiary (if the deposit account is held in connection with a trust), as appropriate. It must also maintain in its deposit account records for each deposit account the applicable ownership right and capacity code. A covered institution should, in the normal course of business, already maintain in its deposit account records, or among other records that it maintains and to which it has access, the information necessary to do this for: single ownership accounts; joint ownership accounts; accounts held by a corporation, partnership, or unincorporated association; informal revocable trust (i.e., “payable-on-death” or “in-trust-for”) accounts; and any account held in connection with an irrevocable trust for which the covered institution itself is the trustee.

The Final Rule recognizes, however, that under the FDIC’s deposit insurance rules, the amount of deposit insurance available may depend on information concerning certain deposit relationships that an IDI does not maintain in its deposit account records and to which it does not have access. When an IDI fails, the account holder must provide this information to the FDIC so that the FDIC can determine the full amount of deposit insurance available. Under the Final Rule, a covered institution does not need to meet the general recordkeeping requirements described above, but may instead meet alternative recordkeeping requirements with respect to certain types of deposit accounts if the information needed to determine the full amount of deposit insurance coverage is held in records maintained by the account holder or by a third party that has undertaken to maintain such records for the account holder. The alternative recordkeeping requirements provide that a covered institution maintain in its deposit account records a unique identifier for the account holder only and assign a “pending” code instead of the

applicable ownership right and capacity code. This provision will apply to deposits placed at covered institutions by community banks, protecting these banks from being forced to share information about their depositors with competitors. For trust accounts, the covered institution must assign a unique identifier to the account holder and, if the account has transactional features, also to the grantor (if not the account holder). The institution will also assign a “pending” code for formal trust accounts when it is not able to assign the applicable right and capacity code. With respect to “official items,” such as a cashier’s check, certified check, or personal money order, a covered institution will need to maintain the necessary information to complete an insurance determination in its deposit account records; if the information is not available, the covered institution will need to complete the pending file.

As a backstop to these changes in the Final rule and to ensure adequate awareness of an institution’s reliance on alternative recordkeeping, including for any potential future contingency plan, a covered institution will need to submit an annual report to the FDIC setting forth the number and dollar amount of those deposit accounts for which the information necessary for the deposit insurance calculation is not maintained at the covered institution.

The Final Rule provides that with respect to accounts with deposits that are insured on a “pass-through” basis if such accounts have transactional features, a covered institution must certify that all information regarding beneficial owners that is necessary to calculate deposit insurance coverage will be submitted to the FDIC in time for the deposit insurance calculation to be performed within 24 hours after the appointment of the FDIC as receiver, ensuring the prompt payment of deposit insurance. This requirement encompasses savings deposits with withdrawal features, such as money market deposit accounts (MMDAs), and pre-paid cards entitled to

deposit insurance coverage. A covered institution that is unable to provide this certification must apply to the FDIC for relief from the certification requirement through the exception process.

A covered institution must comply with the Final Rule no later than three years after the effective date of the Final Rule or the date on which the institution becomes a covered institution by reaching the two million deposit account threshold (which date is defined as the “compliance date”). If a covered institution will be unable to meet the Final Rule’s requirements within that three-year timeframe, then it may submit a request to the FDIC for an extension of the compliance date. The FDIC may also accelerate the implementation time frame under certain circumstances, including composite rating downgrade, undercapitalization or liquidity stress, and on a case-by-case basis.

A covered institution may submit a request to the FDIC for an exception from any of the Final Rule’s requirements if it demonstrates that circumstances exist that would make compliance impracticable or overly burdensome. A covered institution may request an exemption from Part 370 if all of its deposits are currently fully insured and its explicit strategy is to accept only deposits that would be fully insured. A covered institution may also request release from the Final Rule when it no longer meets the definition of a covered institution. The FDIC’s grant of any request may be conditional or time limited.

Covered institutions must submit to the FDIC an annual certification, along with the deposit insurance coverage summary report, to demonstrate that they have tested their IT system for compliance with the Final Rule’s requirements and that the IT system would be capable of accurately calculating deposit insurance coverage upon failure. The FDIC will conduct periodic tests of covered institutions’ compliance with Part 370 on a three-year cycle beginning after the compliance date.

CONCLUSION

Staff recommends that the Board of Directors approve the Final Rule and authorize its publication in the Federal Register.

Staff Contacts

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ATTACHMENTS

A – Resolution

B – Final Rule for Publication in the *Federal Register*