SECTION 337.6 BROKERED DEPOSIT RESTRICTIONS AND DEPOSIT RATE LIMITS
Questions and Answers (Last Updated November 1, 2011)

As of November 1, 2011, institutions that have received a high-rate determination from the FDIC will no longer be required to submit an annual high-rate determination request. The FDIC will continue to monitor the institution's market area and notify the institution if it is no longer operating in a high-rate area.

Restrictions Under Section 337.6

What does Section 337.6 restrict?

Section 337.6 of the FDIC's regulations (12 C.F.R. § 337.6) restricts the acceptance of brokered deposits by less than well-capitalized insured depository institutions. Also, section 337.6 restricts the interest rates that may be offered on deposits by such institutions. Recently, the FDIC amended the interest-rate restrictions. *See* 74 Fed. Reg. 27679 (June 11, 2009).

How does Section 337.6 restrict the acceptance of brokered deposits?

Under Section 337.6, insured depository institutions that are adequately capitalized must seek a waiver from the FDIC to continue to accept, renew, or roll over brokered deposits. Institutions that are undercapitalized are not allowed to accept, renew, or roll over any brokered deposits.

How does Section 337.6 restrict interest rates on deposits?

As amended, Section 337.6 generally provides that a less than well-capitalized insured depository institution may offer the "national rate" plus 75 basis points. If a depository institution believes that the "national rate" does not correspond to the actual prevailing rate in the applicable market, the institution may seek a determination from the FDIC that the institution is operating in a "high-rate area." If the FDIC makes such a determination, the bank will be allowed to offer the actual prevailing rate plus 75 basis points. In any event, for deposits accepted outside the applicable market area, the bank will not be allowed to offer rates in excess of the "national rate" plus 75 basis points.

What is the "national rate?"

The "national rate" is defined as "a simple average of rates paid by all insured depository institutions and branches for which data are available." On a weekly basis, the "national rate" is posted on the FDIC's website. This rate represents the "annual percentage yield" or "APY."

How does a bank seek a determination that it is operating in a high-rate area?

The procedures for seeking such a determination are set forth in FIL-69-2009 (December 4, 2009). As explained in the FIL, an insured depository institution can request the determination by sending a letter to the applicable FDIC regional office. The institution should specify its market area(s). After receiving the letter, the FDIC will make a determination as to whether the bank's market area is a high-rate area. The determination will be effective until the FDIC notifies the institution that it is no longer operating in a high rate area.

Are well-capitalized banks subject to the interest-rate limitations?

Well-capitalized banks are not subject to the Section 337.6 interest-rate limitations. Please note, however, that a bank is not "well capitalized" if it is subject to any written agreement, order, capital directive or prompt corrective action directive requiring the bank to maintain a specific capital level. *See* 12 C.F.R. § 325.103(b)(1)(iv). This rule does not apply to a board resolution or memorandum of understanding (MOU).

Why did the FDIC revise Section 337.6?

The revisions bring the restrictions in line with the regulation's intent and simplify the process for determining conformance. In addition, the low yields on U.S. Treasury securities compressed the national rate caps computed under the FDIC's regulation. Therefore, the national rates fell well short of the national average rates paid on certificates of deposit by depository institutions. Given the increasing prevalence of Internet deposits and Internet advertising of deposit rates, the final rule also addresses the considerable practical difficulties in ascertaining the origin of the deposit and calculating the prevailing rates paid within that area.

<u>High-rate Area Determinations</u>

How will the FDIC determine if the institution is operating in a high-rate area?

As explained in FIL-69-2009 (December 4, 2009), the FDIC will use standardized data (average rates by state, metropolitan statistical area, and micropolitan statistical area) for the market area in which the bank is operating to determine if the institution is operating in a high-rate area. In making this determination, the FDIC will review the following non-jumbo (less than $100,000) deposit product types: (1) money market deposit accounts; (2) 12-month CDs; (3) 24-month CDs; and (4) 36-month CDs. If the standardized average rates in the bank's market area exceed the national average rates by at least 10 percent, for at least three of the four deposit product types, the FDIC will find that the bank is operating in a high-rate area.

Examples

The table below provides three examples using average deposit rates for the state of Washington, the Athens-Clarke County Metropolitan Statistical Area (MSA),[1] and the Maryville, Missouri, Micropolitan Statistical Area (Micro SA).[2] In the example, the

[1] A metropolitan statistical area has at least one urbanized area of at least 50,000 individuals, plus adjacent territory with a high degree of social and economic integration with the core as measured by commuting ties. As of July 2008, 83.6 percent of the population lives in 366 metropolitan statistical areas.
[2] A micropolitan statistical area has at least one urban cluster of at least 10,000 individuals but a population of less than 50,000, plus adjacent territory with a high degree of social and economic integration with the

Athens-Clarke County MSA was deemed to be a high-rate area because at least three of the four deposit products reviewed exceeded the national rate by at least 10 percent. The other two areas reviewed—the state of Washington and the Maryville, Missouri, Micro SA—were not deemed to be high-rate areas because at least three deposit products did not exceed the national rate by at least 10 percent. Since rates are subject to change, the example provided is only applicable for the week the rate averages were generated.

	MMDA	12 Month CD	24 Month CD	36 Month CD	High-rate Area?
National Rate Times 1.10	.41	1.10	1.60	1.90	NA
Washington State	0.40	0.94	1.55	2.02	No. Only 1 one of 4 products exceeds the national average by at least 10%.
Athens-Clarke County Georgia MSA	0.63	1.36	1.81	2.14	Yes. All 4 products exceed the national average by at least 10%.
Maryville Missouri Micro SA	0.60	1.22	1.46	1.89	No. Only 2 of the 4 products exceed the national average by at least 10%.

In determining whether a particular area is a high-rate area, how will the FDIC calculate average rates in that area? In averaging rates, will the FDIC use the rates offered by all branches?

The FDIC will calculate average rates in a particular market area in accordance with the FDIC's definition of "market." In Section 337.6, the term "market" is defined as "any readily defined geographical area in which the rates offered by one insured depository institution soliciting deposits in that area may affect the rates offered by other insured depository institutions operating in the same area." 12 C.F.R. § 337.6(e). Evidence of the average rates or effective yields in a particular market area may include (but is not limited to) the following: (1) evidence as to the rates paid by other insured depository institutions in that market area; (2) evidence as to the rates paid by credit unions in that market area if the FDIC determines that the insured depository institution in question competes directly with the credit unions; and (3) evidence as to the different rates paid on different deposit products in that market area (though the FDIC will not be obligated to recognize all alleged distinctions among various deposit products as explained in greater detail below).

The FDIC recognizes that in the current environment, the spread between the funding costs for community banks and larger banks has widened in a way that reflects a variety of factors, including market perceptions about the likelihood of government support for institutions of various sizes. The materiality of this issue will vary across different geographic areas. Accordingly, in calculating prevailing local interest rates and comparing these to the national rate for the purpose of identifying high cost areas, the

core as measured by commuting ties. As of July 2008, 10 percent of the population lives in 574 micropolitan statistical areas.

FDIC will, when appropriate, exclude the rates offered by multiple branches of the same bank.

Example

The prevailing rate in a market area generally is the average of rates offered by other FDIC insured-depository institutions and branches in the geographic market area in which the deposits are being solicited. In some cases, however, the FDIC may exclude branches in determining whether a bank is operating in a high-rate area (as discussed above). In any event, assuming the bank is operating in a high-rate area, the bank will be allowed to offer the prevailing local rate plus 75 basis points. The prevailing or average local rate will be based on one rate per institution for each product based on size (for example, a one year certificate of deposit less than $100,000) or one rate per institution and branch for each product based on deposit size. The methodology should be consistent across product types, and institutions should not use an all branch approach for some competitors and an entity only approach for other competitors.

Example for "one rate per institution" calculation

A bank is located in City A, Anytown, AnyState. In this area, there are two banks with multiple branches that offer three types of interest checking accounts. The rates are the same at each branch. Under the "one rate per institution" calculation, the bank can calculate the local market average using one rate per entity for each product offered rather than listing the three types of checking accounts for each branch located in the designated market area.

Banks in the Local Market	Rates Offered in the Local Market for Interest Checking
Bank A (subject bank)	
Regular Checking	0.25%
Rewards Checking	2.50%
Bank B – with five branches	
Relationship Checking	0.30%
Premium Checking	3.00%
Bank C – with ten branches	
Regular Checking	0.15%
Premium Checking	1.75%

Average Using All Banks and All Branches

= [(Bank B's relationship rate x 5) + (Bank B's premium rate x 5)+ (Bank C's regular rate x 10) + (Bank C's premium rate x 10)]/30
= (0.30*5) + (3.00*5) + (0.15*10) + (1.75*10)/30 = 1.18

Average Using One Bank per product

= (Bank B relationship rate + Bank B premium rate + Bank C regular rate + Bank C premium rate)/4
= (0.30 + 3.00 + 0.15 + 1.75)/4 = 1.30

In this case, the local market rate cap would be 2.05% using the one bank methodology (0.75 + 1.30). Bank A's rewards checking rate exceeds the calculated rate cap while the regular checking rate does not.

Can an institution that has received a high-rate area determination use the national rate cap when it exceeds the local market rate cap? For example, the national rate cap (national rate plus 75 basis points) for a 1-year, non-jumbo certificate of deposit is 1.63 but the rate cap for the bank's local market (prevailing rate plus 75 basis points) is 1.60.

Yes. When an institution has received a determination that it is operating in a high-rate area, it can use the higher of the local market rate cap or the national rate cap when determining conformance with the interest rate restrictions. Examiners should be able to determine that the rate cap used by the institution conforms to the interest rate restrictions. Regardless of the determination, the national rate cap must be used for all non-local deposits.

Can a market area consist of a subset of banks with similar characteristics, such as asset size or a retail focus?

No. The market area must be a geographic area and include all FDIC-insured competitors.

If the FDIC determines that a bank is operating in a high-rate area, will the bank be allowed to use the local rates until notified otherwise by the FDIC?

Yes. FDIC personnel will monitor market rates for those institutions that receive determinations that their market areas are high-rate areas. If the FDIC determines that the institution is no longer operating in a high-rate area, the regional office will provide written notice to the institution.

If the FDIC makes a determination that a particular bank is operating in a high-rate area, will every bank in that market area be allowed to use the local rates? Or must each bank seek the FDIC's prior approval?

Each insured depository institution must receive a high-rate determination letter from the applicable FDIC regional office before it can use the local rates.

How soon will the FDIC respond to banks that seek determinations that they are operating in high-rate areas?

Requests are expected to be processed within 30 days of receipt of the institution's letter.

How will rates offered on the Internet be factored into the calculation of market rates?

The national rate should be used to determine conformance with the regulation for rates on deposits accepted from depositors outside the local market. If a determination has been made that the institution is operating in a high-rate area, the local market approach will be used for local deposits, including those accepted over the Internet.

How will the FDIC deal with “promotional rates” and “CD specials?”

Special rates will not be used by the FDIC in calculating average or prevailing rates. Rather, the FDIC will use standardized rate data to determine if an institution is operating in a high-rate area. If the FDIC determines that the institution is operating in a high-rate area, the institution will be allowed to offer the prevailing local rate plus 75 basis points. Otherwise, the institution must offer rates that do not exceed the national rate plus 75 basis points.

What about deposits with special features?

In calculating average or prevailing rates, the FDIC will not segregate deposit accounts on the basis of special features. For CD accounts, the comparison of rates will be based on the size and maturity of deposits. For accounts without maturity dates, the FDIC will allow the segregation of savings accounts and NOW accounts but otherwise will not allow account segregation.

What about deposit accounts with different rates for different balances? For example, what if a bank offers an interest-bearing checking account that pays a premium rate for average balances above $10,000? Or what if a bank requires a minimum CD balance of $50,000 to obtain a special rate?

The “national rate” is a simple average of rates paid by all insured depository institutions and branches for which data are available. Rates for savings and interest checking accounts are based on the $2,500 product tier, while rates for money market accounts and certificates of deposit are based on the $10,000 and $100,000 product tiers for non-jumbo and jumbo accounts, respectively. The FDIC uses these account types and maturities because they represent the most common types of interest-bearing accounts for which data are available (representing no fewer than 47,000 locations and as many as 80,000 locations).

What about deposit accounts with tiered rates? What about deposit accounts with rates tied to an index (such as WSJ Prime)? For example, for balances up to $50,000, the first tier rate on an account might be 55 percent of Prime. For balances in excess of $50,000, the second tier rate might be 65 percent of Prime. How does the rule apply to such variable rate products?

All deposit rates offered by institutions subject to the interest rate restrictions in Section 337.6 must conform to those restrictions. In the example above, the first tier rate as well as the second tier rate must conform.

What about CD accounts with odd maturities?

In applying Section 337.6, the FDIC will compare the interest rates on the bank’s CD accounts with the prevailing local rates (if the FDIC determines that the bank is operating in a high-rate area) or the “national rate.” This comparison will be based on the amount and maturity of the account. For example, in a high-rate area, the rate on a bank’s one-year certificate of deposit will be compared to the prevailing local rate for one-year certificates of deposit. If the bank’s rate does not exceed the local rate plus 75 basis points, the bank’s rate will be permissible.

When the term of a bank's CD account is uncommon, leaving few comparables, the FDIC will use linear interpolation (see below) to determine the prevailing rate.

For deposits of comparable maturity, the FDIC will calculate the prevailing rate for deposits under $100,000 (non-jumbo) and over $100,000 (jumbo).

Example

In the example below, the bank's $50,000 tier exceeds the rate cap by five basis points and therefore does not conform to the interest rate restrictions. Lowering the $50,000 tier to 1.45% would bring the rate into compliance. The rate for the $10,000 tier is in compliance.

Bank's Rates – Less Than $100,000	
Tier	Rate
$10,000	1.2
$50,000	1.5

Competitors' Rates - Less Than $100,000	
Bank/Tier	Rate
Bank A/ $10,000	0.5
Bank A/ $50,000	0.7
Bank B/ $10,000	0.8
Bank B Branch/ $10,000	0.8
Prevailing Rate (.5 + .7 + .8 + .8) / 4 =	0.7
Rate Cap (.7 + .75) =	1.45

What is "linear interpolation?"

Linear interpolation is a way of estimating a value based on at least two other values. For example, if there is a market area where we can determine the effective yield for both 9-month CDs and 12-month CDs, but the subject bank wants to offer an 11-month CD for which we find few comparables, we can use linear interpolation to determine the 11-month yield. It would be calculated as follows:

Available data

Market Rate 9-Month CD	0.90%
Market Rate 12-Month CD	1.20%

The 12-month CD is 3 months longer than the 9-month CD.
(12 - 9 = 3)

The 12-month CD yield is 30 basis points more than the 9-month CD.
(1.20 - .90 = .30)

On average, the yield of the CD increases 10 basis points for every additional month of maturity.
(.30 / 3 = .10)

Using linear interpolation, we estimate a 10-month CD would yield 1.00% and an 11-month CD would yield 1.10%.

(.90% + 0.10% = 1.00%)   and   (.90% + 0.20% = 1.10%)

In this example, the maximum allowable rate for an 11-month CD is 1.85% (1.10 + .75).

Should the cost of gifts given by a bank for opening a deposit account be included in the calculation of the deposit rate? For example, what if an institution is giving new certificate of deposit customers an iPod with a retail value of $50?

Small premiums (with a value of $10 or $20) may not qualify as "interest." *See* 12 C.F.R. § 329.103. Larger premiums, however, qualify as "interest." Therefore, in the example above, the cost of the gift should be included in the calculation of the interest rate.

Brokered Deposits

When assessing an application for a brokered deposit waiver, what factors does the FDIC consider?

Applications for brokered deposit waivers are evaluated on a case-by-case basis and are not automatically granted. The waiver request should include a plan for quickly reducing an institution's dependence on brokered funds and restoring capital to well-capitalized status. Expedited processing should not be expected in the current environment. Insured depository institutions are encouraged to use FDICconnect when applying for a brokered deposit waiver.

Waiver applications are evaluated for traditional safety-and-soundness concerns based on an institution's capital position, asset quality, liquidity, and earnings performance. The opinion of an institution's primary federal regulator and an institution's Community Reinvestment Act rating are considered. Management's capability to use brokered deposits, manage the potential volatility, and reduce reliance on such funding weighs heavily on the overall analysis. The FDIC will assess an institution's contingency funding plans related to lines of credit with other correspondent banks and government agencies. Further, the FDIC will review an institution's current business plan, specifically related to expansion or growth. Consideration also will be given to an institution's liquidity monitoring program and its plans to reduce its reliance on brokered deposits.

If a bank falls below well-capitalized, should existing non-brokered certificates of deposit that are more than 75 basis points above the average rate or effective yield in the bank's local market area or the national rate be reported on the Call Report as brokered deposits?

High-cost certificates of deposit, generated before a bank falls below well-capitalized, should not be reported as brokered deposits and may continue to be held until their maturity dates. Upon renewal, the certificate of deposit cannot exceed the applicable market average by more than 75 basis points.

When comparing the actual cost of brokered deposits to the Section 337.6 rate restrictions, should a bank use the Annual Percentage Yield (APY) the depositor receives or the all-in cost the bank pays? For example, if a customer receives 3.50 percent APY and a deposit broker charges a 25-basis points fee on the deposit, should the bank use 3.50 percent or 3.75 percent?

In the above example, the rate restrictions of Section 337.6 would apply to the all-in-cost (APY plus 25 basis points fee or, in this example, 3.75 percent). Interest on deposits should be consistent with the Reports of Condition and Income. The instructions for line item RI 2.a. state in part:

"Include as interest expense on the appropriate category of deposits finders' fees and brokers' fees that represent an adjustment to the interest rate paid on deposits the reporting bank acquires through brokers. If material, such fees should be capitalized and amortized over the term of the related deposits. However, exclude fees levied by brokers that are, in substance, retainer fees or that otherwise do not represent an adjustment to the interest rate paid on brokered deposits."

Are deposits received through a deposit placement network—also referred to as reciprocal deposits—brokered deposits?

For purposes of FDIC Section 337.6 ("Brokered Deposits"), deposits received through a deposit placement network on a reciprocal basis ("reciprocal deposits") are brokered deposits and should be reported as such on Call Reports and Thrift Financial Reports. This is consistent with the final rule approved by the FDIC Board on February 27, 2009, which excludes reciprocal deposits from the newly added adjusted brokered deposit ratio for Risk Category I institutions, but does not alter the general definition of a brokered deposit.