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April 14, 2008

Robert E. Feldman, Executive Secretary  
Attention: Comments  
Federal Deposit Insurance Corporation  
550 17<sup>th</sup> Street, N.W.  
Washington, D.C. 20429

Re: Processing of Deposit Accounts in the Event of an Insured Depository Institution Failure and Large-Bank Deposit Insurance Determination Modernization

Dear Mr. Feldman:

We are writing in response to the Federal Deposit Insurance Corporation's ("FDIC") request for comments on a proposed regulation titled "Processing of Deposit Accounts in the Event of an Insured Depository Institution Failure and Large-Bank Deposit Insurance Determination Modernization" published in the Federal Register on January 14, 2008 (the "Proposed Rule"). Seward & Kissel LLP represents a large number of registered broker-dealers that act as "deposit brokers" in offering certificates of deposit ("CDs") issued by FDIC-insured depository institutions ("Insured Institutions") to their clients and money market deposit accounts ("MMDA") and NOW accounts as part of so-called "sweep" arrangements in which client funds are automatically deposited by the broker-dealers in Insured Institutions.<sup>1</sup> Several of our clients have asked us to submit this letter.

The Proposed Rule would define for purposes of all Insured Institutions "what is meant by a deposit account balance on the day an insured depository institution fails and, thus, would define the deposit account balance on which the FDIC would make insurance determinations." In addition, certain "Covered Institutions" – defined as Insured Institutions having at least \$2 billion in domestic deposits and at least either (i) 250,000 deposit accounts; or (ii) \$20 billion in total assets – would be required to, *inter alia*, have automated processes to impose provisional holds and to have practices and procedures to provide depositor and customer data in a standard format following the closing of the Insured Institution.

The Proposed Rule does not expressly apply to brokered deposit arrangements. For purposes of this letter, brokered deposit arrangements fall into two basic types: CD Programs and Sweep Programs. In a CD Program, a broker-dealer enters into an agreement with

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<sup>1</sup> In many broker-dealer sweep arrangements the Insured Institution, or Insured Institutions, participating in the arrangement are affiliated with the broker-dealer.

an Insured Institution to offer and sell the Insured Institution's CDs to the broker-dealer's clients. The CDs that are issued are represented by a Master Certificate of Deposit – a negotiable instrument representing a number of individual CDs, typically in \$1,000 increments – that is held by The Depository Trust Company (“DTC”)<sup>2</sup> as sub-custodian for the broker-dealer (a “Master Certificate”). The CDs are recorded on the books of the Insured Institution in the name of “DTC, acting for itself and others, each acting for themselves and others,” – a manner of recordation designed to permit the “pass-through” of deposit insurance.<sup>3</sup> The broker-dealer maintains records of the CDs held by its clients and those records would be submitted to the FDIC in the event of the failure of the Insured Institution.

In a Sweep Program a broker-dealer enters into an agreement with an Insured Institution to offer an MMDA, or an MMDA linked to a NOW account, to its clients. The MMDA, and if applicable the NOW account, are recorded on the books of the Insured Institution in the name of the broker-dealer “acting for its clients, acting for themselves and others,” or such other manner of recordation designed to permit the “pass-through” of deposit insurance. The broker-dealer maintains records of the deposit accounts held by its clients and those records would be submitted to the FDIC in the event of the failure of the Insured Institution.

On March 7, 2008, I spoke with Joseph DiNuzzo, Senior Counsel, FDIC Legal Division, concerning the Proposed Rule. Mr. DiNuzzo confirmed that the Proposed Rule is not intended to address brokered deposit arrangements and that the FDIC's policies with respect to processing insurance claims in brokered deposit arrangements are set forth in the Deposit Broker's Processing Guide (the “DBP Guide”). Mr. DiNuzzo stated that the FDIC would welcome comments from Seward & Kissel on behalf of its clients with respect to the scope of the Proposed Rule and the FDIC's policies on processing insurance claims from broker-dealers on behalf of their clients. We appreciate the opportunity to submit comments.

One concern prompting these comments is the significant growth in brokered deposits. According to a Securities Industry Association (now the Securities Industry and Financial Markets Association) survey conducted prior to the adoption of the Federal Deposit Insurance Corporation Improvement Act of 1991, there were approximately \$90 billion in brokered deposits held through registered broker-dealers at that time. As of the December 31, 2007 Call Reports, there were nearly \$600 billion in brokered deposits outstanding, an amount that is likely underreported. In addition, there are significant numbers of large Insured Institutions that rely heavily on brokered deposits and, were one to fail, the resolution of the insurance claims would present issues for the FDIC that would be unprecedented in their scope, if not their nature.

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<sup>2</sup> DTC is a member of the Federal Reserve System, a limited purpose trust company under New York State banking law and a registered clearing agency with the Securities and Exchange Commission.

<sup>3</sup> See letter to Anthony C. J. Nuland, Esq., from Roger A. Hood, General Counsel, FDIC (May 24, 1996).

### 1. Scope of the Proposed Rule

We request that the FDIC confirm that the Proposed Rule, if adopted, would not require changes to the manner in which Insured Institutions and broker-dealers maintain records with respect to the brokered deposit arrangements described above and that neither Insured Institutions nor broker-dealers will need to develop systems in order to comply with the Proposed Rule with respect to such arrangements.

### 2. Correspondent and Settlement Accounts

It is common in both CD Programs and Sweep Programs for client funds being deposited by a broker-dealer with an Insured Institution to be deposited in either an account maintained by the Insured Institution at a correspondent bank, or in a settlement account maintained by the Insured Institution at a bank acting as settlement agent. In each case, the broker-dealer and the Insured Institution agree that it is their intent that a deposit be created when same-day funds are deposited into such accounts.

For most purposes, deposit relationships are governed by state contract law. A deposit is typically created when funds are accepted by a depository institution with the intention of creating a debtor/creditor relationship with the depositor. Where correspondent or settlement accounts are used in a CD Program or a Sweep Program, and the broker-dealer and the Insured Institution agree that a deposit is created when same-day funds are credited to the account at the correspondent bank or the settlement bank, as applicable, a deposit would be accepted by the Insured Institution under state contract law.

We request that the FDIC confirm that funds received by an Insured Institution in a correspondent account or settlement account in connection with a brokered deposit transaction as described above would be considered a "deposit" into the account recorded on the books of the Insured Institution and would be eligible for FDIC insurance upon receipt in the account at the correspondent bank or the settlement bank. Confirmation could be set forth in the explanatory information accompanying a final regulation, or by separate response to this letter.

### 3. DBP Guide

The DBP Guide published by the FDIC, and last updated in January 2002, is intended to provide guidance to deposit brokers in making insurance claims on behalf of their clients. The DBP Guide is a useful tool for deposit brokers. However, it reflects certain misunderstandings about brokered deposits in the securities industry. For example, the DBP Guide discusses multiple tiers of brokers and obligations of "first tier" brokers with respect to "sub-tier" brokers. It is not clear what this refers to. As indicated above, brokered CDs in the securities industry are generally evidenced by Master Certificates held by DTC, which is not a broker-dealer. DTC's records indicate which broker-dealers hold CDs of an Insured Institution. DTC does not, and would likely not, take on the responsibility of submitting client records of broker-dealers to the FDIC in the event of a failure and instructing broker-dealers not to trade in CDs of a failed Insured Institution.

The DBP Guide may be referring to certain clearing arrangements in which a broker-dealer, referred to as a clearing broker, acts as a correspondent for other broker-dealers, referred to as introducing brokers. In these arrangements, the clients of the introducing broker are actually clients of the clearing broker, so again this “sub-tier” reference is not accurate. It would be useful to clarify what the DBP Guide is referring to.

Similarly, there is no acknowledgement that brokered CDs in the securities industry are typically evidenced by a Master Certificate, a negotiable instrument issued by the Insured Institution. In resolving failed institutions in the past, the FDIC has frequently transferred deposits to another Insured Institution or created a new Insured Institution into which deposits were transferred. Depositors have been offered an opportunity to maintain their deposits at the transferee Insured Institution at a new rate, or withdraw their funds. When questioned in the past about the issuance of a new Master Certificate to represent CDs held by brokerage clients that want to retain a CD in the transferee Insured Institution under the new terms, the FDIC staff has not appeared to understand the need to revise or re-issue Master Certificates, or to understand generally the significance of the Master Certificates. It would be useful for the FDIC to address this issue in the DBP Guide.

Finally, the DBP Guide does not specifically address Sweep Programs. While the recordkeeping issues are similar to those of CD Programs, the economic significance of Sweep Programs to clients is different. In a CD Program, clients have placed their funds in a time deposit and the funds are not readily accessible. In a Sweep Program, clients have deposited funds in Insured Institutions that are intended to be readily accessible to them. Many broker-dealers offer checkwriting, debit card and ATM features through the client’s brokerage account and withdraw funds from the client’s MMDA or NOW account to satisfy debits in the brokerage account created by use of the transaction features.

The FDIC’s policy with respect to transaction accounts, NOW accounts and MMDAs maintained directly at failed Insured Institutions has been to expeditiously provide access to funds on deposit. We believe the FDIC needs to consider how it will provide access to funds of a broker-dealer’s clients in MMDAs and NOW accounts at a failed Insured Institution that are held through a broker-dealer’s Sweep Program.

#### 4. NetBank

The recent failure of NetBank raised a number of issues concerning the processing of insurance claims for brokered deposits. At the outset, it is important to note that our clients uniformly praise the professionalism of the FDIC staff in responding to questions concerning insurance claims. Also, insurance payments for most claims were typically received within a few business days of the FDIC’s receipt of client records.

As stated in the explanatory information accompanying the Proposed Rule, NetBank had total deposits of \$1.9 billion and approximately 175,000 deposit accounts at the time of closure. Estimates from our clients indicate that probably in excess of 15,000 client

accounts at broker-dealers held NetBank CDs. It is not clear whether the client accounts at broker-dealers are included in the 175,000 figure.

The primary concerns of our clients involve (i) timely dissemination of information, (ii) parity of treatment with direct deposits, and (iii) requests by the FDIC for extensive documentation for trust accounts and uninsured deposits.

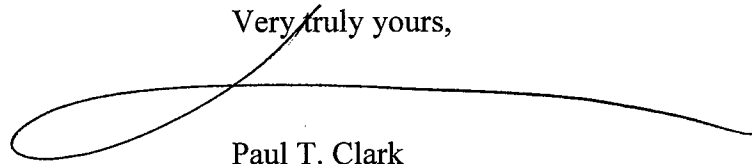
When an Insured Institution fails, the FDIC issues an information release concerning the failure of the Insured Institution. Most information in the release addresses claims by direct depositors. Although a point of contact is designated to receive records from broker-dealers, very little information is provided about the payment of brokered deposits. For example, in the case of NetBank, the FDIC promptly determined that it would pay 50% of all uninsured deposits. However, it was not clear whether this payment would be available to uninsured brokered deposits. In addition, our clients consistently recite the fact that the FDIC appears to lack the resources to respond promptly to questions about insurance claims. This, of course, leads to delay and confusion.

The documentation required by the FDIC to process claims for uninsured amounts and claims by trusts needs to be streamlined. As noted above, the FDIC quickly determined that it would pay 50% of the uninsured deposits of direct depositors. However, clients of broker-dealers were required to forward extensive documentation and waited weeks before receiving payment on uninsured amounts. Unlike the electronic format it accepts from broker-dealers for insurance claims, uninsured depositors were required to complete complicated paperwork. FDIC staff, though polite, responded to inquiries by stating that they lacked sufficient resources to process the clients' claims in a more timely manner. We believe that this is an area that the FDIC could target for improvement.

With respect to trust accounts, a number of our clients have indicated that no payments were made in connection with trust deposits until all affidavits and supporting documents were completed. Deposits held by trusts may be eligible for deposit insurance greater than \$100,000 depending on the number of *bona fide* beneficiaries. However, there appears to be no reason that the first \$100,000 could not be paid by the FDIC pending determination of eligibility for additional amounts.

We hope you find our comments useful. Please do not hesitate to contact us if we can provide additional information on any of the issues raised in this letter.

Very truly yours,

A large, elegant handwritten signature in black ink, which appears to be "Paul T. Clark". The signature starts with a large loop on the left and extends across the page to the right.

Paul T. Clark

PTC:tv