American Bankers Association
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May 7, 2019

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Re: Brokered Deposits RIN 3064-AE94

Dear Mr. Feldman,

The American Bankers Association[1] (ABA) appreciates the opportunity to comment on the Federal Deposit Insurance Corporation's (FDIC) advance notice of proposed rulemaking (ANPR) on brokered deposits. ABA is supportive of the comprehensive review and agrees with the FDIC that significant changes in technology, business models, and products warrant a review of the regulations, interpretations, guidance and other policies that make up the FDIC's approach to brokered deposits. The current overly broad interpretation and application of who is considered a deposit broker, and by extension what deposits are considered brokered, is impeding bank innovation, harming consumers, unnecessarily stigmatizing key funding sources and thus inhibiting bank efforts to innovate and maintain a diversity of funding.

Enacted in 1989, as part of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA), Section 29 of the Federal Deposit Insurance Act (FDIA) sets restrictions on the acceptance of brokered deposits by institutions with weakened capital positions. The statute was intended by Congress to prevent *troubled institutions* from holding funds placed by third-parties whose primary business is "placing deposits or facilitating the placement of deposits of third parties" with insured depository institutions. FDIC interpretations (in the form of staff advisory opinions, frequently asked questions and other guidance) over the last 30 years have gone well beyond the statutory intent by extensively expanding who is considered a deposit broker, narrowly interpreting the exceptions, and applying restrictions beyond the focus of Congress on troubled institutions. Some types of entities that may currently be inappropriately classified as deposit brokers include, among others, —

- Social media platforms
- Fintech partners, such as apps/application programming interfaces (APIs)
- Bank affiliates and subsidiaries, including operating subsidiaries
- Employees of bank affiliates and subsidiaries

[1] *The American Bankers Association is the voice of the nation's $18 trillion banking industry, which is composed of small, midsize, regional, and large banks that together employ more than 2 million people, safeguard nearly $14 trillion in deposits, and extend more than $10 trillion in loans.*

- Homeowners associations
- Advertising and marketing partners
- Websites for personal finance organization, advice, and improvement
- Alumni associations and other member-based organizations
- Universities
- Small businesses.

Compounding the detrimental effect of a broad interpretation of "deposit broker" is an inapt supervisory use of brokered deposits and the national rate cap as a gauge of volatile or high-risk funding. Currently, there is a significant overlap between the FDIC's labeling of deposits as "brokered" and what, for liquidity and interest rate risk management purposes, has historically been considered "core" funding. As a practical matter, the FDIC has failed to recognize that the two categorizations are no longer mutually exclusive, leading to supervisory and regulatory bias against what, in actual practice, are stable, relationship deposits.

A fundamental role of banks is to provide financial services including deposit taking, lending, access to the payment system, wealth management, trust and custody services and cash management services. Modern technology, including an increasing diversity of financial affiliations, and the creation of and growth in online and mobile banking, allows banks to offer these services, gather stable deposits and obtain access to potential depositors via new mechanisms. Going forward, it is imperative that the FDIC improve and modernize its framework to focus on the original purpose of Section 29 and ensure that banks are not penalized for engaging in practices that are well within the bounds of a bank's normal course of business, including responding to evolving customer preferences and enhancing diversification and resilience in bank funding.

A clearer, more modern approach would embrace the use of modern products and deposit gathering mechanisms that allow banks to leverage innovation and provide consumers with more flexibility, convenience, and transparency. To achieve this, we recommend that, consistent with Congressional intent, the FDIC significantly narrow who is considered a "deposit broker" based on clearly articulated policy goals. A good starting point, consistent with the meaning of the statute, would be to limit the classification of an entity as a "deposit broker" to persons that contract to place deposits of unaffiliated third parties. Such a clear definition would decrease uncertainty and distinguish third parties involved in the provision of banking services from those acting as a broker of deposits. Further, consistent with Congress' intent, the restrictions on gathering and holding brokered deposits should be limited to troubled depository institutions.

Of equal importance is a recognition that certain deposits, such as those where the bank and the customer have a direct relationship, are by definition, not "brokered." Relationship deposits would include those generated from operating and other subsidiaries and affiliates of a bank, and other deposits involving a direct, continuing relationship between a customer and an insured depository institution. Empirical evidence suggests that these deposits are among the most stable,; because the FDIC's current interpretation of "deposit broker" hinges on the involvement of *any* third party, many deposits scoped into current interpretations are actually among the most stable funding sources. Penalizing these deposits is harmful both to banks and their customers.

Further, the methodology behind the national rate cap is in need of revision. Many examiners inappropriately use the national rate cap (which Section 29 directs the FDIC to establish) as a proxy for high rate deposits at well capitalized institutions. The rate, however, does not reflect a

market rate consistently across all stages of the economic cycle and is not dynamic enough to adapt to changes in competition or other drivers of deposit market conditions. Establishing a more robust and relevant rate will go a long way to ensuring that healthy, well-capitalized banks are not inappropriately discouraged from holding stable funding gathered at rates consistent with the markets in which they operate.

As the FDIC engages in a comprehensive review of its regulations and policies regarding brokered deposits, we urge the agency to consider the policy goals it seeks to achieve and the alignment of those goals with both Section 29 and modern banking practices. Again, we remind the FDIC that well-capitalized banks should not be subject to general supervisory limitations regarding the amount of brokered deposits they can accept or the deposit rates they may offer. Neither should the application of "brokered deposits" be so broad that the industry is required to perform costly stress tests to manage a potential funding cliff that the FDIC itself has created, by expansive application of its overly broad characterization of brokered deposits. We remind the FDIC, as Congress noted in 1989 and as the FDIC itself has recognized in the ANPR, that brokered deposits are not in and of themselves risky. This has become particularly true given the significant changes in funding markets and various other prudential supervision tools put in place since the early 1980s.

The purpose of this letter is to highlight key problems with the current framework for and application of the FDIC's brokered deposit interpretations and offer suggestions as to how it can be modernized and better aligned with the goals Congress had in mind when enacting Section 29. Below, we first recount the objective of Section 29, then describe the ways in which FDIC's interpretations of Section 29 have been overbroad, then explain how, by focusing its characterizations of deposit broker and excluding relationship deposits, FDIC can modernize its approach to Section 29.

We also refer the FDIC to the letter submitted by ABA's HSA Council, for technical discussion about those products and how they intersect with the brokered deposit framework.

Congress enacted Section 29 to stop abuse of brokered funds by weak and troubled institutions

Section 29 was adopted by Congress in connection with the savings and loan crisis of the 1980s. At that time, many savings and loans relied on funding in the form of certificates of deposit (CDs) bundled for investors by third parties, which became known as brokered deposits. Brokered deposits were then new products, considered unstable and highly rate sensitive. Typically, they were bundled and sold in bulk to the highest bidder. Ultimately, institutions that depended on this type of funding were more expensive for the federal deposit insurance agencies to resolve in the event of failure.

Section 29 was intended to make resolution of failed banks less costly by restricting weak institutions from holding brokered deposits. Initially, the FDIC sought to regulate brokered deposits by limiting the deposit insurance available for such deposits. Its 1984 proposed definition was, however, rejected by a court on the grounds that it exceeded FDIC's authority. When Congress took up the idea of limiting brokered deposits, it started with the rejected definition, but significantly narrowed its scope of application. Despite the rejection of

the FDIC's initially proposed definition by both the courts and Congress, FDIC continues to reflect it in its implementation of Section 29.

The attached legal memorandum from Jones Day provides an analysis of the legislative history of Section 29, including the regulatory initiatives of the FDIC that preceded its adoption. The memo provides insight to Congressional intent and policy goals, as well as affirms that the FDIC has ample authority to make appropriate changes to its body of interpretation and guidance.

The definition of "deposit broker" has expanded well beyond its original purpose, with little justification

With Section 29, Congress took a targeted approach, intending to prevent weaker institutions from accumulating expensive, enhanced risk funding that provides little franchise value to the bank accepting the funds. Today, however, the term "brokered deposits" permeates banking regulation and supervision, yet the current framework, and process for designation of an entity as a deposit broker, is *ad hoc*, and lacks cohesion, public input and transparent policy goals. The result is an expansive definition of "deposit broker" that captures funding and institutions beyond what was targeted under Section 29.

FDIC staff has interpreted two key elements of the statutory definition of deposit broker in issuing its many, expansive, interpretations since Section 29 was adopted: "any person *engaged in the business* of placing deposits, or *facilitating the placement* of deposits, of third parties with insured depository institutions" [emphasis added]. The FDIC staff's interpretations accordingly hinge on the presence of a third party, however peripherally involved.[2] In contrast to the deposit placement practices that generated concern in the 1980s, the FDIC's current brokered deposit classification extends broadly to deposits acquired with the involvement of any unaffiliated party– despite the fact that this is not what Congress intended. For example, under existing interpretative guidance, a deposit broker may be found to include (among others)—

- Social media platforms
- Fintech partners, such as apps/application programming interfaces (APIs)
- Bank affiliates and subsidiaries, including operating subsidiaries
- Employees of bank affiliates and subsidiaries
- Homeowners associations
- Advertising and marketing partners
- Websites for personal finance organization, advice, and improvement
- Alumni associations
- Universities
- Small businesses.

As noted in the ANPR, the FDIC looks to certain criteria to determine whether a person or entity is engaged in placing deposits or facilitating the placement of deposits to determine if that person

[2] In its FAQs the FDIC states that "a brokered deposit may be any deposit accepted by an insured depository institution from or through a third party."

or entity is a "deposit broker." FDIC staff reviews such arrangements on a case-by case basis, considering the following factors:[3]

- Whether the third party receives fees from the insured depository institution that are based (in whole or in part) on the amount of deposits or the number of deposit accounts;
- Whether the fees can be justified as compensation for administrative services (such as recordkeeping) or other work performed by the third party for the insured depository institution (as opposed to compensation for bringing deposits to the insured depository institution);
- Whether the third party's deposit placement activities, if any, are directed at the general public as opposed to being directed at members (or "affinity groups") or clients;
- Whether there is a formal or contractual agreement between the insured depository institution and the third party (e.g., referring or marketing entity) to place or steer deposits to certain insured depository institutions;
- Whether the third party is given access to the depositor's account, or will continue to be involved in the relationship between the depositor and the insured depository institution.

It is unclear how these criteria were derived, on what legal basis, how they are used, and which factors, if any, are drivers of a "deposit broker" designation, since none of them were exposed to public review and comment. What is clear is that the criteria are so broad as to describe features of virtually any third party arrangement, however incidentally linked to a deposit account. Moreover, the parameters do not reflect changes in technology and business structures that are responsive to customer preferences for user simplicity and transparency or new business models. For example, some banks now employ (in whole or in part) a "branchless banking" model whereby depositors are able to establish and manage accounts without having to enter a physical retail branch, increasing access to banking services generally. There is little evidence that suggests these funds, or business models, pose enhanced risk to either banks or the deposit insurance fund.

The wide net cast by the FDIC unnecessarily increases the costs and regulatory consequences associated with holding deposits labeled by the FDIC as brokered. Over the past 30 years, there have been numerous changes to the capital, liquidity, and resolution regulations, most recently through the Dodd-Frank Act and the implementation of Basel III standards. Many of these rules, such as the liquidity coverage ratio, and supervisory exercises such as those related to capital stress testing, incorporate the FDIC's definition of brokered deposits, employing the presumption that deposits designated as brokered are a significantly less stable source of funding than other types of deposits. FDIC deposit insurance assessments incorporate higher costs for deposits that are considered brokered. Accordingly, it is now of even greater importance that FDIC's characterization of deposits as brokered accurately reflect the narrow scope contemplated by Section 29.

[3] 84 Fed. Reg. 2,366 (Feb. 6, 2019).

Customers want the convenient services inhibited by FDIC brokered deposit designations

Given the technological changes that have taken place since the early 1980s, the FDIC's overbroad interpretative framework hinders banks from leveraging innovations that make accessing and managing their financial assets more efficient for customers. Today's banking customers are increasingly looking at the suite of products and services offered, convenient access to their funds, and services such as direct deposit and bill pay or investment management. In the modern marketplace for bank deposits, factors other than interest rate, such as brand awareness/loyalty, customer service, ease of access, mobile applications, digital wallets, etc., are often the most critical factor for acquiring and retaining customers.

Focus the interpretation of "deposit broker" and exclude relationship deposits

In order to ensure that neither banks nor their customers are disadvantaged by an overly broad classification of deposits as brokered, we urge the FDIC to limit the classification of an entity as a "deposit broker" to persons that contract to place deposits of unaffiliated third parties with banks or who contract with troubled insured depository institutions for the purpose of selling interests in their deposits to third parties.

Additionally, deposits involving a direct, continuing relationship between a customer and an insured depository institution should be expressly excluded from consideration as "brokered," even if an unaffiliated third-party is involved in the origination of the deposit or maintains an ongoing relationship with the depositor independent of the deposit relationship. There is scant evidence that the relationship deposits gathered through the normal course of providing banking services through affiliates or marketing partners pose enhanced risk to safety and soundness or the deposit insurance fund. On the contrary, the FDIC, together with the other banking regulators, has recognized retail relationship deposits as among the most stable sources of funding through classifications made in rulemakings such as the liquidity coverage ratio and the net stable funding ratio.[4] Yet, extant FDIC guidance has also caused many such retail deposits to be classified as "brokered" simply because there is a third party indirectly involved or involved only in sourcing the customer relationship with no ongoing involvement with respect to the deposits. Some examples of deposits where the banking organization and the customer have a direct, ongoing relationship are discussed below.

- **Affiliate and Subsidiary Funds**. Since 1989, there have been many regulatory and statutory changes, including the Gramm-Leach-Bliley Act, which allowed for the affiliation of banks and securities firms. Additionally, technological developments have significantly increased customers' ability to access their accounts more efficiently. Together, these developments have significantly altered the way customers engage with their financial institutions and allowed new products to develop that meet customers' demand to have a seamless relationship with their banking organization.

[4] The LCR defines relationship deposits as those where the depositor has another established relationship with a covered company, such that withdrawal of the deposit would be unlikely."https://www.govinfo.gov/content/pkg/FR-2014-10-10/pdf/2014-22520.pdf.

- **Sweep accounts.** One product that has emerged since Section 29 was enacted is sweep deposits. While the FDIC excludes a portion of these deposits from classification as brokered, it imposes arbitrary limitations in order for them to be exempt under the primary purpose exemption. In 2005, the FDIC's General Counsel issued a staff opinion stating that, "when certain conditions are observed, the primary purpose of a broker dealer in sweeping customer funds into deposit accounts at its affiliated IDI is to facilitate customers' purchase and sale of securities."[5]

  Among the conditions is that funds are not swept to a time deposit account and do not exceed 10 percent of the total assets handled by the affiliated broker dealer. Since the broker dealer has little or no control over how much cash customers choose to keep in their brokerage accounts (and that proportion of cash can significantly increase during market downturns and customers' resulting flights to safety), the broker dealer is unable to do anything to ensure that it remains in compliance with this condition—except perhaps by moving customer cash into other products such as money market funds. The insured depository institution is permitted to pay fees to the affiliated broker dealer, but the fees must be flat fees (i.e., per account or per customer fees) representing payment for recordkeeping or administrative services and not for the placement of deposits.

  Sweep deposits received by banks from affiliated brokers are demonstrably stable. Indeed, during the financial crisis data show that banks saw a net *inflow* of sweep deposits from brokerage customers as they de-risked by selling securities holdings. This counter-cyclical effect increased, rather than decreased, stability for these banks in a time of uncertainty. The FDIC has acknowledged in both its 2013 Study on Core and Brokered Deposits and the Liquidity Coverage Ratio regulations that deposits received by a bank through an affiliated broker's sweep program are more stable than various other types of deposits at banks. These deposits from affiliates of the bank should not be classified as "brokered."

- **Referrals.** Many customers of a broker-dealer or other affiliate of a bank may want banking-specific services such as a home mortgage or a savings account. There is no regulatory penalty to the bank (in terms of funding costs) for an employee of the broker-dealer to refer the customer to its affiliated banks for a mortgage, car loan, or credit card. However, it is likely that an employee referral for a checking or savings account would cause those deposits to be considered brokered, which not only impacts the bank's funding costs, but also the customer experience, leading to potential confusion for a customer seeking a consistent experience across their financial products. Such referrals should not be deemed as creating "brokered deposits."

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[5] *See* FDIC Advisory Opinion 05-02 (February 3, 2005) ("2005 Advisory Opinion").

- **Deposits Gathered from Operating Subsidiaries.** For purposes of efficiency, and other reasons, some banking organizations create operating subsidiaries. These deposits do not have share the characteristics of those intended to be restricted by Section 29. Operating subsidiaries are under the exclusive control of the parent insured depository institution (IDI), engage only in activities permissible for an IDI and are treated as a division of the IDI for purposes of most supervision and regulation. Because the activities of operating subsidiaries, including generating deposits for a parent IDI, are activities in which the IDI could engage directly, deposits placed by operating subsidiaries (and their employees) with the parent IDI are essentially deposits generated by the parent IDI itself. The choice of corporate structure, which may provide operational and other benefits, should not be penalized under the FDIC's interpretation of brokered deposits. FDIC should revise its regulations to clarify that operating subsidiaries of an IDI are not deposit brokers with respect to deposits placed with the parent IDI.

- **University Products.** Universities and colleges may enter into an agreement with a bank for the bank to be the provider of banking services to students, faculty, and staff (collectively "University Patrons"), who have the option to access the bank's products and services. These agreements typically are long-term arrangements that provide the bank with the right to market its products and services to University Patrons in exchange for some fee paid by the bank to the university. The university is not in any way involved in opening or maintaining a bank account for a University Patron. The deposit accounts opened through these programs do not behave like traditional brokered deposits: the accounts often represent long-term banking relationships that can extend well beyond a student's graduation.

  One service often offered under the agreement is a campus ID card that has payment functionality through a co-branded debit card. These arrangements offer University Patrons the convenience of carrying a single card for campus identification and banking access while offering additional benefits, such as waivers of certain bank fees for accounts linked to campus cards. The cards are optional, and University Patrons may select a campus ID card without payment functionality. The university is not in any way involved with opening or maintaining the bank account, which is handled exclusively between the bank and University Patron who chooses the debit card option. FDIC has improperly classified these deposits as "brokered," despite bearing no similarities to deposits intended to be covered by Section 29 of FIRREA. The deposit accounts underlying the campus ID cards with payment functionality should not be considered brokered deposits.

- **Health Savings Accounts (HSAs).** As with sweep accounts, HSAs are a new products, created since the enactment of FIRREA. HSAs are an important and growing part of employee benefit strategies and are the only health benefit product in the United States that is portable. They were specifically designed so that employees who move from job to job can associate their HSA with their new employer's HSA-qualifying health plan. This is possible because HSAs are owned by individuals, in all cases, not employers or any other third party. There are no exceptions. By definition, HSAs involve longer-term

relationships with banks, much like individual retirement accounts, and should not be characterized as "brokered deposits."

Firms that provide normal course marketing arrangements and practices should not be considered deposit brokers

Many businesses engage in marketing and advertising to promote their products and attract customers, including digital marketing channels such as social media and other, non-traditional forms of advertising. Banks, like other businesses, need to advertise and market their products and services, through modern channels. However, the current FDIC interpretative guidance, which largely dates back to letters published in the late 1980s and early 1990s, focuses on marketing techniques favored at the time, such as TV and direct mail, and fees earned as key factors informing whether or not a third party is "facilitating the placement of deposits." Additionally, these letters focus on whether a third party is engaged in "active marketing," and in particular whether such third party is engaged in activity that is more than "passive and indirect."[6]

FDIC interpretations have taken an unnecessarily broad view of what constitutes "facilitation" in the context of marketing, finding that mere receipt of a volume-based marketing fee by a third-party would make the third-party a deposit broker. There is little evidence that *deposits* gathered through marketing practices widely employed by businesses today pose enhanced risk to either individual banks or the deposit insurance fund. Given the wide use of these marketing arrangements by a plethora of U.S. corporations, it is hard to understand how the FDIC interprets them as facilitating the placement of deposits for banks. The hiring of a marketing firm, or placing a banner on a popular search engine to advertise its products and attract customers, does not make the marketer or the search engine a "deposit broker" just because it is a bank that has hired the marketer or contracted with the search engine. Moreover, there are no equivalent restrictions on marketing of loans, other assets, or liabilities as there are for deposits, which puts deposit gathering at a disadvantage and can be confusing for customers looking for seamless and consistent interactions with their banks across products. Should an improper or abusive practice arise, it can and should be addressed through appropriate supervisory action.

Regardless of the fee structure, marketing and referral arrangements with third parties should be excluded from brokered deposit considerations, when the customers engage directly with the bank. Active production and distribution of marketing materials does not adversely affect the stability of the funds gathered, nor does the structure of fees paid to the advertising platform. For example, common digital marketing relationships utilize a "cost per click" or "cost per acquisition" compensation model; however, the fee structure has no bearing on the stability of the resultant account relationship.

Additionally, third parties offering prepaid products tied to deposit accounts at a financial institution are not "deposit brokers" simply because they market an alternative to a traditional deposit account. Designation of deposits associated with prepaid products as brokered inappropriately inhibits innovation by financial institutions in this space and by extension impedes banks' ability to provide these customers with the most up to date options. These accounts should not be labeled as "brokered deposits."

[6] FDIC Dodd-Frank Act Study on Core Deposits and Brokered Deposits (July 8, 2011)

The national rate cap should be above the market rate for deposits

In addition to setting restrictions on brokered deposits, Section 29 directs the FDIC to calculate a national rate cap on the interest rates *weaker institutions* may offer on deposits. The cap is established by adding 75 basis points to the "national rate." The national rate is currently established by taking a "simple average of rates paid by all insured depository institutions and branches for which data are available".[7] Because banks with the most branches drive the calculation of the average rate, the current rate does not accurately reflect the cost of deposits for community banks, and others, that do not have extensive branch networks. As a result, the FDIC's rate can be (and currently is) significantly below market in a rising rate environment.

The rates that banks choose to offer on deposits are determined by reference to a variety of factors across multiple tenors and products, including their competitors' rates, and various benchmarks including Treasury rates, Federal Home Loan Bank (FHLB) advances, swap rates, and money market rates, among others. However, the FDIC's methodology does not currently employ or consider these common benchmarks or indexes to set the national rate cap.

An artificially low rate is problematic for well-capitalized and weaker banks alike. Because examiners use the national rate cap as a proxy for higher risk deposits, even well capitalized banks are often discouraged from raising or holding deposits with a rate higher than the national rate cap.[8] For weaker institutions, a non-competitive rate means that these banks have a reduced ability to improve their condition, as they are impaired in their ability to raise funds to sustain their assets. Moreover, it is unclear how the 75 basis point add-on was derived, whether it allows for a sufficiently high level result during all phases of interest rate and business cycles, or if it should be dynamic though the cycles.

In order to identify outlier interest rates, as directed by the statute, we recommend that the FDIC investigate the use of robust, transparent, and widely used benchmarks to determine a market interest rate, with an appropriate and dynamic add-on to establish a threshold for rates that are tolerably above market. For example, as a base rate the FDIC could use the top ten rates posted on bankrate.com, a median of FHLB advance rates or a composite rate of widely understood and accessible benchmarks, or a combination thereof. The add-on to the base rate should be dynamic to ensure the FDIC's national rate is well above that of the deposit market rate. ABA recognizes the difficulty of creating a rate that remains robust through all stages of the economic and interest rate cycles. We recommend that the FDIC allow banks to use their local FHLB advance rate, plus the FDIC's add-on, as an alternative to the national rates. The FHLB rates are a dynamic reflection of the regional market cost of funds and would likely be an accurate gauge of the market through the cycle. An accurate FDIC rate, with add-on, should land sufficiently above normal market rates so as to identify only outlier deposit pricing, including 'specials' or deposit products with features that may not fit into the FDIC's categories for purposes of the national rate cap.

Conclusion

We appreciate the FDIC issuing the ANPR as an important step toward modernization of the

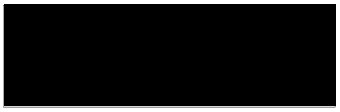
[7] https://www.fdic.gov/news/board/may29no8.pdf.

[8] ABA and state bankers associations joint letter on the national rate cap https://www.aba.com/Advocacy/LetterstoCongress/Documents/Ltr-NationalRateCap20190321.pdf.

brokered deposits rules and policies. We encourage the FDIC to reform its policies and programs regarding brokered deposits using the variety of tools at its disposal. We note that while changes in the statute might be considered, the problems that we have identified in this letter were created by regulation, guidance, regulatory interpretations, and agency policy, all of which can be refined and reformed in similar ways. These policies evolved through various iterations, and it may take a series of actions to conform brokered deposit policies more closely with the purposes of the statute and the realities of banking and customer relationships today. We stand ready to continue this important dialog with the FDIC for the benefit of our customers and to reinforce the strength of the banking system, including through embracing the diversification of funding sources that modern business models and technology make possible.

If you have any questions about these comments, please contact the undersigned at (202) 663-5182 or email: atouhey@aba.com.

Sincerely,



Alison Touhey
Vice President & Senior Regulatory Advisor

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MEMORANDUM

TO: Robert S. Nichols
President and Chief Executive Officer
American Bankers Association

FROM: Lisa M. Ledbetter

DATE: February 25, 2019

RE: Acceptance of Brokered Deposits

EXECUTIVE SUMMARY

In the wake of the savings and loan crisis, Congress enacted Section 29 of the Federal Deposit Insurance Act, titled "Brokered Deposits" ("Section 29"), as part of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA").[1] FIRREA was enacted in direct response to the increasing rate of failures of savings and loan associations with the principal purposes "to reform, recapitalize, and consolidate the Federal deposit insurance system, to enhance the regulatory and enforcement powers of Federal financial institutions regulatory agencies, and for other purposes."[2]

Although Section 29 is titled "Brokered Deposits," the law does not directly define the term "brokered deposit." Instead, the meaning of what constitutes a brokered deposit is derived from the statutory definition of the term "deposit broker."[3] As originally set forth in FIRREA, the key elements of Section 29 for construing which deposits are brokered are the definition of the term "deposit broker," together with the statutory descriptions of arrangements that are within and outside the scope of this definition. Over the years, the Federal Deposit Insurance Corporation ("FDIC") has devoted considerable regulatory attention to interpreting the definition of the term "deposit broker" even in the absence of any intervening legislative amendments to this definition.

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[1] FIRREA, Pub. L. No. 101-73, § 224, 103 Stat. 183 (August 9, 1989); 12 U.S.C. § 1831f.

[2] FIRREA Preamble; *see also* FIRREA at § 101.

[3] By rule, a brokered deposit is "any deposit that is obtained, directly or indirectly, from or through the mediation or assistance of a deposit broker." 12 C.F.R. § 337.6(a)(2).

Since the enactment of FIRREA, staff of the FDIC has issued more than 80 separate and distinct public advisory opinions regarding brokered deposits. Over 60 of these advisory opinions interpret the words the legislature used in defining "deposit broker" and in describing the arrangements that are covered by and excluded from the scope of this definition. These staff advisory opinions predominantly construe the definition of "deposit broker" expansively and/or the exclusions to the definition of "deposit broker" narrowly. An analysis of the FDIC's "Frequently Asked Questions on Identifying, Accepting and Reporting Brokered Deposits"[4] ("FAQs") reveals that the most prevalent answer in the FAQs is that the deposits in question are brokered deposits.

Against this backdrop of numerous case-by-case, fact-specific staff advisory opinions and FAQs that interpret the meaning of Section 29, what constitutes a brokered deposit and in particular, the definition of "deposit broker," it is imperative to ensure that these interpretations are aligned with the language of Section 29 and the reasons Section 29 was enacted into law.

The goal in interpreting any law is to understand the meaning expressed by the words used in the law and the circumstances the legislature intended to address.[5] The words Congress used in defining the term "deposit broker" create genuine uncertainty concerning application of the law to specific fact patterns, as evident from the breadth of circumstances addressed by FDIC staff advisory opinions. In fact, several staff advisory opinions describe the opposing interpretations expressed by the entities to which the opinions are addressed. Moreover, the

[4] *See* FDIC FIL-42-2016, "Frequently Asked Questions on Identifying, Accepting and Reporting Brokered Deposits" (June 30, 2016). The FAQs have not been considered and adopted by the FDIC board of directors at an open meeting. Rather, the FDIC has announced, adopted and updated the FAQs through postings on its public website of Financial Institution Letters ("FILs") addressed to the Chief Executive Officers of FDIC-supervised institutions. FILs "announce new regulations and policies, new FDIC publications, and a variety of other matters of principal interest to those responsible for operating a bank or savings association." *See* https://www.fdic.gov/news/news/financial/index.html.

[5] *See, e.g.*, *Connecticut National Bank v. Germain*, 503 U.S. 249, 255 (1992) (concurring, Stevens) ("Whenever there is some uncertainty about the meaning of a statute, it is prudent to examine its legislative history."); *Wisconsin Public Intervenor v. Mortier*, 501 U.S. 597, 611 n.4 (1991) ("As for the propriety of using legislative history at all, common sense suggests that inquiry benefits from reviewing additional information rather than ignoring it. As Chief Justice Marshall put it, '[w]here the mind labours to discover the design of the legislature, it seizes every thing from which aid can be derived.' … Legislative history materials are not generally so misleading that jurists should never employ them in a good-faith effort to discern legislative intent. Our precedents demonstrate that the Court's practice of utilizing legislative history reaches well into its past. … We suspect that the practice will likewise reach well into the future.") (internal citations omitted); and *Consumer Product Safety Commission v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980) ("We begin with the familiar canon of statutory construction that the starting point for interpreting a statute is the language of the statute itself. Absent a clearly expressed legislative intention to the contrary, that language must ordinarily be regarded as conclusive.").

FDIC statement accompanying the FAQs notes that, "Despite the existence of the statute, regulations, advisory opinions and the [FDIC's Study on Core Deposits and Brokered Deposits, issued July 2011], questions continue to arise regarding the proper classification of certain types of deposits."[6]

Due to ambiguity in the statute regarding whether particular arrangements are or are not covered by the definition of "deposit broker," it is necessary to consider the intent of the legislature in order to formulate an appropriate interpretation.[7] Shortly after the Senate Banking Committee adopted its version of FIRREA in April 1989, the bill was sent to the Senate floor where Senator Frank H. Murkowski (R-AK) and Senator J. James Exon (D-NE) introduced a brokered deposits amendment that was ultimately enacted in a comparable form in FIRREA.

Senator Murkowski expressed his views on the purpose and intent of this brokered deposits amendment several times (each of which is described below): (1) when initially offered in April 1989; (2) before the House Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs ("House General Oversight Subcommittee") during a hearing on "Insured Brokered Deposits and Federal Depository Institutions" in May 1989; and (3) after enactment of FIRREA, during consideration of a potential amendment to Section 29 before enactment of the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"). [8]

During Senate floor consideration of the brokered deposits amendment offered by Senator Murkowski in April 1989, at the request of both the Chairman and the Ranking Member of the Senate Banking Committee, Senator Murkowski modified the amendment to remove an exception for deposit listing services that had been part of a deposit insurance rule adopted by the FDIC and the Federal Home Loan Bank Board ("FHLBB"),[9] contemporaneously

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[6] See Attachment to FIL-42-2016, Statement of the Director of the Division of Risk Management Supervision, p. 1.

[7] *See, e.g., Yates v. U.S.*, 135 S. Ct. 1074, 1081-1082 (2015) ("Whether a statutory term is unambiguous, however, does not turn solely on dictionary definitions of its component words. Rather, '[t]he plainness or ambiguity of statutory language is determined [not only] by reference to the language itself, [but as well by] the specific context in which that language is used, and the broader context of the statute as a whole.' … Ordinarily, a word's usage accords with its dictionary definition. In law as in life, however, the same words, placed in different contexts, sometimes mean different things.") (internal citations omitted).

[8] FDICIA, Pub. L. No. 102-242, 105 Stat. 2236 (December 19, 1991).

[9] In 1984, the FDIC and the FHLBB had promulgated a joint rule that would have precluded pass-through deposit insurance for deposits obtained through a deposit broker. "Brokered Deposits; Limitations on Deposit Insurance," Federal Deposit Insurance Corporation and Federal Home Loan Bank Board, 49 Fed.

describing the effect to include "listing services, specifically hot money houses in which we share the same concern."[10] Senator Murkowski stated further, "I want to make sure we all understand that we clearly only cover troubled banks and thrifts. There is no limitation on healthy institutions. They can proceed as they should."[11]

After the full Senate passed its version of FIRREA and the House Committee on Banking, Finance, and Urban Affairs reported its version of FIRREA (which included similar amendments on brokered deposits), Senator Murkowski explained the goal and purpose of the amendment before the House General Oversight Subcommittee hearing on brokered deposits in May 1989,

> The goal of this provision is to prevent the flagrant abuse of the deposit insurance system by troubled institutions that take excessive risks and leave the taxpayers to suffer the consequences. By preventing troubled institutions from using brokered deposits – unless permitted to do so by the FDIC – we accomplish this goal and create accountability on the part of the FDIC.[12]
>
> . . .
>
> In summary, this amendment is designed to rein in the abuses of brokered deposits by troubled institutions and to create accountability on the part of Federal regulators. This is a not a blanket prohibition on the use of brokered deposits, but a narrowly drawn provision that specifically targets the most flagrant abusers. A provision intended to protect the taxpayers of this country.[13]

Reg. 13003 (April 2, 1984). The FHLBB administered the Federal Savings and Loan Insurance Corporation which insured the deposits of savings and loan associations.

[10] *See* Congressional Record – Senate, 7142 (April 19, 1989) (emphasis added).

[11] *See id*. (emphasis added).

[12] Testimony of Hon. Frank H. Murkowski, U.S. Senator from the State of Alaska, "Insured Brokered Deposits and Federal Depository Institutions," Hearing before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 7 (May 17, 1989) (emphasis added); *see also id.* at 71 (written testimony). The purpose of this hearing was to update the record on brokered deposits following a prior hearing by the House General Oversight Subcommittee during the 99th Congress on July 16, 1985.

[13] *Id.* at 10-11 (emphasis added); *see also id.* at 74 (written testimony).

Two years after the enactment of FIRREA, Senator Murkowski articulated his view of the reason for having enacted Section 29 during consideration of amendments to Section 29 prior to the enactment of FDICIA. In comments on an amendment to prohibit federal deposit insurance coverage of brokered deposits, Senator Murkowski expressed his view that the flagrant abuses by unhealthy financial institutions that led to the enactment of Section 29 had already been eliminated,

> I think we have a clear case here of an effort to address a problem that really no longer exists. It did exist at one time and it existed in a manner where there was clearly flagrant abuse of the process. The abuse occurred as a consequence of brokered deposits by unhealthy financial institutions...[14]

During the House General Oversight Subcommittee hearing in May 1989, the leaders of the federal banking agencies testified that restrictions on brokered deposits were unnecessary in light of the agencies' supervisory and enforcement authorities and that legislative action on brokered deposits should be deferred pending findings of a proposed study, that was ultimately enacted in FIRREA, on the role of brokered deposits and the need for any limitation on the use of brokered funds. Then-Comptroller of the Currency Robert L. Clarke stated, "[I] do not believe, however, that the proposed prohibition on brokered deposits is the best way to address the problem..." and Governor H. Robert Heller of the Board of Governors of the Federal Reserve System stated, "[w]e believe that it would be more appropriate to defer legislative action at this time and to await the outcome of the anticipated deposit insurance system study, which will include a detailed review of the advantages and disadvantages of brokered deposits." [15]

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[14] *See* Congressional Record – Senate, 33488 (Nov. 21, 1991). Senator Robert Graham (D-FL) offered the amendment under consideration (Amendment No. 1372), which would have prohibited federal deposit insurance of brokered deposits. As mandated by FIRREA, the Department of the Treasury had submitted a report to Congress, including brokered deposits, recommending eliminating deposit insurance coverage for brokered deposits. The report stated, "FIRREA corrected the worst abuses of brokered deposits by curtailing their use by weak banks and thrifts. But the fact remains that brokered deposits allow even healthy institutions to expand their sources of government-guaranteed funding." *See* "Modernizing the Financial System: Recommendations for Safer, More Competitive Banks," Part One: Deposit Insurance and Banking Reforms, pp. 24-25, February 1991. Amendment No. 1372 failed to pass.

[15] *See* Statement of Hon. Robert L. Clarke, Comptroller of the Currency, Hearing on "Insured Brokered Deposits and Federal Depository Institutions," before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 19-22 (May 17, 1989) (*Id*. at 21.); *See also* Statement of Hon. H. Robert Heller, Member, Board of Governors of the Federal Reserve System, Hearing on "Insured Brokered Deposits and Federal Depository Institutions," before the Subcommittee on General Oversight and Investigations of the

The written testimony of then-FDIC Chairman L. William Seidman stated, "In general, we do not find the use of brokered deposits to be a major problem in the banking industry at this time. This is in spite of the fact that brokered deposits usage has increased over the past several years…"[16] Nonetheless, the FDIC Chairman recommended that Congress provide the FDIC with specific authority to regulate the use of brokered deposits at all institutions, not just troubled ones, whenever brokered deposits were being used in an unsafe or unsound manner. However, these recommendations were not adopted and FIRREA was enacted without the specific authority the FDIC requested. Congress instead enacted limited authority for the FDIC to implement "additional" restrictions regarding troubled financial institutions.

The August 1989 Conference Report described the brokered deposits section of FIRREA in relevant part as follows:

> Any insured depository institution which does not meet the minimum capital requirements applicable with respect to such institutions and is thus a 'troubled' institution may not accept funds obtained directly or indirectly by or through any deposit broker for deposit into one or more accounts. A troubled institution is also prohibited from soliciting deposits by offering rates of interest which are significantly higher than the prevailing rates of interest on deposits offered by other insured depository institutions of the same type, *i.e.*, banks or thrifts, in such financial institution's normal market area. This latter provision prohibits the solicitation of deposits by in-house salaried employees through so-called money desk operations.
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> The FDIC is also explicitly authorized to impose by regulation or rule additional restrictions on the acceptance of brokered deposits by troubled institutions. Explicitly providing such authority to the FDIC with regard to troubled institutions is not meant to imply that the Corporation does not already have the

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Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 22-26 (May 17, 1989) (*Id*. at 24-25.)

[16] Written Testimony of L. William Seidman, Chairman, Federal Deposit Insurance Corporation, Hearing on "Insured Brokered Deposits and Federal Depository Institutions," before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., Appendix, 98 (May 17, 1989); *See also* Statement of L. William Seidman, Chairman, Federal Deposit Insurance Corporation, *Id*. at 25 ("We support the idea of giving the regulators the authority to regulate brokered deposits. However, we do not believe legislating specific prohibitions or restrictions on brokered deposits is the best approach.").

> authority to regulate the use of brokered deposits by fully capitalized and under capitalized institutions.[17]
>
> The provision authorizes the FDIC to waive the prohibition on the acceptance of brokered deposits by troubled institutions, but only after a case-by-case review of applications made by such institutions and then only upon a finding that the acceptance of brokered deposits by a given institution does not constitute an unsafe or unsound practice.
>
> The conferees understand that there are situations where brokered deposits are useful and needed particularly for liquidity purposes. Although the provision requires a case-by-case application by a troubled institution for waiver of the prohibition, the [FDIC] may indicate by rulemaking the type or types of situations in which the [FDIC] would consider granting a waiver consistent with the statute. The prohibition, however, could only be waived by a finding that the use of brokered deposits by a particular troubled institution does not constitute an unsafe or unsound practice for it.[18]

Altogether, this legislative history of Section 29 does not appear to support an expansive reading that broadens its scope to cover arrangements outside the plain language and intent expressed by the drafters of the law. Contrary to congressional intent, many of the FDIC's FAQs and staff advisory opinions transform Section 29 from part of a narrowly drawn provision of law that specifically targets the most flagrant abusers of brokered deposits to a significantly more expansive prohibition covering arrangements that do not appear to present risks of flagrant abuses.

Moreover, broad interpretations of the restrictions in Section 29, combined with integrating those interpretations into other rules, may have a significant adverse impact on well capitalized

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[17] This language may be referring to the FDIC's general safety and soundness authority. During the House General Oversight Subcommittee's hearing in May 1989, Representative Floyd Flake (D-NY) asked then-FDIC Chairman Seidman, "If the amendment by Senator Murkowski is passed, it does no more than the things which you now have the authority to do, correct?" The FDIC Chairman responded, "It gives direct authority to do it, otherwise what we do, we have to do in the name of safety and soundness, and prove what we are doing is backed up by a safety and soundness consideration." *See* "Insured Brokered Deposits and Federal Depository Institutions," Hearing before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 36 (May 17, 1989).

[18] Joint Explanatory Statement of the Committee of Conference, H.R. Conf. Rep. No. 222, 101st Cong., 1st Sess. 1989, 402-403 (Aug. 4, 1989) (emphasis added).

insured depository institutions ("IDI") because the amount of brokered deposits can affect the deposit insurance assessment rate of an IDI, and also the liquidity coverage ratio requirement and contingency funding plans for an IDI.[19] These outcomes seem inconsistent with the intent of the legislature not to place limits on brokered funds of healthy institutions.

Further, in issuing the FAQs, the FDIC stated that it plans to continue issuing additional advisory opinions on a case-by-case basis as it has before. Presumably, the FDIC intends the FAQs and staff advisory opinions to explain the FDIC's supervisory expectations and articulate the staff's views on brokered deposits. However, the specificity and number of FAQs and staff advisory opinions may create complexity and opacity contrary to the FDIC's Trust through Transparency initiative[20] and raise serious administrative process questions if the FDIC treats these documents as authoritative rules equivalent to rules promulgated through notice-and-comment rulemaking under the Administrative Procedure Act.

A reasoned understanding of the meaning of Section 29 should be based upon an examination of the language of the law, the context and public policy objectives of the law and the intent of the legislature. This paper describes the statutory framework of Section 29; representative interpretations of the meaning of "deposit broker" and "facilitating the placement of deposits" within Section 29; the pre-FIRREA regulatory and public policy context; the pertinent legislative history of Section 29 during consideration of FIRREA and FDICIA; and additional amendments to Section 29.

I. STATUTORY FRAMEWORK OF SECTION 29

The statutory framework of Section 29 is straightforward. Section 29(a) establishes the general prohibition that an IDI "that is not well capitalized may not accept funds obtained, directly or indirectly, by or through any deposit broker for deposit into 1 or more deposit accounts."[21]

Section 29(b), "Renewals and Rollovers Treated as Acceptance of Funds," specifies that, "[a]ny renewal of an account in a troubled institution and any rollover of any amount on deposit

[19] *See* 12 C.F.R. Part 327 (Assessments); and "Interagency Policy Statement on Funding and Liquidity Risk Management," Office of the Comptroller of the Currency, Federal Reserve System, Federal Deposit Insurance Corporation, Office of Thrift Supervision, and National Credit Union Administration, 75 Fed. Reg. 13656 (March 22, 2010).

[20] Information on the Trust through Transparency initiative is available at https://www.fdic.gov/transparency.

[21] 12 U.S.C. § 1831f(a).

in such account" must be "treated as an acceptance of funds by such troubled institution for purposes of" the general prohibition.[22]

Section 29(c), "Waiver Authority," permits the FDIC to waive the general prohibition on a case-by-case basis upon application from an adequately capitalized IDI if the FDIC finds that the IDI's acceptance of brokered deposits does not constitute an unsafe or unsound practice.[23]

Section 29(d), "Limited Exception for Certain Conservatorships," provides a limited, temporary exception to the prohibition on accepting brokered deposits by an IDI in conservatorship if the FDIC determines that the acceptance of brokered deposits "(1) is not an unsafe or unsound practice; (2) is necessary to enable the [IDI] to meet the demands of its depositors or pay its obligations in the ordinary course of business; and (3) is consistent with the conservator's fiduciary duty to minimize the [IDI's] losses."[24] The acceptance, by an IDI in conservatorship, of funds obtained, directly or indirectly, by or through any deposit broker is limited; effective 90 days after the date on which an IDI is placed in conservatorship, the IDI may not accept such deposits.

As set forth in Section 29(e), "Restriction on Interest Rate Paid," either of these types of IDIs that the FDIC may authorize to accept funds obtained, directly or indirectly, by or through a deposit broker may not pay a rate of interest on such funds that significantly exceeds the rate paid on deposits of similar maturity in the IDI's normal market area for deposits accepted in that area, or the national rate paid on deposits of comparable maturity, as established by the FDIC, for deposits accepted outside the IDI's normal market area.[25]

Adequately capitalized IDIs that do not have a waiver from the FDIC to accept brokered deposits may not offer deposit rates that are "significantly higher" than the "prevailing rates" in the bank's "normal market area" even if the deposits are accepted from outside that area. The interest rate restrictions for less than well-capitalized institutions apply to reciprocal deposits that are excepted from treatment as brokered deposits.[26]

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[22] *Id*. at § 1831f(b).

[23] *Id*. at § 1831f(c).

[24] *Id*. at § 1831f(d).

[25] *Id.* at § 1831f(e).

[26] *See* Economic Growth, Regulatory Relief, and Consumer Protection Act, Pub. L. 115-174 § 202 (May 24, 2018); and "Limited Exception for a Capped Amount of Reciprocal Deposits From Treatment as Brokered Deposits," FDIC, 84 Fed. Reg. 1346 (Feb. 4, 2019).

Section 29(f), "Additional Restrictions," authorizes the FDIC to "impose, by regulation or order, such additional restrictions on the acceptance of brokered deposits by any [IDI] as the [FDIC] may determine to be appropriate."[27]

Section 29(g), "Definitions Relating to Deposit Broker," defines the term "deposit broker" as used in the general prohibition to mean "[a]ny person engaged in the business of placing deposits, or facilitating the placement of deposits, of third parties with [IDIs] or the business of placing deposits with [IDIs] for the purpose of selling interests in those deposits to third parties" and "an agent or trustee who establishes a deposit account to facilitate a business arrangement with an [IDI] to use the proceeds of the account to fund a prearranged loan."[28]

The definition of deposit broker is subject to nine statutory exclusions, such as for an IDI with respect to funds placed with that IDI, for an employee of an IDI with respect to funds placed with the employing IDI, and for a trust department of an IDI "if the trust in question has not been established for the primary purpose of placing funds with" IDIs.[29] The definition of deposit broker includes any IDI that is not well capitalized, and any employee of such an IDI, "which engages, directly or indirectly, in the solicitation of deposits by offering rates of interest which are significantly higher than the prevailing rates of interest on deposits offered by other" IDIs in that IDI's normal market area.[30]

Section 29(h), "Deposit Solicitation Restricted," prohibits an IDI that is undercapitalized from soliciting deposits by offering rates of interest that are significantly higher than the prevailing rates on insured deposits in the undercapitalized IDI's normal market area or in the market area where such deposits would otherwise be accepted.[31]

Additionally, Congress recently added Section 29(i), "Limited Exception for Reciprocal Deposits", to permit well capitalized and well rated IDIs to exclude a limited amount of

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[27] 12 U.S.C. § 1831f(f).

[28] *Id.* at § 1831f(g)(1).

[29] *See id.* at § 1831f(g)(2). Section 29 specifies six additional exclusions from the definition of the term "deposit broker" and the FDIC has adopted a tenth exclusion by rule for deposits placed by an IDI "acting as an intermediary or agent of a U.S. government department or agency for a government sponsored minority or women-owned depository institution deposit program." 12 C.F.R. § 337.6(a)(5)(ii)(J).

[30] 12 U.S.C. § 1831f(g)(3).

[31] *Id.* at . § 1831f(h).

reciprocal deposits from treatment as brokered deposits.[32] Specifically, under the reciprocal deposits exclusion, well capitalized and well rated IDIs are not required to treat reciprocal deposits as brokered deposits up to the lesser of 20 percent of total liabilities, or $5 billion.

In summary, the statutory framework of Section 29 provides the following key elements regarding the acceptance of brokered deposits:

(1) A well-capitalized IDI may accept brokered deposits and may pay any rate of interest on any deposit without restriction.
(2) An IDI that is adequately capitalized may accept brokered deposits on a case-by-case basis only upon application if the FDIC issues a waiver.
(3) The FDIC can authorize the acceptance of brokered deposits by an IDI in conservatorship for a limited period of time.
(4) No IDI in any other capital classification may accept brokered deposits.
(5) An IDI that is less than well-capitalized cannot pay a rate of interest on deposits that significantly exceeds its normal market area or the national rate as established by the FDIC through rules.

II. REPRESENTATIVE INTERPRETATIONS OF SECTION 29

Although FIRREA did not require the FDIC to adopt implementing rules on brokered deposits, the FDIC promulgated an interim rule several months after enactment of FIRREA followed by a final rule the following year.[33] The substance of these rules did not vary appreciably from the statutory language of Section 29.

Since FIRREA was enacted, staff of the FDIC has issued more than 80 separate and distinct public advisory opinions and an unknown number of non-public advisory opinions regarding brokered deposits. The FDIC has explained that the determination of whether a party is a deposit broker is "fact specific" and "considered on a case-by-case basis."[34] There are more

[32] *See* note 26, supra. IDIs that are not both well capitalized and well rated may also exclude reciprocal deposits from their brokered deposits under certain circumstances.

[33] *See* 54 Fed. Reg. 51012 (Dec. 12, 1989) (interim rule); and 55 Fed. Reg. 39135 (Sept. 25, 1990) (final rule). Following enactment of FDICIA, the FDIC issued additional rules required to carry out the interest rate restrictions.

[34] *See* FDIC FIL-42-2016, A5. In the FDIC statement accompanying FIL-42-2016, on p. 2, the Director of the Division of Risk Management Supervision noted, "The FDIC recognizes that brokered

advisory opinions that interpret the meaning of the statutory definition of "deposit broker" than opinions that interpret any other provision of Section 29. Although the FDIC's rule on brokered deposits closely tracks the statutory language, the staff advisory opinions consistently interpret the applicability of Section 29 broadly.

Prior to the enactment of Section 29, the FDIC and the FHLBB had promulgated a joint rule that limited deposit insurance for deposits obtained through a deposit broker.[35] Although this joint FDIC and FHLBB rule was overturned by judicial ruling,[36] the definition of the term "deposit broker" adopted in the joint FDIC and FHLBB rule formed the basis of the definition of this term in Section 29.[37]

Section 29 defines the term "deposit broker" to mean,

> (A) any person engaged in the business of placing deposits, or facilitating the placement of deposits, of third parties with [IDIs] or the business of placing deposits with [IDIs] for the purpose of selling interests in those deposits to third parties; and
> (B) an agent or trustee who establishes a deposit account to facilitate a business arrangement with an [IDI] to use the proceeds of the account to fund a prearranged loan.[38]

This definition is subject to nine statutory exclusions and one additional regulatory exclusion.[39] As with other provisions of the FDIC's rule on brokered deposits, the definition of "deposit broker" in the FDIC's rule aligns closely with the statutory definition.[40]

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deposit determinations are fact-specific and influenced by a number of factors. Thus, the FDIC considers these determinations on a case-by-case basis…" *See* note 6, supra.

[35] *See* "Brokered Deposits; Limitations on Deposit Insurance," Federal Deposit Insurance Corporation and Federal Home Loan Bank Board, 49 Fed. Reg. 13003 (April 2, 1984) (Final Rule); and "Brokered Deposits; Limitations on Deposit Insurance," Federal Deposit Insurance Corporation and Federal Home Loan Bank Board, 49 Fed. Reg. 2787 (January 23, 1984) (Proposed Rulemaking).

[36] *See* FAIC Sec., Inc. v. United States, 595 F. Supp. 73 (D.D.C. 1984), *aff'd*, 768 F.2d 352 (D.C. Cir. 1985).

[37] *See* 49 Fed. Reg. at 13010; and 12 U.S.C. § 1831f(g).

[38] 12 U.S.C. § 1831f(g)(1).

[39] *See id*. at § 1831f(g)(2) and 12 C.F.R. § 337.6(a)(5).

[40] *See* 12 C.F.R. § 337.6(a)(5).

The definition of the term "deposit broker" is a key element of Section 29 because the statute does not define what constitutes a brokered deposit. Possibly for this reason, staff of the FDIC has issued more than 60 public advisory opinions that interpret the words Congress used in the definition of the term "deposit broker." These advisory opinions predominantly construe the definition of "deposit broker" expansively and the exceptions to the definition of "deposit broker" narrowly.[41] Through the years, staff of the FDIC has regularly characterized as "broad" both the statutory definition and the FDIC's interpretations of the term "deposit broker." As an example, staff of the FDIC has indicated that "[t]he FDIC has interpreted this definition [of deposit broker] broadly to include companies or other entities that refer clients or other persons to an [IDI] for banking services."[42]

Staff of the FDIC has adopted interpretations of the phrase "facilitating the placement of deposits," as appears within the definition of "deposit broker," that construe this phrase broadly. These interpretations cover a vast array of actions taken by third parties to connect IDIs with potential depositors and consider factors that are not present in the statutory language of the definition of the term "deposit broker," including fee structure, any connection between the amount of fees and the amount of deposits, the purpose of the fees and the degree of involvement by the third party.[43] The FDIC employs the definition of the term "facilitate" found in Black's Law Dictionary – "to free from difficulty or impediment; to make easy or less difficult" – as the "common usage" meaning of the term in the marketplace, finding that many acts that make it easier to place funds with an IDI constitute facilitating the placement of deposits and make the entity a deposit broker.[44]

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[41] *See, e.g.*, FDIC Advisory Opinion No. 15-01 (Apr. 16, 2014) ("The FDIC has interpreted this ['deposit broker'] definition broadly"); No. 94-15 (Mar. 16, 1994) ("We believe Congress' intent in defining 'deposit broker' so broadly was to control the flow of brokered funds to all but the best capitalized depository institutions insured by the FDIC."); No. 93-71 (Oct. 1, 1993) ("The statutory definition of 'deposit broker' is broad. The FDIC has interpreted the definition to encompass numerous activities in an effort to discourage the flow of deposits to undercapitalized institutions."); No. 93-50 (July 27, 1993) ("…the term 'deposit broker' is broadly defined"); No. 93-14 (Feb. 24, 1993) ("This definition is quite broad and unless the activity in question comes within one of the statutory or regulatory exclusions, the FDIC must and will consider the activity deposit brokering."); and No. 92-88 (Dec. 10, 1992) ("…the definition of deposit broker is very broad.").

[42] *See* "Question regarding whether Financial Firms that Refer Clients to a Bank Qualify as Deposit Brokers," FDIC Advisory Opinion No. 15-01 (April 16, 2014) (emphasis added).

[43] *See* FDIC FIL-42-2016, A5, referencing FDIC Advisory Opinion No. 92-79 (November 10, 1992) and FDIC Advisory Opinion No. 94-15 (March 16, 1994); and *See, e.g.*, FDIC Advisory Opinion No. 16-01 (May 19, 2016) ("The term 'facilitating the placement of deposits' is interpreted broadly.").

[44] *See* FDIC Advisory Opinion 94-15 (March 16, 1994); FDIC Advisory Opinion 92-79 (November 10, 1994).

The breadth of the interpretations in the FAQs and staff advisory opinions enable the conclusion that a party may be facilitating the placement of deposits, and therefore, may be a deposit broker, if the party "takes any actions that connect an [IDI] with depositors or potential depositors."[45]

FDIC staff has also advised that an insurance agent, lawyer, or accountant who refers clients to a bank is a deposit broker due to "facilitating the placement of deposits" and on later reconsideration, clarified the advice, explaining that informal referrals are not brokered, but if, for example, an accountant refers clients to a bank, and the accountant has entered into a written agreement with the bank for the referral of depositors, or receives fees from the bank, the FDIC would consider the deposits to be brokered.[46] Similarly, FDIC staff has concluded that if an individual or a group endorses a bank in the individual's or group's promotional materials, the individual or group providing the endorsement would be a deposit broker and the deposits would be brokered.[47]

In contrast to these expansive interpretations of the phrase "facilitating the placement of deposits" within the definition of "deposit broker," many FDIC staff advisory opinions construe one of the broadest statutory exclusions from the definition of "deposit broker" narrowly. The "primary purpose" exclusion from the definition of "deposit broker" excludes from the definition "an agent or nominee whose primary purpose is not the placement of funds with depository institutions."[48]

FDIC staff has expressed the view that the primary purpose exclusion does not exclude a party simply because the placement of deposits is incidental to its business.[49] In interpreting this exclusion, the FDIC considers "the reason or intent of the third party when acting as agent or nominee in placing the deposits, as well as other factors which might indicate whether the third party agent is incentivized to place deposits at the IDI" in determining whether the party is a

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[45] *See* FDIC FIL-42-2016, B2 (emphasis added), referencing FDIC Advisory Opinion No. 92-79 (November 10, 1992).

[46] *See* FDIC FIL-2-2015, B6, and FDIC FIL 42-2016, B6, referencing FDIC Advisory Opinion No. 15-04 (February 4, 2015).

[47] *See* FDIC FIL 42-2016, B8, referencing FDIC Advisory Opinion No. 93-71 (October 1, 1993).

[48] 12 U.S.C. § 1831f(g)(2)(I) (emphasis added).

[49] *See* "'Primary Purpose' Exclusion From Definition of Deposit Broker," FDIC Advisory Opinion No. 90-21 (May 29, 1990).

deposit broker.[50] The FDIC indicates that, "In interpreting the application of the primary purpose exception, the FDIC frequently relies upon information provided by the requesting party, and other available information."[51] Contrary to these interpretations, the plain language of the primary purpose exclusion in Section 29 does not refer to any additional factors, focusing instead only on the primary purpose for placing the deposits.

Further, although the FDIC has incorporated many staff interpretations into the FAQs,[52] the granularity and number of interpretations of the term "deposit broker" make the definition opaque, complex and uncertain, undermining a fundamental premise of the FDIC's Trust through Transparency initiative to build a foundation of trust and accountability.

III. PRE-FIRREA REGULATORY AND PUBLIC POLICY CONTEXT

In the years prior to enactment of FIRREA, the federal financial institutions regulatory agencies, financial services industry and Congress were beginning to examine the use of brokered deposits because IDIs were relying on brokered deposits as funding sources with increasing frequency throughout the 1980s.

In the mid-1980s, the FDIC and the FHLBB were so concerned about the use of brokered deposits that they jointly adopted a rule restricting pass-through deposit insurance for deposits obtained through a deposit broker.[53] In subsequent litigation, the U.S. District Court for the District of Columbia enjoined the agencies from implementing the rule on the ground that the rule exceeded the agencies' statutory authority, and on appeal, the U.S. Court of Appeals for the District of Columbia Circuit affirmed the District Court's decision.[54]

During the pendency of the rulemaking and litigation concerning the joint FDIC and FHLBB rule, several congressional hearings were held specifically to examine issues related to the use

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[50] *See* "Unsafe and Unsound Banking Practices: Brokered Deposits and Interest Rate Restrictions," Federal Deposit Insurance Corporation, 84 Fed. Reg. 2366, 2372 (Feb. 6, 2019).

[51] *See* FDIC FIL 42-2016, E9.

[52] *See* FDIC FIL 42-2016, which supersedes FIL-2-2015 (Jan. 5, 2015) and FIL-51-2015 (Nov. 13, 2015).

[53] *See* "Brokered Deposits; Limitations on Deposit Insurance," Federal Deposit Insurance Corporation and Federal Home Loan Bank Board, 49 Fed. Reg. 13003 (April 2, 1984) (Final Rule). The vote of the FDIC Board of Directors was not unanimous as the then-Comptroller of the Currency, C.T. Conover, had voted against the rule. The proposed rulemaking, "Brokered Deposits; Limitations on Deposit Insurance," was published on January 23, 1984 at 49 Fed. Reg. 2787.

[54] *See* note 36, *supra*.

of brokered deposits.[55] In 1983, the Subcommittee on Financial Institutions, Regulation and Insurance of the Committee on Banking, Finance, and Urban Affairs of the House of Representatives ("Financial Institutions Subcommittee") held a hearing that addressed the use of brokered deposits.[56] During this hearing, in response to questions from Representative Bruce Vento (D-MN) concerning the magnitude of exposure of the deposit insurance funds to brokered deposits, then-FDIC Chairman William Isaac stated,

> The failed and problem banks are the ones we are most concerned about. . . .I don't intend to affect any banks other than problem banks. Through our supervisory efforts, we are going to be going directly to the problem banks. Through our insurance changes, we would hope to encourage money to go where it should go. Right now our rules are encouraging money to go to failing banks.[57]

While the views of the FDIC and the FHLBB were aligned regarding limiting pass-through federal deposit insurance coverage on brokered deposits, the views of the other federal financial institutions regulatory agencies and the Department of the Treasury differed regarding the need for the joint FDIC and FHLBB rule and how to carry out effective regulatory oversight of the use of brokered funds.

For example, in his written statement for the Financial Institutions Subcommittee hearing record, then-Comptroller of the Currency C.T. Conover stated, "In the near term, I believe that we can and should rely on our supervisory capabilities to deal with problems raised by deposit brokering. Increased reliance on examination and reporting of brokered funds should be adequate to monitor and control on a case-by-case basis the use of brokered funds by individual

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[55] *See* "Proposed Restrictions on Money Brokers," Hearing before the Subcommittee on Commerce, Consumer and Monetary Affairs of the House Committee on Government Operations, 98th Cong., 2nd Sess. (Mar. 14, 1984); "Brokered Deposits," Hearing before the Subcommittee on Financial Institutions and Consumer Affairs of the Senate Committee on Banking, Housing and Urban Affairs, 99th Cong., 1st Sess. (June 5, 1985); and "Impact of Brokered Deposits on Banks and Thrifts: Risks Versus Benefits," Hearing before the Subcommittee on General Oversight and Investigations of the House Committee on Banking, Finance and Urban Affairs, 99th Cong., 1st Sess. (July 16, 1985).

[56] *See* "The Demand Deposit Equity Act of 1983," Hearings before the Subcommittee on Financial Institutions Supervision, Regulation and Insurance of the House Committee on Banking, Finance and Urban Affairs, 98th Congress, 1st Sess., on H.R. 3535 (A bill to authorize depository institutions to offer interest-bearing demand deposits) and H.R. 3895 (A bill to permit the payment of interest on demand deposits held by depository institutions) (September 28; October 4, 6, and 27, 1983).

[57] *Id*. at 460.

institutions."[58] The Honorable Thomas J. Healey, Assistant Secretary for Domestic Finance, Department of the Treasury encouraged further study and monitoring of brokered deposits to better understand the steps that should be taken.[59]

Mirroring the disparate views of the federal financial institutions regulatory agencies, in Congress there was similarly no single prevailing view of the use of brokered deposits. In 1984, and again in 1986, the House Subcommittee on Government Operations issued reports regarding brokered deposits. The 1984 report concluded, in relevant part, that,

> (1) "Forceful use of their existing supervisory powers on a case-by-case basis can be more effectively used by the agencies as a principal mode of attack on the problems of improper lending by rapidly growing problem institutions, including those that rely on brokered funds";
> (2) "Brokered deposits were not a significant source of deposit growth for the great majority of rapidly growing problem institutions during the period from December 31, 1983, through March 31, 1984"; and
> (3) "Eliminating the insurance coverage for brokered funds would not be likely to stimulate increased market discipline by brokers and depositors, as intended by the agencies."[60]

Similarly, the 1986 report concluded, "While supervisory restrictions limiting the access of individual problem banks and thrifts to brokered funds, applied on a case-by-case basis, may be an appropriate supervisory tool…neither the recent bank and thrift failures involving brokered funds nor any other recent information on the role of insured brokered funds in troubled banks and thrifts demonstrates any need to prohibit or tightly restrict all institutions' access to such funds."[61]

During this time, several bills were introduced in Congress that would have placed limits on the use of brokered deposits, measured against an IDI's level of capital, and at the same time, authorized the federal deposit insurers to permit an IDI to maintain greater levels of brokered

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[58] *Id*. at 431-432.

[59] *See id*. at 21.

[60] *See* "Federal Regulation of Brokered Deposits in Problem Banks and Savings Institutions," House Committee on Government Operations, 98th Cong., 2nd Sess., H. Rept. 98-1112, 9-10 (Sept. 28, 1984).

[61] *See* "Federal Regulation of Brokered Deposits: A Followup Report," House Committee on Government Operations, 99th Cong., 2nd Sess., H. Rept. 99-676, 13 (July 16, 1986).

deposits upon application. Some of these bills contain elements of Section 29 as later enacted in FIRREA.

In the House of Representatives, the Broker Deposit Limitation Act, H.R. 5913 (1984), introduced by Representative Robert Garcia (D-NY), would have prohibited an IDI with unimpaired capital and surplus of less than three percent of its total liabilities from accepting any short-term brokered deposits, and would have authorized the deposit insurer to permit an IDI, upon application, to maintain short-term brokered deposits in greater amounts.[62]

In the Senate, two bills – (1) the Financial Services Competitive Equity Act, S. 2851 (1984), introduced by Senator E.J. (Jake) Garn (R-UT), then-Chairman of the Senate Committee on Banking, Housing and Urban Affairs, and (2) the Brokered Deposits Act of 1984, S. 2679, introduced by Senator Alfonse D'Amato (R-NY) – would have prohibited the FDIC from promulgating rules which would have the effect of restricting deposit insurance available to a person for deposits or accounts placed through a deposit broker.[63] Both of these bills would have prohibited an IDI from accepting or maintaining short-term insured accounts placed through a deposit broker in excess of the lesser of 200 percent of the institution's unimpaired capital and unimpaired surplus, or 15 percent of total deposits.[64]

Like the House Broker Deposit Limitation Act (H.R. 5913), the Senate Brokered Deposits Act (S. 2679) would have prohibited an IDI that had unimpaired capital and unimpaired surplus in an amount less than three percent of its liabilities from having any insured accounts placed by or through a deposit broker. Similar to the House bill (H.R. 5913), the Senate bill (S. 2679) would have authorized the deposit insurer to permit an IDI, upon notice and application, to maintain short-term brokered deposits in greater amounts, giving equal weight to both competitive factors and safety and soundness considerations.

The brokered deposit limitations in these bills were targeted to IDIs with lower amounts of capital and these bills contained a version of the process for submitting an application to the deposit insurer as appears in FIRREA.

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[62] *See* H.R. 5913 (1984) (referred to the Subcommittee on Financial Institutions Supervision, Regulation and Insurance following introduction in the House of Representatives).

[63] *See* S. 2851 (1984) (passed the Senate by a recorded vote of 89 to 5) and S. 2679 (1984) (referred to the Committee on Banking following introduction in the Senate).

[64] *See id.*

In 1988 and in early 1989, Senator Murkowski introduced two separate bills that would have limited federal deposit insurance for funds deposited in a troubled institution by or through a deposit broker. Senator Murkowski intended these bills to restore provisions of the rule promulgated by the FDIC and FHLBB in 1984.[65] As described below, however, the bill Senator Murkowski introduced as part of the Senate's version of FIRREA did not restrict federal deposit insurance coverage of brokered deposits.

IV. LEGISLATIVE HISTORY OF SECTION 29 AND FIRREA

FIRREA was enacted in the wake of the savings and loan crisis of the 1980s to "begin a new era for insured institutions and their regulators."[66] As evident from congressional hearings and testimony of the federal financial institutions regulators during consideration of FIRREA, brokered deposits were viewed both positively and negatively.

This dual view of brokered deposits is clear in testimony on "Insured Brokered Deposits and Federal Depository Institutions" delivered by then-FDIC Chairman L. William Seidman before the House General Oversight Subcommittee on May 17, 1989, in which he described the FDIC's views of brokered deposits,

> In our view, brokered deposits have both negative and positive aspects. On the negative side, they have been used to fund excessive growth and imprudent, even fraudulent, loans or other investments. This has led to the failure of a number of banks and has increased our costs in those cases. From a failure resolution standpoint, the presence of long-term, high-cost brokered deposits in a failing bank tends to reduce its franchise value. This makes it more difficult to satisfy our cost test for arranging a purchase and assumption transaction – our preferred method of resolving failed banks.
>
> On the positive side, brokered deposits can represent a valuable liquidity management tool for all financial institutions, including undercapitalized

[65] *See, e.g.*, Congressional Record-Senate, 21618 (Aug. 10, 1988) (regarding S. 2722, Brokered Deposits Act of 1988, "The bill will restore a similar 1984 FDIC and Federal Home Loan Bank Board regulation that was later overruled in a Federal court case as an invalid exercise of statutory authority"); and Congressional Record-Senate, 2088 (Feb. 9, 1989) (regarding S. 398, Brokered Deposits Act of 1988: "My bill seeks to restore the provisions of a similar 1984 FDIC and Federal Home Loan Bank Board regulation that was subsequently overruled in a Federal court case as an invalid exercise of authority."). S. 2722 (1988) and S. 398 (1989) were referred to the Senate Banking Committee, and were not enacted into law.

[66] H.R. Rep. 101-54 , 101st Cong., 1st Sess., 291 (May 16; June 1, 8, 1989).

> ones, and in some markets may even represent a low-cost funding option. In the current savings and loan situation, the controlled use of brokered deposits has been an important tool in handling some of the liquidity pressures that have arisen. Without the use of brokered deposits to allow continued funding for liquidity purposes, the thrift crisis would be much worse. Consequently, we must not foreclose the use of brokered deposits to undercapitalized institutions in all circumstances. Brokered deposits should be denied to undercapitalized institutions only when used as a means to grow and not when needed as a continued source of liquidity.[67]

In the face of competing views of brokered deposits and the dire circumstances of the savings and loan industry in particular, both chambers of Congress passed legislative language to address the use of brokered deposits.

Initially, the Senate Banking Committee adopted a version of FIRREA, S. 774, introduced by the Chairman of the Committee, Donald Riegle (D-MI), on April 13, 1989 that did not contain any provisions prohibiting the use of brokered deposits. However, a short time later, on April 19, 1989, Senator Murkowski and Senator Exon offered a floor amendment (No. 58) to limit the use of brokered deposits by financially troubled institutions, and the amendment unanimously passed the full Senate by voice vote as part of S. 774.[68]

The operative provisions of the Senate floor amendment were similar to the operative provisions of Section 29 as adopted in FIRREA. These provisions read,

> SEC. 30. BROKERED DEPOSITS.
> (a) In General. – A troubled institution may not accept funds deposited into one or more deposit accounts by or through a deposit broker.
> (b) Grandfathered Accounts. – The prohibition contained in subsection (a) shall not apply to any account opened before the effective date of [FIRREA] unless such account has been added to or renewed after the effective date of such Act.
> (c) Waiver Authority. – The Corporation is authorized, on a case-by-case basis, and upon application by an insured financial institution,

[67] Testimony of L. William Seidman, Chairman, Federal Deposit Insurance Corporation, Hearing on "Insured Brokered Deposits and Federal Depository Institutions," before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., Appendix, 97 (May 17, 1989).

[68] *See* Congressional Record – Senate, 7140-7142 (April 19, 1989).

> to waive the applicability of subsections (a) and (b) upon a finding that the acceptance of such deposits does not constitute an unsafe or unsound practice.[69]

Senator Murkowski's original amendment included a definition of "deposit broker" that was drawn from the joint FDIC and FHLBB rule restricting pass-through deposit insurance for brokered deposits that had been invalidated by the Court of Appeals for the D.C. Circuit as exceeding the agencies' statutory authority. At the request of both Senate Banking Committee Chairman Riegle and Ranking Member Garn, Senator Murkowski removed from the amendment an exception for deposit listing services that had been part of the FDIC and FHLBB's rule, contemporaneously describing the effect as "basically includ[ing] more people in the definition of deposit broker, now it includes listing services, specifically hot money houses in which we share the same concern."[70] At the same time, Senator Murkowski stated further, "I want to make sure we all understand that we clearly only cover troubled banks and thrifts. There is no limitation on healthy institutions. They can proceed as they should."[71]

Representative Stephen L. Neal (D-NC) offered a similar amendment on brokered deposits that was included in the House version of FIRREA, H.R. 1278. As passed by the House Banking Committee on May 2, 1989, the House version of FIRREA, H.R. 1278, provided that troubled institutions may not increase brokered funds above current levels and like the Senate version of FIRREA, S. 774, the House bill allowed the deposit insurer to waive this limitation upon determining that the acceptance of brokered funds did not constitute an unsafe or unsound practice.

At a hearing on "Insured Brokered Deposits and Federal Depository Institutions," convened by the House General Oversight Subcommittee on May 17, 1989, Senator Murkowski testified concerning the brokered deposits amendment in S. 774,

> Under the amendment, Mr. Chairman, banks and thrifts that do not meet minimum capital requirements would be prohibited from using federally insured brokered deposits. These institutions would have an option of making an application to the FDIC to waive this prohibition.

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[69] *See id.* at 7142.

[70] *See id.*

[71] *See id.*

> A waiver would be available if the FDIC makes a determination, in advance, that the use of brokered deposits by that particular institution does not constitute an unsound banking practice.
>
> The purpose of the waiver clause is to give the FDIC the discretion to permit the use of brokered deposits, based on the specific facts of a specific case. When used by sound institutions in a commercially reasonable manner, brokered deposits can be beneficial.
>
> The goal of this provision is to prevent the flagrant abuse of the deposit insurance system by troubled institutions that take excessive risks and leave the taxpayers to suffer the consequences. By preventing troubled institutions from using brokered deposits—unless permitted to do so by the FDIC—we accomplish this goal and create accountability on the part of the FDIC.[72]

Senator Murkowski concluded the opening statement of his testimony,

> In summary, this amendment is designed to rein in the abuses of brokered deposits by troubled institutions and to create accountability on the part of Federal regulators. This is not a blanket prohibition on the use of brokered deposits, but a narrowly drawn provision that specifically targets the most flagrant abusers. A provision intended to protect the taxpayers of this country.[73]

During the House General Oversight Subcommittee hearing, Senator Murkowski addressed the concerns that led him to introduce the brokered deposits amendment adopted by the Senate. Representative Peter Hoagland (D-NE) asked Senator Murkowski the question,

> Is it your principal concern that in a sense we ought to have a way of cooling down the situation so that if you have a troubled thrift that is willing to offer unprofitably high interest rates, they should not have a

[72] Testimony of Hon. Frank H. Murkowski, U.S. Senator from the State of Alaska, "Insured Brokered Deposits and Federal Depository Institutions," Hearing before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 7 (May 17, 1989).

[73] *See id*. at 9-10.

> mechanism for getting so much money in the door so quickly that you just put more taxpayer dollars in jeopardy through the insurance fund? Does that oversimplify your concern?[74]

Senator Murkowski responded, "It doesn't oversimplify but it leads to one more consideration and that is the role of the regulator during this process…"[75]

Representative Doug Barnard (D-GA) asked Senator Murkowski, "Are you concerned restrictions on brokered funds could easily be circumvented by deposits or institutions which could solicit funds through a money desk or national advertisements? What can a broker do that the institutions themselves now cannot do?"[76]

Senator Murkowski responded,

> …The bottom line is still not where the funds come from, but in the manner in which the process is expedited, the broker serves as a catalyst to collect and redistribute the funds. It can be done directly….I think the question isn't where the money comes from, so much as the reality if we are taking advantage of a federally-insured program that wasn't designed specifically for this kind of an opportunity that the sophisticated brokerage houses have seen available to them to enable institutions that are troubled and have to pay a high rate of interest to go out and solicit.[77]

During the House General Oversight Subcommittee hearing, the heads of the federal banking agencies uniformly expressed concerns regarding legislative restrictions on brokered deposits. Then-Comptroller of the Currency Robert L. Clarke stated, "Mr. Chairman, I believe the prohibitions on brokered deposits contemplated by [the House version of FIRREA] H.R. 1278 are unnecessary, and I believe that, if enacted, they would be ineffective. Furthermore, if enacted, in their present form, I believe they have the potential to be harmful" and then-Governor of the Federal Reserve System H. Robert Heller stated, "The administration's legislative proposal to address the thrift industry's problems calls for a study that would, among other things, review the role of brokered deposits and the need for any limitation on the use of

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[74] *Id.* at 13.

[75] *Id.*

[76] *Id.* at 17.

[77] *Id.*

these funds. Thus, while the Board shares the concern of Congress over the use of brokered deposits by troubled institutions, we believe that it would be more appropriate at this time to defer legislative action on brokered deposits pending the findings of the anticipated study." [78]

The FDIC Chairman's written testimony stated, "In general, we do not find the use of brokered deposits to be a major problem in the banking industry at this time."[79] Nonetheless, the FDIC Chairman's testimony recommended that Congress provide the FDIC with specific authority to regulate the use of brokered deposits at all institutions, not just troubled institutions, whenever brokered deposits were being used in an unsafe or unsound manner and the FDIC Chairman provided two sets of legislative language that differed from the language approved in both the House and Senate bills.[80]

The amendment described as FDIC Alternative 1 would have prohibited a troubled institution from increasing the amount of funds deposited by a deposit broker beyond the amount of net interest credited, unless the FDIC determined otherwise, by regulation or order, and would have granted the FDIC the authority to waive the applicability of these provisions altogether. FDIC Alternative 1 would also have authorized the FDIC, by regulation or order, to grant additional exemptions or impose additional restrictions on the acceptance or use of brokered deposits by troubled institutions. The amendment described as FDIC Alternative 2 would have provided the FDIC authority "by regulation or order" to "prohibit or limit" the acceptance of

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[78] *See* Statement of Hon. Robert L. Clarke, Comptroller of the Currency, Hearing on "Insured Brokered Deposits and Federal Depository Institutions," before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 19-22 (May 17, 1989) (*Id*. at 21.); *See also* Statement of Hon. H. Robert Heller, Member, Board of Governors of the Federal Reserve System, Hearing on "Insured Brokered Deposits and Federal Depository Institutions," before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 22-26 (May 17, 1989) (*Id*. at 24-25.) *See also* note 15, *supra*.

[79] Testimony of L. William Seidman, Chairman, Federal Deposit Insurance Corporation, "Insured Brokered Deposits and Federal Depository Institutions," Hearing before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 98 (May 17, 1989).

[80] *Id*. at 25-26 and 40-41 (Rep. Hoagland: "Chairman Seidman, you suggest we take a different approach in the bill. You outline in some detail the kind of amendment you would suggest replace the House and Senate versions. Would you mind having that language prepared and providing it to the committee?" Chairman Seidman: "We will be happy to do that."). *Compare* S. 774, Engrossed in Senate version, § 226 (Brokered Deposits) (Apr. 19, 1989); H.R. 1278, Engrossed in House version, § 222 (Brokered Deposits) (June 15, 1989); and FDIC Alternatives 1 and 2 in Appendix to "Insured Brokered Deposits and Federal Depository Institutions," Hearing before the Subcommittee on General Oversight and Investigations of the Committee on Banking, Finance and Urban Affairs, House of Representatives, 101st Congress, 1st Sess., 189-190 (May 17, 1989).

brokered deposits for any IDI. Neither of these alternatives was enacted in FIRREA as proposed; instead, Congress enacted limited authority for the FDIC to implement "additional" restrictions regarding troubled financial institutions.

The Conference Report summarized the brokered deposits section of FIRREA in relevant part as follows:

> Any [IDI] which does not meet the minimum capital requirements applicable with respect to such institutions and is thus a 'troubled' institution may not accept funds obtained directly or indirectly by or through any deposit broker for deposit into one or more accounts. A troubled institution is also prohibited from soliciting deposits by offering rates of interest which are significantly higher than the prevailing rates of interest on deposits offered by other [IDIs] of the same type, i.e., banks or thrifts, in such financial institution's normal market area. This latter provision prohibits the solicitation of deposits by in-house salaried employees through so-called money desk operations.
>
> The FDIC is also explicitly authorized to impose by regulation or rule additional restrictions on the acceptance of brokered deposits by troubled institutions. Explicitly providing such authority to the FDIC with regard to troubled institutions is not meant to imply that the Corporation does not already have the authority to regulate the use of brokered deposits by a given institution by fully capitalized and under capitalized institutions.[81]
>
> The provision authorizes the FDIC to waive the prohibition on the acceptance of brokered deposits by troubled institutions, but only after a case-by-case review of applications made by such institutions and then only upon a finding that the acceptance of brokered deposits does not constitute an unsafe or unsound practice.
>
> The conferees understand that there are situations where brokered deposits are useful and needed particularly for liquidity purposes. Although the provision requires a case-by-case application by a troubled institution for waiver of the prohibition, the [FDIC] may indicate by rulemaking the type or types of situations in which the [FDIC] would consider granting a waiver consistent with

[81] This language may be referring to the FDIC's general safety and soundness authority, which requires a safety and soundness determination by the FDIC. *See* note 17, *supra*.

the statute. The prohibition, however, could only be waived by a finding that the use of brokered deposits by a particular troubled institution does not constitute an unsafe or unsound practice for it.[82]

V. LEGISLATIVE HISTORY OF SECTION 29 AND FDICIA

FDICIA was enacted into law two years after the enactment of FIRREA. FDICIA amended Section 29 of FIRREA by replacing the term "troubled institution" (defined as not meeting minimum capital ratios) with references to new capital classifications created as part of the framework of prompt corrective action ("PCA") also established in FDICIA. PCA classifies IDIs into five categories according to their regulatory capital ratios and provides for increasingly more stringent regulatory actions as capital ratios deteriorate.[83]

In FDICIA, Congress amended the threshold for application of the general prohibition in Section 29 to comport with the new PCA capital classifications. Specifically, Congress changed the general threshold for prohibiting the acceptance of brokered deposits from a "troubled institution" to an IDI that is not in the highest capital classification under PCA, "well capitalized."[84] Additionally, FDICIA authorized the FDIC, by application on a case-by-case basis, to grant a waiver from this general prohibition to an IDI that is classified as "adequately capitalized"[85] under PCA upon finding that the acceptance of brokered deposits does not constitute an unsafe or unsound practice. Thus, FDICIA permitted an adequately capitalized IDI to accept brokered deposits but only with a waiver from the FDIC.

FDICIA precluded an undercapitalized IDI from accepting brokered deposits. FDICIA also generally prohibited an IDI that is not well capitalized from offering interest rates that significantly exceed the prevailing rate in the applicable area or the national rate established by the FDIC.

During consideration of FDICIA, and in particular during consideration of an amendment offered by Senator Robert Graham (D-FL) to prohibit federal insurance of brokered deposits,

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[82] Joint Explanatory Statement of the Committee of Conference, H.R. Conf. Rep. No. 222, 101st Cong., 1st Sess. 1989, 402-403 (Aug. 4, 1989).

[83] *See* FDICIA, Pub. L. No. 102-242, § 131 (Prompt Regulatory Action) and § 301 (Limitations on Brokered Deposits and Deposit Solicitations), 105 Stat. 2236 (Dec. 19, 1991).

[84] *See* 12 U.S.C. § 1831o(b)(1)(A).

[85] Adequately capitalized is the second highest capital classification under PCA. *See* 12 U.S.C. § 1831o(b)(1)(B).

Senator Murkowski, author of the original brokered deposits amendment in FIRREA, commented,

> I think we have a clear case here of an effort to address a problem that really no longer exists. It did exist at one time and it existed in a manner where there was clearly flagrant abuse of the process. The abuse occurred as a consequence of brokered deposits by unhealthy financial institutions being marketed by the securities industry. It greatly increased the cost of the S&L bailout. And I would have certainly welcomed the presence of my colleagues on this matter prior to 1989 when I debated the issue of brokered deposits on the floor. I spoke out against the inappropriate use of brokered deposits in that timeframe in 1989. But in 1989, we took the first major step to address the flagrant abuse. I authored a provision of the 1989 S&L cleanup legislation under FIRREA restricting the use of brokered deposits by unhealthy institutions. [86]

Senator Murkowski further explained that the case-by-case waiver for troubled institutions established in Section 29 resolved the brokered deposits issue, stating that "[t]he enactment of this [waiver] provision has worked. It stopped the bleeding of the insurance fund."[87]

VI. ADDITIONAL AMENDMENTS TO SECTION 29

Since enactment of FIRREA and FDICIA, Congress has amended Section 29 several times. None of these amendments has resulted in substantive revisions to the statutory definition of the term "deposit broker" in Section 29.

Congress made technical amendments to Section 29 in the Housing and Community Development Act of 1992, and conforming amendments to Section 29 in the Riegle Community Development and Regulatory Improvement Act of 1994, which amended the interest rate restrictions in Section 29(g)(3) to ensure conformity with the PCA framework established in FDICIA.[88]

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[86] *See* Congressional Record – Senate, 33488 (Nov. 21, 1991) (regarding Senator Graham's amendment to prohibit federal deposit insurance of brokered deposits) (emphasis added).

[87] *Id*. at 33490.

[88] *See* Housing and Community Development Act of 1992, Pub. L. 102–550, § 1605(a)(1) (Oct. 28, 1992); and Riegle Community Development and Regulatory Improvement Act of 1994, Pub. L. 103–325, § 337 (Sept. 23, 1994).

More recently, Congress amended Section 29 to permit well capitalized and well rated IDIs to exclude a limited amount of reciprocal deposits from treatment as brokered deposits.[89] Pursuant to this exclusion, well capitalized and well rated IDIs are not required to treat reciprocal deposits as brokered deposits up to the lesser of 20 percent of total liabilities, or $5 billion.

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[89] The Economic Growth, Regulatory Relief, and Consumer Protection Act, Pub. L. 115-174, § 202(a) (May 24, 2018). IDIs that are not both well capitalized and well rated may also exclude reciprocal deposits from their brokered deposits under certain circumstances.