FDIC

Federal Deposit Insurance Corporation
550 17th Street NW, Washington, D.C. 20429-9990

Financial Institution Letter
FIL-2-2008
January 14, 2008

PROCESSING DEPOSIT ACCOUNTS IN A BANK FAILURE; MODERNIZING LARGE-BANK INSURANCE DETERMINATIONS

Notice of Proposed Rulemaking

Summary: The FDIC is proposing the attached two-part rulemaking relating to the potential failure of an FDIC-insured depository institution: The first part of the proposal would govern how and at what point deposit account balances would be determined in the event of a failure, and applies to all FDIC-insured depository institutions. The second part proposes requirements to facilitate the process for determining the insurance status of depositors of *large* insured depository institutions in the event of failure. Comments on the Notice of Proposed Rulemaking are due by April 14, 2008.

Distribution:
All Insured Depository Institutions

Suggested Routing:
Chief Executive Officer
Chief Operations Officer

Related Topics:
Deposit Insurance Coverage
12 C.F.R. Part 330

Attachment:
Notice of Proposed Rulemaking

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Note:
FDIC financial institution letters (FILs) may be accessed from the FDIC's Web site at www.fdic.gov/news/news/financial/2007/index.html.

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Paper copies of FDIC financial institution letters may be obtained through the FDIC's Public Information Center, 3501 Fairfax Drive, E-1002, Arlington, VA 22226 (1-877-275-3342 or 703-562-2200).

Highlights:

- When an FDIC-insured depository institution fails, the FDIC must determine the total insured amount for each depositor. The rules used by the FDIC to determine account balances as of the day of failure must be clearly established. As proposed, a deposit account balance on the day of failure would be defined as the end-of-day *ledger* balance of the deposit account on the day of failure. The proposed rule would apply to all insured depository institutions.

- The FDIC also is modernizing its current business processes and procedures for determining deposit insurance coverage in the event of a failure of one of the largest insured depository institutions (i.e., the 159 institutions with at least $2 billion in domestic deposits and either more than 250,000 deposit accounts or at least $20 billion in total assets, regardless of the number of deposit accounts).

- The proposed claims modernization rule would require the largest institutions to modify their deposit systems so that the FDIC could calculate deposit insurance coverage quickly in the event of failure.

- The FDIC originally solicited comments on claims modernization in 2005 and 2006. Based on its review of the comments, the FDIC is proposing the least-costly approach that would meet its objectives in the event of a large-bank failure.

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MODERNIZING LARGE-BANK INSURANCE DETERMINATIONS
Notice of Proposed Rulemaking

The Federal Deposit Insurance Corporation (FDIC) has issued the attached two-part Notice of Proposed Rulemaking relating to the potential failure of an insured depository institution:

- *Part 1* proposes a rule governing how and at what point deposit account balances would be determined in the event of an insured depository institution failure. This part would apply to all insured depository institutions.
- *Part 2* proposes requirements to facilitate the process for determining the insurance status of depositors of large insured depository institutions in the event of failure. As proposed, the Part 2 requirements currently would apply only to the 159 insured depository institutions with at least $2 billion in domestic deposits and either (1) more than 250,000 deposit accounts or (2) total assets over $20 billion, regardless of the number of deposit accounts. These "Covered Institutions" amount to less than two percent of the more than 8,500 insured depository institutions.

Part 1. A deposit account balance on the day of failure would be defined as the end-of-day *ledger* balance of the deposit account on the day of failure. This account balance would take into consideration any prearranged sweep transactions scheduled to occur that day, as long as funds are not removed from the depository institution after the time of failure.

When an FDIC-insured depository institution fails, the FDIC must determine the total insured amount for each depositor. To make this determination, the FDIC must ascertain the balances of all deposit accounts owned by the same depositor in the same ownership capacity at a failed institution as of the day of failure. The second part of this proposed rule would require certain large depository institutions to place holds on deposits accounts in the event of failure. The amount held would vary depending on the account balance. In order to calculate these hold amounts, the rules used by the FDIC to determine account balances as of the day of failure must be clearly established.

Under Part 1, the FDIC also requests comment on whether repurchase-agreement sweep arrangements, as actually structured and executed, pass title to the customer in a transaction that is enforceable against the FDIC or create perfected security interests that are enforceable against the FDIC. The FDIC is concerned that the structure of certain sweep arrangements labeled as repurchase agreements in fact do not result in perfected security interests, and thereby may result in a loss exposure to the customer in the event of failure.

Part 2. This part of the proposed rule applies to large FDIC-insured institutions with complex deposit systems. Covered Institutions would be required to adopt mechanisms that would, in the event of the institution's failure:

- Allow automatic posting of provisional holds on large deposit accounts in any percentage specified by the FDIC on the day of failure.
- Provide the FDIC with deposit account data in a standard format.
- Allow automatic removal of the provisional holds and posting of the results of insurance determinations as specified by the FDIC.

When handling a depository institution failure, the FDIC is required to structure the least costly of all possible resolution transactions, except in the event of systemic risk. In addition, the FDIC is required to pay insured deposits "as soon as possible" after an institution fails. The FDIC places a high priority on providing access to insured deposits promptly and, in the past, has usually been able to allow most depositors access to their deposits on the business day following closing. Doing so enables the FDIC to (1) maintain public confidence in the banking industry and the FDIC; (2) provide the best possible service to insured depositors by minimizing uncertainty about their status and avoiding costly disruptions that may limit their ability to meet financial obligations; (3) mitigate the spillover effects of a failure, such as risks to the payments system, problems stemming from depositor illiquidity and a substantial reduction in credit availability; and (4) retain, where feasible, the franchise value of the failed institution (and, thus, minimize the FDIC's resolution costs).

The largest insured institutions are growing increasingly complex. The proposed rule would help facilitate an insurance determination and dramatically improve access to depositor funds if one of these institutions were to fail. The proposed rule is intended to allow the deposit operations of a failed institution to be continued on the day following failure. It is also intended to permit the FDIC to meet its legal mandates regarding the resolution of failed insured institutions, provide liquidity to depositors promptly, enhance market discipline, ensure equitable treatment of depositors at different institutions, and help preserve the franchise value of a failed institution (thus, reducing the FDIC's costs).

The FDIC last updated its deposit insurance determination process in 1999. The largest number of deposit accounts in a failed institution for which the FDIC has had to make an insurance determination was about 175,000 for NetBank, FSB, Alpharetta, Georgia, on September 28, 2007. Today, some of the larger banks have more than 50 million deposit accounts.

Comments on the Notice of Proposed Rulemaking are due by April 14, 2008.

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Director
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