
May 17, 2021

Brokered Deposits

SUMMARY

On December 15, 2020, the Federal Deposit Insurance Corporation (FDIC) adopted a final rule that creates a new framework for analyzing certain provisions of the “deposit broker” definition, including “facilitating” and “primary purpose”.¹ The new rule also establishes a transparent application process for persons that seek a “primary purpose exception” but do not meet one of the “designated exceptions”. In addition, the rule also covers interest rate restrictions for less than well capitalized insured depository institutions. The final rule took effect on April 1, 2021 with full compliance extended until January 1, 2022.

Among other things, the FDIC final rule seeks to modernize its brokered deposit regulations to reflect recent technological changes and innovations that have occurred and recognize that the definition of deposit broker may not be as relevant compared to the deposit placement arrangements that exist in the market today. The FDIC issued a Brokered Deposit Fact Sheet: <https://www.fdic.gov/news/fact-sheets/broker-deposit12-15-20.pdf>, an Interest Rate Restrictions Fact Sheet: <https://www.fdic.gov/news/fact-sheets/irr-12-15-20.pdf> and a staff memorandum: <https://www.fdic.gov/news/board/2020/2020-12-15-notice-dis-a-mem.pdf>.

BACKGROUND

Under current law, a well-capitalized insured depository institution (IDI) is not restricted from accepting deposits from a deposit broker. An adequately capitalized IDI may accept deposits from a deposit broker if the FDIC has provided a waiver, and an undercapitalized depository institution is not allowed to accept deposits from a deposit broker.

Historically, Section 29 of the Federal Deposit Insurance Act does not directly define what a brokered deposit is, but instead defines a deposit broker and from this the meaning of brokered deposit is determined. The deposit broker definition has been subject to nine statutory exceptions. The new rule creates a framework for analyzing certain provisions of the deposit broker definition including facilitating and primary purpose.

DEFINITION OF DEPOSIT BROKER

The final rule alters the definition of “deposit broker”, which previously set forth what “being engaged in the business of placing deposits and being engaged in the facilitating the placement of deposits” means. These terms were broadly construed by regulators using the prior version of the

¹ The FDIC rule is codified at 12 CFR § 337.6.

rule such that most activity was considered subject to the definition and its restrictions.

Under the new rule, being engaged in the business of placing deposits maintains that the person must have a business relationship with its customers and the person must receive customer funds before placing deposits.

The final rule also changes the facilitation prong of the definition to clarify that if a third party has meaningful, significant control or influence over an account then they are acting as a deposit broker. The new rule specifies that a person is engaged in the act of facilitating the placement of brokered deposits if:

- The person has legal authority, contractual or otherwise, to close the account or move the third party's funds to another insured depository institution;
- The person is involved in negotiating or setting rates, fees, terms, or conditions for the deposit account; or
- The person engages in matchmaking services.

As mentioned above, the final rule includes matchmaking services as activities that will be considered brokered. Matchmaking is defined as:

- a person is engaged in matchmaking if the person proposes deposit allocations at, or between, more than one bank based upon both (a) the particular deposit objectives of a specific depositor or depositor's agent, and (b) the particular deposit objectives of specific banks, except in

the case of deposits placed by a depositor's agent at a bank affiliated with the depositor's agent. A proposed deposit allocation is based on the particular objectives of:

- a depositor or depositor's agent when the person has access to specific financial information of the depositor or depositor's agent and the proposed deposit allocation is based upon such information; and
- a bank when the person has access to specific information of the deposit balance objectives of the bank and proposed deposit allocation is based upon such information.

Lastly, the definition of deposit broker is further clarified in the final rule by excluding from the definition any person that has an exclusive deposit placement with one IDI and is not placing or facilitating the placement of deposits at other IDIs.

DEFINITION EXCEPTIONS

The new rule allows the primary purpose exception to the deposit broker definition to apply when, with respect to a particular business line, the primary purpose of the agent's or nominee's business relationship with its customers is not the placement of funds with a depository institution, and whether they do qualify for the primary purpose exception will be based on an analysis of their relationship with those customers.

The final rule further creates specified business relationship exceptions that meet

the primary purpose exception and are automatically exempt (i.e. with no notice or application requirement) including those that have been previously determined by the FDIC as meeting the primary purpose exception. These business relationship exceptions are as follows:

- customer funds for the primary purpose of providing property management services;
- customer funds for the primary purpose of providing cross-border clearing services to its customers;
- customer funds for the primary purpose of providing mortgage servicing;
- customer funds for the primary purpose of facilitating a real estate transaction;
- customer funds for the purpose of facilitating the exchange of properties under section 1031 of the Internal Revenue Code;
- customer funds in compliance with 17 CFR 240.15c3-3(e) or 17 CFR 1.20(a);
- customer funds for the primary purpose of posting as collateral to obtain a credit-card loan;
- customer funds for the primary purpose of paying for or reimbursing qualified medical expenses under section 223 of the Internal Revenue Code;
- customer funds the primary purpose of investing in qualified tuition programs under section 529 of the Internal Revenue Code;
- customer funds to enable participation in certain tax-advantaged retirements programs;

- customer funds to deliver funds to the beneficiaries of government programs; and
- customer funds placed pursuant to such other relationship that the FDIC identifies as a designated business relationship that meets the primary purpose exception.

In addition, the FDIC identifies certain business relationship exceptions that also qualify for the primary purpose exception without an application requirement but that do have a notice requirement. These relationships are as follows:

- relationships where less than 25 percent of the total assets that the agent or nominee has under administration for its customers is placed at depository institutions;
- where 100 percent of depositors' funds are placed into transactional accounts for the purpose of enabling transactions.

For those agents or nominees who do not qualify for any of the listed exceptions but still wish to be considered for the primary purpose exceptions, the FDIC has created an application process to evaluate these requests.

Finally, the FDIC has noted that the content of some prior staff advisory opinions has been included in the final rule. However, upon the final compliance date of January 1, 2022, previous staff advisory opinions will be moved to inactive status and the final rule will supplant these opinions.

The information contained in this CBA Regulatory Compliance Bulletin is not

May 17, 2021

intended to constitute, and should not be received as, legal advice. Please consult with your counsel for more detailed information applicable to your institution.

