ALERT MEMORANDUM

FDIC Overhauls Brokered Deposit Regulation:

Aims to Reduce Deposits Treated as Brokered; Final Rule Replaces Decades of Interpretive Letters

January 25, 2021

In December 2020, the Federal Deposit Insurance Corporation ("FDIC") approved a final rule (the "Final Rule") to reframe the definition and exceptions for "brokered deposits", incorporating industry developments, the significant comments received and the FDIC's interpretations over the past 30 years.[1] Since Section 29 of the Federal Deposit Insurance Act was adopted in 1989, the FDIC has broadly defined virtually any third party connecting a depositor with a bank as a "deposit broker" and the resulting deposits as "brokered deposits". The Final Rule responds to long-standing industry criticisms seeking a more narrow definition of "deposit broker" and responds to more recent initiatives urging the FDIC to reflect a more practical view of the role of third parties in light of industry and technological innovation.

In short, the Final Rule clarifies and narrows the FDIC's prior interpretations of "deposit broker". Departures from the proposed rule[2] and from prior interpretations appear to permit substantially more deposits to be excluded from treatment as "brokered deposits". More specifically, the Final Rule focuses more narrowly on those third parties that take an active role in opening accounts or in influencing or controlling the depositor's relationship with the bank. In addition, the Final Rule establishes specific designated business exceptions that would automatically meet the "primary purpose" exception from the deposit broker definition ("Designated Business Exceptions") and a formal application process for parties seeking additional "primary purpose" exemptions. In particular, the Final Rule's substantially narrower definition of "deposit broker" and significantly expanded exceptions relative to previously issued FDIC advisory opinions should help pave the way for more bank-fintech partnerships.

The Final Rule is effective April 1, 2021. Beginning April 1, 2021, an entity seeking to rely on a Designated Business Exception that requires a notice submission to the FDIC must file its notice and comply with applicable reporting requirements. Entities desiring a Primary Purpose Exception outside of those enumerated in the Final Rule should also begin submitting applications after April 1, 2021. Nevertheless, entities may continue to rely on existing staff advisory opinions or other interpretations regarding brokered deposits that predated the Final Rule until January 1, 2022, at which point those opinions and interpretations will be moved to inactive status.

The Final Rule was published in the *Federal Register* on January 22, 2021, but may be subject to a potential delay in effectiveness due to the recent change in Administration.

---

[1] FDIC, *Unsafe and Unsound Banking Practices: Brokered Deposits and Interest Rate Restrictions,* 86 Fed. Reg. 6742 (Jan. 22, 2021).

[2] 85 Fed. Reg. 7453 (Feb. 10, 2020) (the "Proposal").

Key Takeaways

- The Final Rule marks a significant shift in the FDIC's approach to brokered deposits. Previously, FDIC interpretations had defined virtually any third party participating in connecting a depositor with an insured depository institution ("IDI") as a "deposit broker". These standards had evolved over the past 35 years through an extensive series of FDIC staff advisory opinions generally published on the FDIC's website.
- The Final Rule focuses more narrowly on:
    - whether the third party has a "business relationship" with the depositor or the bank and
    - whether the third party takes an "active role" in placing the deposits or otherwise maintains a "level of influence or control" over the deposit account.

  While the preamble to the Final Rule leaves some ambiguity in interpreting these concepts, it clearly shifts the nature of the analysis compared with past FDIC opinions.
- The FDIC's approach is a significant shift from the case-by-case "common law" approach used by the FDIC in its advisory opinions, and the FDIC indicated that the Final Rule is an attempt to provide more transparency and clarity to the determination of whether deposits are brokered. Three decades worth of interpretations will be moved to "inactive" status as of the end of 2021, and the law (and "lore") going forward will be developed based on both the Final Rule's text and the FDIC's disclosure of determinations made based on applications and other interpretive requests under the Final Rule.
- Two principal modifications drive the more narrow definition of brokered deposits:
    - **Narrowing the "deposit broker" definition**. Among other elements narrowed from the Proposal and from prior interpretations, the Final Rule states that a person will not be "engaged in the business of placing deposits" or "engaged in the business of facilitating the placement of deposits" and therefore not a "deposit broker", if the person has an exclusive deposit placement arrangement with one IDI and is not placing or facilitating the placement of deposits at any other IDI.
    - **Expanding the scope of the "primary purpose" exception**. The Final Rule clarifies the "primary purpose" exception (the "Primary Purpose Exception") in a number of ways. The FDIC has sought to incorporate bright-line tests from prior interpretations and, in a departure from the Proposal, not to require notice or an application for a number of those tests. In addition, the FDIC explicitly expanded the Primary Purpose Exception to (1) agents with a business line that deposits with IDIs less than 25% of total customer assets under administration and (2) agents that place deposits solely in transactional accounts with no interest rate or fees paid to the depositor. These two exceptions will require notice to the FDIC, but the FDIC also listed 11 additional Designated Business Exceptions that do not require either notice or application. To address specific cases beyond those described in the Final Rule, the FDIC has created an application process to reach determinations on the availability of the Primary Purpose Exception in an efficient and streamlined manner.
- Nevertheless, we expect that the changes introduced by the Final Rule will initiate their own version of uncertainty regarding the types of deposits that must be considered brokered. Bank regulation has evolved such that the determination around what is or is not a brokered deposit has taken on greater significance since the original statutory introduction of the concept. For example, changes to the scope of the definition of brokered deposits or limitations on the scope of the statutory exemptions from this classification could, among other things, affect an IDI's deposit insurance premiums and complicate determinations for purposes of the liquidity coverage ratio and net stable funding ratio requirements applicable to large banking organizations.

The Final Rule

The Final Rule significantly liberalizes the FDIC's treatment of deposits placed by third parties. The substance of the Final Rule represents a rebalancing of the FDIC's goals of modernizing banking regulations and promoting safety and soundness.[3]

I. Statutory and Regulatory Framework

The restrictions on brokered deposits were initially enacted by Congress under the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 in Section 29 of the Federal Deposit Insurance Act (the "FDIA"). Two years later in 1991, Congress modified the framework to restrict the use of brokered deposits for less than well-capitalized IDIs under the Prompt Corrective Action ("PCA") regime.[4] The legal framework for brokered deposit regulation was largely unchanged until 2018 when Congress adopted a limited exception for certain "reciprocal deposits" placed through bank networks in Section 202 of the Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018.[5]

Well capitalized IDIs are not restricted from accepting deposits from a deposit broker. An "adequately capitalized" IDI may accept deposits from a deposit broker only if it has received a waiver from the FDIC.[6] In addition, IDIs relying extensively on brokered deposits pay higher assessment premiums for deposit insurance,[7] and banking organizations subject to minimum liquidity coverage ratio and net stable funding ratio requirements must assume a higher outflow rate and maintain a higher amount of stable funding for many brokered deposits than for non-brokered deposits.[8]

The statutory text does not provide a definition of "brokered deposit". Instead, under the FDIA and its implementing regulations, deposits are "brokered" if they are obtained by an IDI, directly or indirectly, through a "deposit broker".[9] The statutory definition of "deposit broker" includes "any person engaged in the business of placing deposits, or facilitating the placement of deposits, of third parties with [IDIs]".[10]

The term "facilitating the placement of deposits" has been interpreted broadly by the FDIC to include actions taken by third parties to connect IDIs with potential depositors.[11] The FDIC has generally defined any person (with limited exceptions, such as for IDI employees[12]) or entity that places deposits in an IDI for a customer as a deposit broker unless a statutory exception applies. In the past, the FDIC has emphasized that the analysis is highly fact specific.[13]

[3] "Through this rulemaking process, the FDIC attempted to ensure that the brokered deposit regulations would continue to promote safe and sound practices while ensuring that the classification of a deposit as brokered appropriately reflects changes in the banking landscape". Final Rule at 6742.

[4] *See generally* 12 U.S.C. §1831f(a) and 12 C.F.R. § 337.6.

[5] 12 U.S.C. § 1831f(i), as adopted in Section 202 of the Economic Growth, Regulatory Relief, and Consumer Protection Act, Pub. L. No. 115-174 (enacted May 24, 2018). *See also* Cleary Gottlieb, *President Signs Regulatory Relief Bill* (May 24, 2018), 7, https://www.clearygottlieb.com/-/media/files/alert-memos-2018/2018_05_24-regulatory_relief_bill_enacted_summary-pdf.pdf.

[6] 12 U.S.C. § 1831f(c). The Final Rule narrows the scope of deposits considered "brokered deposits," which allows IDIs rated less than well-capitalized to obtain such deposits without restriction. According to the FDIC, there were only 10 such IDIs as of June 30, 2020, which held a total of approximately $2.5 billion in assets. *See* Final Rule at 6762.

[7] 12 C.F.R. § 327.9(d)(3).

[8] *See* 12 C.F.R. Part 249 (Federal Reserve Board); 12 C.F.R. Part 50 (Office of the Comptroller of the Currency); and 12 C.F.R. Part 329 (FDIC).

[9] 12 C.F.R. § 337.6(a)(2). *See also* 12 U.S.C. § 1831f(a).

[10] 12 U.S.C. § 1831f(g)(1). *See* FDIC, *Identifying, Accepting and Reporting Brokered Deposits Frequently Asked Questions* (the "FDIC FAQs") (last revised July 14, 2016), A5, https://www.fdic.gov/news/news/financial/2016/fil16042b.pdf.

[11] FDIC FAQs, A2.

[12] *See* 12 U.S.C. § 1831f(g)(2)(B) (providing an exception from the definition of deposit broker for "an employee of an [IDI], with respect to funds placed with the employing depository institution"). *See also* 12 C.F.R. § 337.6(a)(5)(ii)(B); FDIC FAQs, E3 (noting that the exception applies only to "employees," defined in the FDIA to mean any employee (i) employed *exclusively* by the IDI, (ii) whose compensation is primarily in salary form, (iii) who does not share such compensation with a deposit broker and (iv) whose office space is used *exclusively* for the benefit of the IDI that employs that individual).

[13] *See*, *e.g.*, FDIC FAQs, A5.

The statutory definition of "deposit broker" also includes nine statutory exceptions.[14] The most significant statutory exception is the Primary Purpose Exception, as described in Section III below. The FDIC has previously clarified uncertainties through staff interpretive letters issued publicly, confidentially or in non-public staff advisory opinions.

As Chairman McWilliams acknowledged, quoting Federal Reserve Board Governor Randy Quarles, this method of communicating interpretations mirrors the "subtle hermeneutics of Federal Reserve lore" developed with respect to the Bank Holding Company Act's definition of "control". The FDIC did issue frequently asked question guidance in 2016,[15] but the FDIC FAQs were not subject to notice and comment, and did not modify or modernize the FDIC's approach to brokered deposits.

Indeed, many in the industry thought that the FDIC FAQs reinforced the conservative approach that the FDIC had taken to interpreting the statute. The FDIC's prior interpretations have been viewed by many as sweeping too many relationships into the deposit broker or brokered deposit categories, particularly in light of the increasing role of online and mobile banking and of other new channels for banks and advertisers to interact with potential depositors. While the prior interpretations could potentially be adapted to incorporate these new channels for delivering banking services, bankers and many market participants have sought a rethinking of the prior interpretations to provide greater clarity and to update the standards.

The FDIC issued an advance notice of proposed rulemaking and request for comment early in 2019[16] before issuing the Proposal early in 2020.

II. Revised "Deposit Broker" Definition

The Final Rule expands the current definition of "deposit broker" into four enumerated prongs:[17]

- ***Any person engaged in the business of placing deposits of third parties with IDIs***.[18] Consistent with the Proposal, the preamble to the Final Rule clarifies that a deposit broker is a "person [that] has a business relationship with its customers, and as part of that relationship, places deposits on behalf of the customer (*e.g.*, acting as custodian or agent for the underlying depositor)".[19] The FDIC's addition of the business relationship between the agent and the customer is the critical revision and is key to the FDIC's analysis.

  In contrast to the next prong regarding "facilitation", to be deemed "engaged in the business of placing deposits", a person must also "*receive[] third party funds* and deposit[] those funds at *more than one* [IDI]".[20]

  - Therefore, the main distinction with the "facilitation" prong is that a deposit broker must actually "receive customer funds before placing deposits".[21]

  - In a significant narrowing of the definition, the preamble also clarifies that "any person that has an exclusive deposit placement arrangement with *one IDI*, and is not placing or facilitating the placement of deposits at any other IDI" is not treated as a deposit broker.[22] The FDIC indicated that it has adopted this change, in part, to avoid being inundated with applications seeking the Primary Purpose Exception under the new application process. However, the FDIC also determined that an exclusive business relationship with one IDI "is less likely to [result in the

[14] 12 U.S.C. § 1831f(g)(2).

[15] FDIC FAQs.

[16] FDIC, *Unsafe and Unsound Banking Practices: Brokered Deposits and Interest Rate Restrictions*, 84 Fed. Reg. 2366 (Feb. 6, 2019).

[17] Any person that meets the definition of "deposit broker" may still be able to avail itself of one or more of the various exceptions, such as the Primary Purpose Exception or the Designated Business Exceptions.

[18] 12 C.F.R. § 337.6(a)(5)(i)(A).

[19] Final Rule at 6745.

[20] 12 C.F.R. § 337.6(a)(5)(ii) (emphasis added).

[21] Final Rule at 6745.

[22] *Id.* (emphasis added).

movement of] customer funds to other IDIs in a way that makes the deposits less stable".[23]

The FDIC further clarifies that under the revised definitions, wholly-owned subsidiaries of IDIs that have an exclusive deposit placement arrangement with their parent would not be considered "deposit brokers" under the Final Rule.[24] The FDIC also warned that it inserted an anti-evasion provision in the Final Rule so that entities that may break up relationships among multiple entities in order that each entity would only have a relationship with one IDI would be rolled up into "one person" and fail the exclusive business relationship exception.[25]

- ***Any person engaged in the business of facilitating the placement of deposits***.[26] The FDIC has traditionally viewed "facilitation" broadly to "include actions taken by third parties to connect [IDIs] with potential depositors".[27] As a result, a variety of activities were caught by the FDIC's traditional approach.

  While the Proposal included a definition of "engaged in the business of facilitating the placement of deposits", the Final Rule significantly narrows the proposed definition, as well as the concepts used in prior interpretations, by constricting the scope of activities that constitute "facilitating" to persons engaged in any one of three enumerated types of activities:

  - acting in a legal capacity to close an account or move funds for a depositor,
  - negotiating or setting rates, fees, terms or conditions for the deposit account, or
  - engaging in "matchmaking" activities.[28]

  The preamble to the Final Rule clarifies the FDIC's intent for "facilitation" activities to require an indication that a person "takes *an active role* in the opening of an account or *maintains a level of influence or control* over the deposit account even after the account is open".[29]

  Under the Final Rule, 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".[30]

  This definition of "matchmaking" was not included in the Proposal and is a significant change for a number of reasons:

  - First, deposit allocations are to be based upon objectives of both a depositor (or its agent) and a specific bank. Each of these require that the broker have "specific information" about the depositor and the bank, respectively, and the "proposed deposit allocation is based upon such information". In the FDIC's view, sharing information in an effort to match depositors with banks indicates that the person has influence over the movement of deposits between or among IDIs. The "matchmaking activities" prong appears to recast and significantly narrow the Proposal's "information sharing" prong.[31] Because both sets of information are required, it could be possible for a person to solicit banks on behalf of customers or market on behalf of banks, without having the requisite information of the other party. Administrative services without the proposing of deposit allocations and traditional listing services also are not intended to be captured by the matchmaking prong.
  - Second, the matchmaking definition includes an exception for "deposits placed by a depositor's agent with a bank affiliated with the depositor's agent".[32] In particular, the FDIC noted that this exception was intended "not to disrupt business

[23] *Id.*

[24] Final Rule at 6748.

[25] Final Rule at 6745.

[26] 12 C.F.R. § 337.6(a)(5)(i)(B).

[27] Final Rule at 6745.

[28] 12 C.F.R. § 337.6(a)(5)(iii).

[29] Final Rule at 6746 (emphasis added).

[30] 12 C.F.R. § 337.6(a)(5)(iii)(C).

[31] Final Rule at 6746.

[32] 12 C.F.R. § 337.6(a)(5)(iii)(C)(i).

arrangements that have existed for a number of years in reliance on prior staff guidance related to affiliate sweep arrangements" by broker-dealers and other affiliates.[33] Nevertheless, (i) sweep arrangements from unaffiliated brokers will be considered matchmaking, and (ii) there may be some ambiguities regarding whether affiliated sweep arrangements could still be considered brokered under the "engaged in placing" prong or under the alternative "facilitation" criteria, notwithstanding the FDIC's intent not to disrupt pre-existing business arrangements.[34]

- Third, this prong of the definition could enable fintech firms to participate in the placement of deposits without qualifying as deposit brokers.[35] However, the preamble notes that traditional listing services, entities that provide marketing services, and entities that design their own deposit products must evaluate the new criteria set forth in the final rule to determine whether their current arrangements meet the deposit broker definition. The FDIC indicates, however, that it expects that many will not, provided they do not assume an active role in the opening of an account or maintain a level of influence or control over the deposit account after it is opened, and otherwise do not meet any of the three facilitation prongs.[36] In addition, the preamble to the Final Rule describes a more narrow formulation, requiring that, even if a third party may participate in the allocation of deposits (*e.g.*, through creation of a software program or algorithm), if that party "does not subsequently play an *ongoing role*", then such deposits would not be deemed brokered.[37]
- Finally, the Final Rule also removed several provisions from the Proposal that would have created significant uncertainty or breadth to the definition and that commenters strongly opposed. In particular:
  - The breadth of the proposed "information sharing" prong, under which any person that directly or indirectly shared information with the IDI may have been a deposit broker, has been removed, and only more narrow remnants of this prong remain in the matchmaking definition. The FDIC indicated that the Proposal's information sharing prong could have captured "persons that do not have influence or control over the placement of deposits".[38]
  - The concept of "providing assistance" with setting rates, fees, terms or conditions was removed in favor of the more active "involved in" concept which, the FDIC indicated, is meant to capture "only . . . a third party [that] is negotiating or setting rates, terms or conditions for a particular deposit product (on behalf of a particular depositor or particular banks)".[39]

- ***Any person engaged in the business of placing deposits with IDIs <u>for the purpose of selling those deposits or interests</u> in those deposits to third parties***.[40] This prong is intended to cover brokered certificates of deposit, which have historically been treated as brokered deposits and remain so treated under the Final Rule.[41] The FDIC also indicated their current view that, "[r]egardless of any future innovations and re-structuring in the brokered CD market", brokered CDs are likely to continue to be classified as brokered deposits.[42]

[33] Final Rule at 6747, n. 23.

[34] In these situations, an entity could seek to avoid being treated as a deposit broker through other means, for example, by limiting its sweep arrangements to one bank, relying on the Primary Purpose Exception, or applying for a waiver.

[35] *See* OCC, News Release No. 2020-170, *New Brokered Deposit Rule Promotes Bank-Fintech Partnerships* (Dec. 15, 2020).

[36] Final Rule at 6760.

[37] Final Rule at 6748 (emphasis added).

[38] Final Rule at 6746.

[39] Final Rule at 6747.

[40] 12 C.F.R. § 337.6(a)(5)(i)(C).

[41] Brokered certificates of deposit would also be ineligible for the Primary Purpose Exception, without exception. *See* 12 C.F.R. § 303.243(b)(5).

[42] Final Rule at 6748.

- ***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.***[43] This prong is the current text of 12 C.F.R. § 337.6(a)(5)(i)(B) and remains unchanged in the Final Rule.

III. Expanding the Scope of the Primary Purpose Exception

The subject of extensive guidance and interpretation over the last few decades, the Primary Purpose Exception is defined by statute to exclude "an agent or nominee whose primary purpose is not the placement of funds with depository institutions" from the statutory definition of "deposit broker".[44]

The FDIC's approach to date has been to consider the primary purpose of an agent or nominee on a case-by-case, fact-specific basis, to determine whether an agent's placement of deposits is for a substantial purpose other than to provide deposit insurance or to place deposits.[45] In a series of advisory opinions dating back to 1989, the FDIC concluded that the Primary Purpose Exception has been met where

- foreign affiliates of a U.S. IDI connected clients with deposit accounts at the U.S. IDI to be used for clearing U.S. dollars;[46]
- a broker-dealer swept client funds into money market deposit accounts at two affiliated banks to facilitate customers' purchase of securities;[47]
- a securities firm deposited client funds in a deposit account to satisfy a mandatory Securities and Exchange Commission "reserve account" requirement;[48] and
- a credit card bank connected customers with deposit accounts at another bank to take security interests in those accounts,[49] among other examples.

Conversely, the FDIC has declined to apply the Primary Purpose Exception, for example, where customers were connected with an IDI by a financial management or investor services business (without a regulatory or non-investment transactional purpose for opening the account).[50]

The Final Rule would generally codify this line of advisory opinions into a list of 13 Designated Business Exceptions that will meet the Primary Purpose Exception and that will not be required to go through the application process. In addition, the FDIC provided that it may specifically identify other Designated Business Exceptions in the future. Beginning January 2022, entities must rely solely on the Final Rule (and any approvals provided pursuant to the application process thereunder) and may no longer rely on staff advisory opinions or other interpretations that predated the Final Rule. The FDIC has provided a list of advisory opinions and other publicly available interpretations that will be moved to inactive status.[51]

The Primary Purpose Exception applies to a deposit broker on a business-line level. The FDIC will determine what counts as a "business line" based on all the facts and circumstances, rather than a proscriptive rule, but intends that this process will be straightforward and involve considerable deference to an applicant's good-faith judgment about what counts as a "business line".[52]

For two of these 13 exceptions, a simple notice will be required, while for the other 11 Designated Business Exceptions, no notice, application or reporting will be required. Persons that do not meet one of the designated exceptions may apply for a Primary Purpose Exception.

- ***Entities seeking to qualify for the Primary Purpose Exception under one of 11 Designated Business Exceptions that require neither a notice nor an application.*** These generally consist of business relationships that the FDIC staff has previously viewed as meeting the Primary Purpose Exception and

[43] 12 C.F.R. § 337.6(a)(5)(i)(D).

[44] 12 U.S.C. § 1831f(g)(2)(I).

[45] FDIC FAQs, E8.

[46] FDIC Adv. Op. 16-01 (May 19, 2016).

[47] FDIC Adv. Op. 05-02 (Feb. 3, 2005).

[48] FDIC Adv. Op. 94-39 (Aug. 17, 1994).

[49] FDIC Adv. Op. 94-13 (Mar. 11, 1994).

[50] *See*, *e.g.*, FDIC Adv. Op. 17-02 (June 19, 2017).

[51] Final Rule at 6759.

[52] Final Rule at 6756.

that have been the subject of prior FDIC advisory opinions. These Designated Business Exceptions include placements of deposits related to property management services, cross-border clearing services, mortgage servicing, other real estate transaction facilitation, like-kind exchanges of properties, broker-dealer or futures commission merchant required reserves, collateral to secure credit card loans, qualified health savings accounts, qualified tuition savings programs, tax-advantaged retirement account programs, and certain government programs.

- ***Entities seeking to qualify for the Primary Purpose Exception based on the "25%" or "enabling transactions" Designated Business Exceptions would only need to submit notice to the FDIC.*** The Final Rule includes two new exceptions as proposed:
  - A business line that places less than 25% of the total assets it has under administration for its customers at an IDI; and
  - A business line that places 100% of depositors' funds at IDIs into transactional accounts that do not pay any fees, interest, or other remuneration to the depositor.

  Helpfully, the Final Rule removes the application requirement to rely on these two Designated Business Exceptions, and requires only a notice. The notice will need to include (1) the designated exception upon which the business line is relying; (2) a brief description of the business line; (3) the applicable specific contents for the designated exception (see below); (4) a statement that there is no involvement of any additional third party who qualifies as a deposit broker or a brief description of any additional third party that may qualify as a deposit broker; and (5) if the notice is provided by a nonbank entity, a list of the IDIs that are receiving deposits by or through the particular business line at the time that the notice is filed.
  - **Specific Content for the "25%" Exception Notice**: The specific contents for notice under the "25%" exception are: (1) the total amount of customer assets under administration by the third party for that particular business line and (2) the total amount of deposits placed by the third party on behalf of its customers, for that particular business line, at all depository institutions (exclusive of the amount of brokered CDs placed by the third party, which is treated as a separate business line).
  - **Specific Content for the "Enabling Transactions" Exception Notice**: The specific contents for notice under the "enabling transactions" exception are: (1) contractual evidence that there is no interest, fee, or other remuneration being paid to any customer accounts, and (2) a certification that all customer deposits are in transaction accounts.

  The "enabling transactions" Designated Business Exception is specifically limited:
  - If no interest, fees or remuneration are paid, then only notice is required.
  - If "nominal" interest, fees or other remuneration are paid (as determined by the FDIC), then an application would be required.[53]
  - If interest, fees or other remuneration are more than nominal, then the business line would not qualify for the "enabling transactions" exception.

  These two Designated Business Exceptions also require ongoing reporting:
  - For the "25%" exception, quarterly reporting is required to provided updated calculations of compliance with the 25% requirement.
  - For the "enabling transactions" exception, if only notice is required, then the broker must provide an

[53] 12 C.F.R. § 303.243(b)(4)(i). The FDIC will consider (i) the amount of interest, fees or other remuneration; (ii) the amount of transactions that customers make in the account; (iii) the marketing materials provided by the agent or nominee; and (iv) the percentage of customer funds placed in deposit accounts that are not transactions accounts. The FDIC indicated that, if customers earn a nominal amount of remuneration and, on average, make more than six transactions per month from the account, then it will make a positive determination under the Primary Purpose Exception.

annual certification that no interest, fees, or other remuneration are paid. However, if an application is required, then the FDIC intends to impose ongoing reporting requirements, as discussed below.[54]

- ***Entities seeking to qualify for the Primary Purpose Exception and that do not meet one of the Designated Business Exceptions would need to submit an application to the FDIC.***
  - **Application Contents**:[55] An agent or nominee, or an IDI acting on behalf of an agent or nominee, seeking a Primary Purpose Exception for business relationships that are not Designated Business Exceptions would be required to file an application including: (1) a description of the deposit placement arrangements with all involved entities; (2) the particular business line and its primary purpose; (3) the total amount of assets under administration and the total amount of deposits placed by the third party at all IDIs; (4) the revenue generated from deposit placement activities relative to total revenue; (5) the marketing activities of the third party; (6) the reasons the third party meets the Primary Purpose Exception; and (7) any other relevant information.
  - **FDIC Review**:[56] The FDIC will approve an application that demonstrates, with respect to a particular business line, that the primary purpose of that business line is other than the placement of facilitation of placement of deposits. Among other things, the FDIC will consider the following factors:
    - The revenue structure of, and the fees and types of fees earned by, the agent or nominee; and
    - Marketing materials, and in particular whether they are aimed at opening accounts or the opening of accounts is incidental to another primary service.

    The FDIC stated that it will not grant the Primary Purpose Exception if the agent or nominee's primary purpose for placing deposits is to encourage savings, maximize yield or provide deposit insurance.[57]

    The FDIC will notify an applicant within 45 days of submission if an application is not complete. The FDIC will then provide a determination within 120 days of receipt of a complete application, although that timeframe may be extended by a maximum of 120 additional days, if the FDIC determines an extension is necessary.[58]
  - **Reporting Requirements**:[59] If an application is granted, the FDIC will describe ongoing reporting requirements (if any) to an FDIC office and the IDI's primary federal regulator, as appropriate. The FDIC does not expect to require ongoing reporting in all cases and will tailor the requirements on a case-by-case basis. Reporting will not be required more frequently than quarterly.
  - **Revocation**:[60] If the FDIC learns that an exempt entity no longer meets the criteria of the designated exception or that information provided in a notice or subsequent reporting was inaccurate or the exempt entity fails to submit required reports, the FDIC may, with notice, revoke the entity's Primary Purpose Exception.
  - **Publication and Reliance on Applications and Waivers**:[61] The Final Rule indicates that that the FDIC expects to make publicly available on the FDIC's website redacted summaries of certain approved applications, as soon as practicable, and additional designated exceptions that will describe additional business arrangements that the FDIC in the future determines meet the Primary Purpose Exception without requiring an application. The FDIC further clarifies in the preamble that designated exceptions identified

[54] 12 C.F.R. § 303.243(b)(4)(vi).
[55] 12 C.F.R. § 303.243(b)(4)(ii).
[56] 12 C.F.R. § 303.243(b)(4)(v).
[57] Final Rule at 6755.
[58] 12 C.F.R. § 303.243(b)(4)(iv).
[59] 12 C.F.R. § 303.243(b)(4)(vi).
[60] Final Rule at 6763.
[61] Final Rule at 6755.

following the Final Rule may be relied upon, without application, by any agent or nominee that meets the published criteria.

- **IDI Requirements for Monitoring**:[62] The FDIC expects the IDI would be able to access records of a third party's eligibility for the Primary Purpose Exception, including the notices delivered to the FDIC and any accepted applications. If an IDI has reason to believe that a third party no longer qualifies for the exception (for example, due to a change in business model), the IDI would be expected to notify the FDIC and its primary financial regulator and report the deposits as brokered.

IV. Additional Observations

Despite the much greater clarity and transparency that the Final Rule provides, including resolving several interpretive issues raised by the Proposal, some open issues remain.

- ***Assessments and Call Reports***. The FDIC asserted that revisions to assessment rates and reporting requirements in call reports are outside the scope of the Final Rule. However, the FDIC indicated that these issues are under consideration for future rulemaking.[63] FDIC Chairman Jelena McWilliams recently indicated that the FDIC is considering changes to make assessments more risk sensitive, including addressing funding concentrations at larger banks that present higher risks to the Deposit Insurance Fund (such as unaffiliated sweeps that rely on the Primary Purpose Exception).
- ***Recommendations for Congressional Action***. Although the Final Rule's text and preamble do not include explicit recommendations for congressional action on brokered deposits, Chairman McWilliams has posed an alternative path. In particular, the Chairman suggested that Congress consider replacing the relevant statutory text in Section 29 of the Federal Deposit Insurance Act with "a simple restriction on asset growth for banks that are in trouble".[64] Alternatively, the Chairman suggested repealing the Primary Purpose Exception and replacing it with a "more flexible exception based on actual risk to the [FDIC's deposit insurance fund]".[65] The Chairman reiterated her support for these proposals and for congressional action more broadly, in remarks announcing the publication of the Final Rule.[66]

...

CLEARY GOTTLIEB

[62] Final Rule at 6758.

[63] Final Rule at 6761.

[64] Remarks of Chairman Jelena McWilliams, *Brokered Deposits in the Fintech Age* (Dec. 11, 2019), https://www.fdic.gov/news/news/speeches/spdec1119.pdf

[65] *Id*.

[66] Statement by FDIC Chairman Jelena McWilliams on the Combined Final Rule on Brokered Deposits and Interest Rate Restrictions at the FDIC Board Meeting (Dec. 15, 2020), https://www.fdic.gov/news/speeches/spdec1520b.html.

Contacts

If you have any questions concerning this memorandum, please reach out to your regular firm contact or the following authors:

Derek M. Bush
Partner
Washington, D.C.
+1 202 974 1526
dbush@cgsh.com

Katherine Mooney Carroll
Partner
Washington, D.C.
+1 202 974 1584
kcarroll@cgsh.com

Hugh C. Conroy, Jr.
Partner
New York
+1 212 225 2828
hconroy@cgsh.com

Jack Murphy
Senior Counsel
Washington, D.C.
+1 202 974 1580
jmurphy@cgsh.com

Michael H. Krimminger
Senior Counsel
Washington, D.C.
+1 202 974 1720
mkrimminger@cgsh.com

Allison H. Breault
Senior Attorney
Washington, D.C.
+1 202 974 1532
abreault@cgsh.com

Patrick Fuller
Senior Attorney
Washington, D.C.
+1 202 974 1534
pfuller@cgsh.com

Zachary Baum
Associate
Washington, D.C.
+1 202 974 1873
zbaum@cgsh.com