November 21, 2024

VIA ELECTRONIC SUBMISSION

James P. Sheesley, Assistant Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Re: Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions (RIN 3064-AF99)

Ladies and Gentlemen:

The Financial Services Forum (the "Forum")[1] appreciates the opportunity to submit this letter to the Federal Deposit Insurance Corporation (the "FDIC") on its proposed rule (the "Proposal") to amend its regulations related to brokered deposits.[2] The Proposal is relevant to each of our member institutions, the eight U.S. global systemically important bank holding companies ("U.S. GSIBs"), the insured depository institution ("IDI") subsidiaries of which would be subject to a revised rule.

The Proposal would unjustifiably reverse long-settled policy and legal interpretive positions, including those resulting from a multi-year FDIC rulemaking process, thus destabilizing the brokered deposit marketplace and creating unnecessary costs for IDIs without a corresponding benefit to the safety and soundness of IDIs.

Moreover, because the U.S. GSIBs are subject to the full daily Liquidity Coverage Ratio ("LCR"), the Net Stable Funding Ratio ("NSFR") and the GSIB capital surcharge, the Proposal would materially disrupt U.S. GSIBs' funding strategies relative to those of other banking organizations, without regard to the actual liquidity risks presented by

---

1 The Financial Services Forum is an economic policy and advocacy organization whose members are the chief executive officers of the eight largest and most diversified financial institutions headquartered in the United States. Forum member institutions are a leading source of lending and investment in the United States and serve millions of consumers, businesses, investors and communities throughout the country. The Forum promotes policies that support savings and investment, deep and liquid capital markets, a competitive global marketplace and a sound financial system.

2 Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions, 89 Fed. Reg. 68244 (August 23, 2024).

deposits the Proposal would reclassify as brokered and even though U.S. GSIBs are already subject to the highest level of prudential requirements.

* * *

In this letter, we wish to highlight the following key observations:

- **The Proposal would disrupt longstanding and stable sweep arrangements**. The Proposal generally would disrupt historically stable sweep arrangements through which banks have long held customer cash awaiting reinvestment. By reclassifying many types of previously exempt sweep arrangements as brokered deposits, the Proposal would disrupt stable, long-term relationships between market participants.

- **The FDIC has not provided evidence to support the Proposal**. Our analysis indicates the Proposal would result in a 42% increase in the deposits considered brokered across our member institutions. Despite this significant change, the Proposal fails to demonstrate that the expanded categories of deposits that would be classified as brokered present risks that the FDIC believes brokered deposits generally present. The FDIC has also failed to adequately consider the costs associated with the Proposal, which encompass not just compliance and operational costs, but also costs to the financial system as the Proposal would reduce stable sources of funding and may deter institutions from taking deposits that the Proposal would reclassify as brokered.

- **The Proposal would impose significant hidden costs on U.S. GSIBs**. The Proposal's arbitrary reclassification of certain deposits as brokered would have an outsized effect on U.S. GSIBs because they are subject to the most stringent implementations of the LCR and NSFR, as well as to the GSIB surcharge. Classifying these deposits as brokered would result in more punitive weightings under LCR and NSFR in a manner that is not supported by publicly available analysis or data on which we can provide feedback. As a result, the Proposal's inflation of brokered deposits would disrupt U.S. GSIBs' funding strategies. This would be an inappropriate outcome, particularly in light of U.S. GSIBs' sound risk management practices and given the fact that U.S. GSIBs are subject to the highest level of prudential requirements.

Because of these reasons, the FDIC should withdraw the Proposal. If it does not do so, the final rule should adopt our following key recommendations:

- **The FDIC should retain the 25% Test PPE.** The Proposal would narrow the types of entities and customer funds that could rely on the 25% Test PPE (as defined below), including in counterintuitive ways. Further, the Proposal would reduce the threshold for the amount of customer funds these third parties could place at a bank with respect to a particular business line resulting in procyclicality that would exacerbate periods of market stress.

- **The Proposal's revisions to the definition of a deposit broker are flawed and should not be adopted.** The FDIC should retain the current rule's exemption for third parties that propose deposit allocations at affiliated banks, which helps to mitigate liquidity risks by providing additional touchpoints between the customer and the firm. Further, the final rule should not consider fees as part of the definition of deposit broker.

- **The Proposal's approach to notice and applications should be significantly revised.** The Proposal would impose substantially burdensome notice and application requirements that would require banks to undertake costly operational buildouts. The final rule should retain the current rule's approach to notice and applications, or significantly revise the Proposal's approach including by providing banks with adequate time to comply with any new rule.

I. Key Observations and Shortcomings of the Proposal

A. <u>The Proposal's amendments to the current brokered deposits rule are unwarranted</u>.

In 2020, the FDIC significantly enhanced its brokered deposits regulations following a multi-year comment period that included both an advance notice of proposed rulemaking as well as a notice of proposed rulemaking. If adopted, the Proposal would reverse that rule within just a few years without adequate reasoning or justification. In particular, the Proposal would:

- Remove the current rule's exception from the definition of deposit broker for third parties that place or facilitate the placement of deposits as a single IDI.

- Replace the "matchmaking activities" prong in the current definition of deposit broker, including the matchmaking prong's exclusion of deposits placed by an IDI's affiliate, with a deposit allocation prong.

- Add to the definition of deposit broker persons who receive a fee or remuneration in exchange for or related to the placement of deposits.

- Replace the primary purpose exception ("<u>PPE</u>") available to agents or nominees that place at IDIs less than 25% of the total assets the agent or nominee has under administration for its customers for a particular business line (the "<u>25% Test</u>")

with a significantly narrowed PPE available to Securities and Exchange Commission ("SEC") registered broker-dealers and investment advisers that place less than 10% of its assets under management for its customers for a particular business line at an IDI ("Broker-Dealer Sweep Exemption").

- Remove the PPE available to agents or nominees who place 100% of depositors' funds at IDIs in transactional accounts (the "Enabling Transactions PPE").

- Require that an IDI on behalf of a broker-dealer submit a notice or application to rely on the newly proposed Broker-Dealer Sweep Exemption, in the case of each sweep relationship, and eliminate an IDI's ability to rely on existing PPE applications, 25% Test notices or enabling transactions exception notices or applications.

As an initial matter, we do not believe these amendments are warranted as they would upend well-established deposit placement arrangements. Moreover, the amendments would result in significant costs to the banking sector and U.S. GSIBs that the FDIC has not adequately considered.

B. The Proposal would disrupt longstanding and stable sweep arrangements between market participants.

The IDI subsidiaries of U.S. GSIBs play a critical role in safeguarding deposits swept to banks by broker-dealers, investment advisers and other market participants by providing a low-risk means to hold cash awaiting reinvestment. These sweep deposits arise out of stable, long-term relationships with market participants.

Sweep deposits are a longstanding feature of the traditional banking marketplace, as the FDIC has recognized.[3] These arrangements may take on various forms depending on the nature of the third party, the purpose of the arrangement and customer preferences. We are concerned that the Proposal, taken as a whole, would upset these longstanding and historically stable arrangements based on spurious reasoning.

Moreover, several specific aspects of the Proposal would make it more costly for banks to enter into sweep arrangements by reclassifying significantly more sweep deposits as brokered. Narrowing the existing 25% Test PPE to the Broker-Dealer Sweep Exception would reduce the scope of entities that could rely on the PPE and the amount of money they may place without being considered deposit brokers as well as narrow the types of

3 Unsafe and Unsound Banking Practices: Brokered Deposits and Interest Rate Restrictions, 84 Fed. Reg. 2366, 2372 (Feb. 2, 2019) ("Beginning in 1999, the FDIC became aware of broker dealers offering their brokerage customers an automatic sweep program by which customers' idle funds were swept to affiliated insured depository institutions.")

deposits that could be placed at a bank in reliance on the PPE. Removing the exception for bank affiliates from the matchmaking prong of the definition of deposit broker would make it more costly for banks to provide sweep services to their own customers (which would *decrease* rather than increase the stickiness of those relationships). Considering fee arrangements, including for administrative fees, as part of the definition of deposit broker would interfere with the business model of sweep relationships built up over decades in a way that would not accurately reflect the liquidity risks of those deposits. And proposing onerous new notice and application requirements would create substantial burdens on banks and third parties to maintain their existing sweep relationships. We do not believe the FDIC should make it more onerous and expensive for banks to hold customer cash for safekeeping, which is a fundamental part of the business of banking.

Finally, we note that the FDIC's concerns about the run risk of these sweep deposits generally appears misplaced, as these deposits are intended to be placed at IDIs "temporarily [to] safe-keep customer free cash balances . . . that are awaiting reinvestment."[4]

C. The FDIC has not provided evidence to support the Proposal.

As mentioned above, the Proposal would generally reverse the FDIC's recently adopted brokered deposit rule without adequate justification. This rapid reversal of regulatory practices would impede the practice of safe and sound banking by reducing consistency and transparency surrounding the FDIC's expectations. Indeed, in line with the Supreme Court's recent observations in *Loper Bright*, such a reversal would "foster[] unwarranted instability in the law, leaving those attempting to plan around agency action in an eternal fog of uncertainty."[5] Not only would the Proposal arbitrarily reverse the FDIC's recent rule, it would do so without any clear rationale, ignoring the FDIC's own fact-finding and reasoning, as well as the many public comments, from the multi-year process that led to the 2020 rule. Such frequent and contradictory changes to core bank regulation largely dictated by politics rather than policy are inimical to a stable regulatory environment that supports financial stability.

Our analysis indicates that the Proposal would result in $353 billion worth of deposits newly being considered brokered across our member institutions, representing a nearly 42% increase in brokered deposits. It is not appropriate for the FDIC to propose such a significant change in the market for deposits without an adequate analysis of the impacts of the Proposal.

Yet the FDIC does not attempt to calculate the costs associated with the Proposal. Instead, it repeatedly claims that the "FDIC does not have information to estimate"

---

[4] 89 Fed. Reg. at. 68245, 68256 (emphasis added).

[5] *Loper Bright Enterprises v. Raimondo* 603 U.S. __ (2024).

various costs.[6] The costs associated with the Proposal range from costs to financial institutions (such as compliance and operational costs) to risks to the financial system since the Proposal would reduce the availability of stable sources of funding and may deter institutions from taking deposits that would newly be classified as brokered. The FDIC should not engage in such a broad rulemaking that would unnecessarily destabilize its own recently settled approach without first understanding the potential costs and benefits of the Proposal.

Moreover, as the Forum and other commenters have noted to the FDIC, the Proposal does not provide sufficient data to explain why the FDIC believes it is necessary to turn back the clock on its brokered deposit regulations.[7] Indeed, FDIC Director McKernan pointed out, the Proposal "does not . . . offer any evidence that some of the deposits that this proposal would re-classify as brokered deposits actually present" the same risks as brokered deposits in general.[8]

In part this may be because in its Request for Information ("RFI") on Deposits, released simultaneously with the Proposal, the FDIC admits that it "does not have historical data" as to how "different types of deposits would behave under conditions of economic or liquidity stress."[9] As a result, the RFI on Deposits seeks input as to how data on deposits informs a bank's risk and funding stability.[10] To the extent, then, that the Proposal is motivated by the "expansion of IDI arrangements with third parties to deliver deposit products" and the stability of such arrangements,[11] it would behoove the FDIC to first consider the public comments on the RFI on Deposits as well as the FDIC and other agencies' RFI on Bank-Fintech Arrangements. As it stands now, given the FDIC's professed lack of understanding as to the riskiness of various types of deposits and the agencies' desire to "build on their understanding"[12] of third-party arrangements, the Proposal is premature at best and suggests the FDIC may have predetermined its response to the RFIs (and the Proposal) without considering any public comments.

Finally, the Proposal is part of a series of recently finalized, proposed or previewed rules from the FDIC and other banking agencies that would significantly alter the prudential framework applicable to U.S. GSIBs and other banking organizations. As such, the FDIC and other agencies should consider the effect of this Proposal along with their

---

6 *See generally* 89 Fed. Reg. 68259–60.

7 Letter from the Forum and other trade groups to FDIC (Aug 21, 2024), available *here*.

8 FDIC, Statement by Jonathan McKernan, Director, FDIC, Board of Directors, on the Proposed Brokered Deposit Restrictions (July 30, 2024), available *here*.

9 Request for Information on Deposits, 89 Fed. Reg. 63946 (August 6, 2024).

10 In a similar vein, the FDIC, together with other agencies, also released an RFI on Bank-Fintech Arrangements that seeks input related to third-party deposit placement arrangements, including liquidity considerations. Request for Information on Bank-Fintech Arrangements Involving Banking Products and Services Distributed to Consumers and Businesses, 89 Fed. Reg. 61577 (July 31, 2024).

11 89 Fed. Reg. at 68250.

12 89 Fed. Reg. at 61579.

outstanding proposals to revise the capital framework, amend rules related to total loss absorbing capacity ("TLAC") and long-term debt ("LTD") and their potential approach to revised liquidity rules. A piecemeal approach to rulemaking prevents market participants, the FDIC and other agencies from understanding the totality of regulatory changes and their impact on the banking sector and broader economy.

D. The Proposal also would impose significant hidden costs on U.S. GSIBs.

1. *The Proposal would have an outsized impact on U.S. GSIBs*.

The FDIC acknowledges that "the amount of deposits at IDIs considered brokered under the proposed rule is likely to increase" and that the increases in the amount of brokered deposits "can affect the calculation of certain regulatory ratios, such as the [LCR] and [NSFR]."[13] Despite this recognition, the Proposal fails to analyze whether the changes in classification are commensurate with the liquidity assumptions underlying the LCR and NSFR, or the ultimate costs of such reclassification. Instead, the Proposal simply states that the FDIC "cannot estimate how many IDIs . . . may incur costs associated" with the LCR and NSFR.[14]

As a general matter, the Proposal would result in deposits newly classified as brokered to be treated as riskier than they would be under the current rule for purposes of the LCR and NSFR without providing any analysis or evidence, beyond conclusory statements, that such deposits are likelier than other deposits to run during a period of stress.

Specifically, the LCR assigns a higher outflow rate to brokered deposits relative to other deposits. For example, under the current rule, retail wealth management deposits that are not part of a sweep program and for which wealth management employees earn a fee can be categorized as retail deposits with a 3%/10% outflow rate. However, under the Proposal, the fee component would make these brokered deposits, resulting in a 20%/40% outflow rate.[15] An increased outflow rate assigned to deposits reclassified as brokered would require banking organizations to hold additional, costly, high-quality liquid assets, a needless cost to IDIs that does not reflect the realities of these relationships. Similarly, relationships that leverage third-party platforms also would be captured by the broad deposit allocation prong under the Proposal, even though IDIs otherwise may have a direct relationship with the end customers. Similar to passive listing services, a third party may not have the legal authority to close the account or move customer funds to another IDI. These parties are also not involved in negotiating or setting fees and do not determine deposit allocations. Accounts are also opened directly with IDIs for such platforms, and these platforms do not themselves receive or

[13] 89 Fed. Reg. at 68259.
[14] 89 Fed. Reg. at 68260.
[15] *Compare* 12 CFR 329.32(a)(1), (2) *with* 12 CFR 329.32(g)(3), (4).

deposit any funds. As such, the presence of the third party is not germane as to the riskiness of the deposits such that classifying them as "brokered" would be inappropriate.

Similarly, brokered deposits also generally receive a lower available stable funding ("ASF") factor in calculating the NSFR. For example, retail brokered deposits generally receive a 90%, 50% or 0% ASF factor (depending on factors such as the remaining maturity of the deposit), while retail deposits (regardless of maturity) that are neither stable retail deposits nor brokered receive a 90% ASF factor, and stable retail deposits that are not brokered have an ASF factor of 95%.[16] As with the LCR, the lower ASF assigned to deposits required to be reclassified would mean that banking organizations would have to reduce their reliance on such funding and, assuming no shift in the banking organization's required stable funding, require the banking organization to increase its reliance on more costly non-brokered deposits, capital or debt, which in turn would increase costs for the economy as a whole.

These impacts to the LCR and NSFR would have an outsized effect on U.S. GSIBs, which, unlike most other banking organizations, are subject to the most stringent implementations of the LCR and NSFR. In particular, U.S. GSIBs are subject to the full daily LCR and NSFR (smaller banking organizations either are not subject to the LCR and NSFR, or subject to significantly less stringent implementations).

In addition, U.S. GSIBs are subject to the eponymous GSIB capital surcharge, which imposes on each of our member institutions a supplementary risk-based capital charge (in addition to minimum capital requirements, the stress capital buffer and any applicable countercyclical capital buffer). An increase in brokered deposits would increase a U.S. GSIB's short-term wholesale funding score, and as such, its GSIB surcharge and overall regulatory capital requirements.[17] This Proposal does not even consider the costs associated with the Proposal's capital increase for U.S. GSIBs, a particularly glaring omission at a time when the FDIC and other agencies have an outstanding proposal to drastically increase capital requirements for U.S. GSIBs.

2. *The Proposal's costs to U.S. GSIBs are not justified*.

U.S. GSIBs' sound liquidity and funding risk management practices (which are not based on arbitrary regulatory classifications) operate together with a robust and sometimes overly-conservative prudential framework to address the bank regulators' and Congress's underlying policy concerns with respect to brokered deposits, including that brokered deposits "could facilitate a bank's rapid growth in risky assets without adequate controls," banks could use brokered deposits to 'grow out' of problems, and deposit

16 *Compare* 12 CFR 329.104(c)(2), (d)(7) and (e)(2) *with* 12 CFR 329.104(b)(1), (c)(1).
17 12 CFR 217.406(b)(2)(v).

brokers and customers are prone to leave a bank due to higher rates elsewhere or problems at the bank.[18]

Specifically, U.S. GSIBs have stable funding sources and high-quality assets and engage in prudent and effective asset-liability management practices. In addition, U.S. GSIBs are subject to the highest level of prudential requirements. In particular, Regulation YY requires U.S. GSIBs to have a number of frameworks in place that have significantly enhanced the liquidity risk management capabilities of banks, including: (1) liquidity stress testing frameworks, which would capture the risk profile of their deposits, as well as corresponding liquidity buffers at the appropriate size and composition; (2) a contingency funding plan; (3) cash flow projections processes; (4) liquidity risk limits, which would capture deposit funding concentration risks; (5) a process to review new product lines and businesses; and (6) appropriate governance and senior management oversight of these frameworks.

U.S. GSIBs also must factor losses on available-for-sale securities into the calculation of their capital ratios and their compliance with TLAC requirements requires them to incur the cost of holding a minimum amount of LTD above and beyond minimum regulatory capital requirements (including a GSIB surcharge, as mentioned above). By factoring in unrealized losses in their capital requirements,[19] and by issuing sufficient amounts of eligible LTD and making other changes to support their resolvability,[20] U.S. GSIBs have reduced the likelihood of deposit runs at their subsidiary banks[21] and have substantially increased their resilience, including relative to other banking organizations.[22]

---

18 89 Fed. Reg. at 68245.

19 FDIC, Remarks by Chairman Martin J. Gruenberg on the Basel III Endgame at the Peterson Institute for International Economics (June 22, 2023) (noting that including unrealized losses in capital ratios "might have averted the loss of market confidence and the liquidity run" at Silicon Valley Bank), available *here*.

20 Letter from Kevin Fromer, President and CEO, FSF, to Financial Stability Board ("FSB") (June 28, 2019), available *here*; Letter from Kevin Fromer, President and CEO, FSF, and Rob Nichols, President and CEO, American Bankers Association, to FSB (noting "the significant progress made in achieving reform goals, specifically the substantial increases of [TLAC], the implementation of robust crisis management plans through recovery and resolution planning, and the development of legal, financial and operational strategies to support orderly resolution if required.") (Sept. 30, 2020), available *here*.

21 LTD supports the U.S. GSIBs' single-point-of-entry resolution plans. Because only a top-tier holding company would enter resolution proceedings and losses would be imposed on the holding company's equity and LTD holders, short-term creditors of the holding company's subsidiaries (such as depositors of its subsidiary bank) would be less likely to run. *See* Total Loss-Absorbing Capacity, Long-Term Debt, and Clean Holding Company Requirements for Systemically Important U.S. Bank Holding Companies and Intermediate Holding Companies of Systemically Important Foreign Banking Organizations 82 Fed. Reg. 8266, 8298 (Jan. 24, 2017).

22 *See* Sean Campbell, Capital and Beyond: Total Loss Absorbency and Financial Resiliency, Financial Services Forum (Feb. 13, 2019) (discussing cost of LTD), available *here*.

The reduced liquidity risk and increased resilience reduces the likelihood of significant deposit outflows, whether brokered or otherwise. In fact, during times of stress, the U.S. GSIBs generally experience deposit inflows and act as sources of strength and support to the broader banking sector to prevent further market turmoil and cost to the economy.

Finally, the Proposal recognizes that, as a result of reclassifying certain deposits as brokered, "an IDI's [deposit insurance] assessment may increase."[23] As a general matter, it is inappropriate for the FDIC to effectively increase IDIs' deposit insurance assessment without first understanding the size of the potential increase. More specifically, it is unjustifiably punitive to subject the U.S. GSIBs to an increased deposit insurance assessment through the Proposal even as the U.S. GSIBs are paying the majority of the FDIC's special assessment related to the invocation of the systemic risk exception in connection with the failures of Silicon Valley Bank and Signature Bank, despite not having benefited from the systemic risk exception.[24]

II. **Recommendations.**

For the reasons discussed above, we recommend that the Proposal be withdrawn. However, if the FDIC choses to finalize a rule based on the Proposal, we offer certain specific recommendations below.

A. <u>The FDIC should retain the 25% Test PPE</u>.

The Proposal would improperly narrow the scope of the existing 25% Test PPE and replace it with the Broker-Dealer Sweep Exception, as discussed below. Contrary to the FDIC's assertions, U.S. GSIBs' experience with the 25% Test PPE over the last several years has proven that the exception is useful and workable, without creating undue risk to the banking system. Accordingly, the final rule should retain the current 25% Test PPE. In this section, we highlight the key flaws of the Broker-Dealer Sweep Exception.

1. *This Broker-Dealer Sweep Exception is arbitrarily narrow*.

Limiting the availability of the Broker-Dealer Sweep Exception to only registered broker-dealers and investment advisers is arbitrarily restrictive. For example, the Broker-Dealer Sweep Exception would exclude uninsured trust companies as well as numerous types of third parties that exhibit similar profiles to SEC-registered broker-dealers such as smaller investment advisors with $100 million or less of assets under management, which are typically registered with state securities agencies, and futures commission merchants, which are regulated by the Commodity Futures Trading Commission, but may place customer funds at FDIC-insured accounts.

---

[23] 89 Fed. Reg. at 68260.
[24] *See* Letter from Kevin Fromer, President and CEO, FSF, to FDIC (July 21, 2023), available *here*.

There is no compelling reason to eliminate the availability of this PPE to this broader range of entities. As a result, we believe the FDIC's suggestion of limiting the Broker-Dealer Sweep Exception only to broker-dealers or registered investment advisers affiliated with an IDI is misguided.[25]

2. *The Broker-Dealer Sweep Exception would be improperly limited to sweep arrangements*.

Further, the Proposal would limit reliance on the Broker-Dealer Sweep Exception to only sweep arrangements, which reflect a mechanism of automatic money movement by contract to a bank. It is not clear why only funds deposited in this manner would qualify for the PPE, and the Proposal fails to adequately justify this limitation.

3. *The proposed 10% threshold is too low*.

Moreover, in proposing to replace the 25% Test PPE with the Broker-Dealer Sweep Exception, the FDIC offers no analysis as to why it seeks to more than halve the amount under administration for a particular business line to qualify for this PPE. In particular, the 10% threshold is too low and would arbitrarily exclude even sweep arrangements where the broker-dealer and registered investment adviser do place *de minimis* amounts of customer funds in deposit accounts.

In our experience, broker-dealers, investment advisers or other third-party agents or nominees typically advise their clients to retain about 10% of their investment accounts as cash. However, because changing market conditions may affect the value of securities even during periods of relatively low volatility, adherence to sound cash management practices may result in breaches of the 10% limit solely as a result of market volatility, without any change to the amount of deposits placed at a bank.

Further, often during periods of market stress, such as during the Covid pandemic or in high-interest rate environments, customers tend to increase the percentage of their assets held in cash, which is held in deposit accounts with automatic sweep features. As a result, these third parties may, as a function of the automatic sweep that moves funds to the bank as cash in customer accounts increases, become more likely to place more than 10% of their assets under administration for a business line at an IDI during these times.

Though market driven changes in consumer preferences do not negate the fact that the primary purpose of the third party "is not the placement of funds with depository institutions,"[26] the Proposal would classify such third parties as deposit brokers. The

[25] 89 Fed. Reg. at 68258.
[26] 12 U.S.C. §1831f(g)(2)(I).

25% Test PPE, unlike the proposed Broker-Dealer Sweep Exception, provides sufficient room for these fluctuations to be addressed and accounts for these cyclical events.

4. *Use of assets under management, as opposed to assets under administration, is inappropriate.*

The Proposal would use as the denominator of the Broker-Dealer Sweep Exception assets under management instead of assets under administration, as in the current rule. It is inappropriate to use assets under management for purposes of the PPE, given that assets under administration include actively managed accounts, as well as an array of passive/self-directed accounts, which are more representative of a broker-dealer's full range of services. Indeed, in many cases, cash accounts for these related businesses (i.e., actively managed and passive accounts) may be managed by the same cash management function and invested in similar assets.

5. *In total, the Broker-Dealer Sweep Exception would harm financial stability*.

These restrictions would require U.S. GSIBs to increase their holdings of high-quality liquid assets under the LCR, pursue other sources of funding under the NSFR and hold more capital as a result of increased short-term wholesale funding score under the GSIB surcharge. Particularly because increases in customers' cash holdings may coincide with periods of market stress, reclassifying these deposits as brokered would have a procyclical effect and reduce the ability of the banking system to serve as a source of stability during these events, an outcome the FDIC should want to avoid.

For these reasons, we recommend retaining the current 25% Test PPE.

B. <u>The Proposal's revisions to the definition of a deposit broker are flawed and should not be adopted</u>.

The Proposal would make several changes to the definition of a deposit broker, including removing the current rule's exception from the definition of deposit broker for third parties that place or facilitate the placement of deposits as a single IDI; replacing the "matchmaking activities" prong in the current definition of deposit broker, including the matchmaking prong's exclusion of deposits placed by an IDI's affiliate, with a deposit allocation prong; and adding to the definition persons who receive a fee or remuneration in exchange for or related to the placement of deposits. These changes are inappropriate and do not accurately reflect actual risks of these relationships.

1. *The FDIC should retain the current rule's approach to IDI affiliates because deposits gathered through affiliate relationships have mitigating factors that reduce risk.*

In addition to the harm to affiliate relationships through narrowing the 25% Test PPE, the Proposal would also harm longstanding affiliate relationships by removing the exemption from the definition of deposit broker related to IDI affiliates that propose deposit allocations between customers and affiliated IDIs on the basis that "recent experience has demonstrated" that uninsured deposits proposed or determined by third parties "do not seem to act in a more 'sticky' manner just because there is an affiliation between a broker and an IDI."[27] The Proposal's general approach is misguided because deposits gathered through arrangements with affiliates are mitigated by having a broader firm relationship with customers. Moreover, the FDIC's specific proposal with respect to the exemption for affiliates in the matchmaking prong is misguided, as the impact of that exemption is limited.

This "recent experience" that solely animates the FDIC's proposal to remove the exemption for IDI affiliates appears to be driven by a single anecdote related to First Republic Bank ("First Republic"). It is plainly inappropriate to base such a substantial change on preliminary impressions based on what is likely to be an anomalous event. It is even more inappropriate considering that neither the FDIC's review of its supervision of First Republic, nor the FDIC's Office of the Inspector General Material Loss Review of First Republic point to (or even discuss) affiliate sweep deposits as a potential cause of First Republic's failure.[28]

The Proposal's approach is particularly concerning, because the current rule represents longstanding views based on historical analyses and data. For example, in the final LCR rule, the agencies observed that, as opposed to unaffiliated sweep relationships, "[a]ffiliated brokered sweep deposits generally exhibit a stability profile associated with retail customers because the affiliated sweep providers generally have established relationships with the retail customer that in many circumstances include multiple products with both the covered company and the affiliated broker-dealer," these relationships are developed over time and because affiliates "would be incented to minimize harm to any affiliated depository institution."[29]

In addition, the FDIC's Study on Core Deposits and Brokered Deposits acknowledges that deposits gathered through affiliate sweep arrangements and through referrals from affiliates are less volatile and "pose fewer problems compared to brokered deposits in

[27] 89 Fed. Reg. at 68252.

[28] FDIC, FDIC's Supervision of First Republic Bank (Sept. 8, 2023), available *here*; FDIC, Material Loss Review of First Republic Bank (Nov. 28, 2023), available *here*.

[29] Liquidity Coverage Ratio: Liquidity Risk Measurement Standards, 79 Fed. Reg. 61440, 61493 (Oct. 10, 2014).

general."[30] Moreover, even in his dissent on the 2020 final rule on brokered deposits, now-Chairman Gruenberg acknowledged that "[b]ank affiliates, since they are part of the same organization as the bank, may be more cautious withdrawing deposits because of the corporate relationship."[31] It would be inappropriate to make policy changes that imply judgments regarding the riskiness of deposit liabilities without first reconciling these contradictory findings, including by reflecting customers' relationships with the firm in totality and analyzing the underlying characteristics of the deposit liability and the depositor.

2. *The current rule's exemption for affiliates is narrow.*

The current rule's exemption for affiliate relationships does not categorically exempt deposits gathered through affiliate relationships from being considered brokered; rather it narrowly excludes IDI affiliates that are engaged only in "matchmaking activities" from the definition of deposit brokers.[32] The exemption does not extend, for example, to IDI affiliates that place deposits at the IDI or to affiliates that have the legal authority or move a customer's funds to another IDI.[33] Though some affiliates may rely on other exemptions from the definition of deposit brokers, many others may be considered deposit brokers under the current rule.

As such, the current rule adequately addresses risks associated with affiliate relationships. Accordingly, given the FDIC's inadequate justification for the proposed change, its misplaced concerns about affiliate sweeps and recognition by Chairman Gruenberg, the FDIC and other banking agencies that deposits gathered through affiliate relationships are safer than those gathered through non-affiliates, we recommend that the FDIC retain the current rule's limited exemption for IDI affiliates.

3. *The final rule should not consider fees as part of the definition of deposit broker.*

The Proposal would include in the definition of deposit broker a person that "has a relationship or arrangement with an [IDI] or customer where the [IDI] or the customer pays the person a fee or provides other remuneration in exchange for deposits being placed at one or more [IDI]."[34] However, whether any fee is paid to a third party does not imply that the associated deposit is any riskier, and therefore, it would be inappropriate to conclude that the presence of generic "fees" are dispositive to the deposit broker determination.

---

[30] FDIC, Study on Core Deposits and Brokered Deposits (July 8, 2011) at 55–57, available *here*.

[31] FDIC, Statement by FDIC Board Member Martin J. Gruenberg on the Final Rule: Brokered Deposits and Interest Rate Restrictions at the FDIC Board Meeting (Dec. 15, 2020), available *here*.

[32] 12 CFR 337.6(a)(5)(iii)(C).

[33] *See, e.g.*, 12 CFR 337.6(a)(5)(ii); 12 CFR 337.6(a)(5)(iii)(A).

[34] Proposed 12 CFR 337.6(a)(5)(ii)(E).

Further, though the Proposal claims that this inclusion would revert back to the FDIC's approach prior to the adoption of its current brokered deposit regulations, the Proposal's breadth is inconsistent with the current rule and nearly 20 years of FDIC precedent. For example, in 2005, when it first allowed broker-dealers to sweep deposits to affiliated IDIs pursuant to a PPE, the FDIC explicitly held that the presence of "flat" fees, such as for "administrative services (such as recordkeeping and tax reporting information)," did not change its conclusion that the broker-dealer satisfied a PPE.[35] In so doing, the FDIC supported viewing these fees to be for administrative services "and not payment for the placement of deposits."[36] As such, these fees do not "reflect[] whether the involvement of the third-party intermediary [is] to earn fees . . . through placing or facilitating the placement of third-party deposits to [an] IDI," as the Proposal contends.[37]

In contrast, the Proposal provides that "[f]ees that would be covered under the proposed 'deposit broker' definition would include fees for administrative services provided in connection with a deposit placement arrangement."[38] In addition to being contrary to its precedent, the FDIC's focus on fees more generally is misplaced because there is no evidence that fees associated with certain deposit placement arrangements, including, for example administrative, recordkeeping, marketing or referral fees, would increase or even inform the riskiness of the associated deposits. Moreover, fees may be paid in connection with a variety of business arrangements that are related only incidentally to an IDI's deposit products or may be so low that they do not incentivize the placement of deposits by third parties. In such cases, third parties would be unlikely to divert deposits from one IDI to another based on amount of fees received. The Proposal's approach to fees, then, would increase the amount of deposits considered brokered without regard to their riskiness.

Accordingly, we recommend that any final rule refrain from tying the definition of deposit broker to fees. Similarly, we recommend the final rule not include an additional factor related to fees as part of a PPE application; the current rule's requirements with respect to revenue generation sufficiently addresses the FDIC's concerns in this regard.

C. <u>The Proposal's approach to notice and applications should be significantly revised</u>.

Currently, either an IDI or third party can submit a notice under the 25% Test (and Enabling Transactions PPE) and rely on the notice immediately.[39] The Proposal would require that an IDI on behalf of a broker-dealer submit a notice or application to rely on

---

35 FDIC Advisory Opinion 05-02 (Feb. 3, 2005).
36 FDIC Advisory Opinion 05-02 (Feb. 3, 2005).
37 89 Fed. Reg. at 68252.
38 89 Fed. Reg. at 68252 (emphasis added).
39 12 CFR 303.243(b)(3); 89 Fed. Reg. at 68248 ("Under the current process, the FDIC provides immediate email acknowledgement of receipt of the notice filing and the third party that is the subject of the notice may rely upon the applicable designated exception for the particular business line.")

the newly proposed Broker-Dealer Sweep Exemption, in the case of each sweep relationship.[40] The FDIC would have up to 180 days to disapprove a notice prior to an IDI being able to rely on the notice. For sweep arrangements involving multiple third parties, the Proposal would require an application, which the FDIC would have up to 240 days to approve, which period the FDIC may further extend. Moreover, the Proposal would eliminate an IDI's ability to rely on existing PPE applications, 25% Test notices or Enabling Transaction PPE notices or applications.

The FDIC's proposed review periods would begin after the FDIC deems the notice or application complete and the FDIC would be able to extend the period for review; the Proposal provides no threshold or standard for when the FDIC is permitted to extend the time to review. These opaque timelines therefore would only be workable to the extent IDIs may report deposits on their Call Report as non-brokered while the FDIC reviews a notice or application.

Moreover, because only IDIs would be able to submit notices or applications, banks would have to develop and implement operational processes and procedures to be able to complete these notices or applications, creating material and unnecessary operational costs for IDIs to simply regain approval for existing relationships that the FDIC itself determined were appropriate in its 2020 rule.

Further, in many cases, a third party is best positioned to describe the operational details of its activities and provide the information that may be required on a notice or application. For example, the third party is better able to define the scope of a line of business within its organization and provide the numerical data required to calculate whether an exception is available.

The Proposal would unnecessarily create operational costs and burdens not just for IDIs, but also for the FDIC. As Vice Chair Hill pointed out, the Proposal's approach to notices and applications will result in "an enormous avalanche of applications [that] may hit the FDIC on day 1, which the agency is completely unequipped to process in any sort of timely or efficient manner."[41] It would not be appropriate to create a new, burdensome process without clear timelines that will ostensibly require the FDIC to reallocate resources from core bank supervisory functions to conducting in-depth reviews of safe and longstanding business relationships between third parties and IDIs.

As such, we recommend that the final rule retain the current rule's approach and allow both an IDI and a third party to file notices with respect to PPEs. To the extent any final

[40] 89 Fed. Reg. at 68254, 68256.

[41] FDIC, Statement by Vice Chairman Travis Hill on the Notice of Proposed Rulemaking on Brokered Deposit Restrictions (July 30, 2024), available *here*.

rule modifies the current rule's approach, we recommend certain specific changes to the Proposal. In particular, the FDIC should:

- Grandfather previously approved notices and applications;
    - It is critical that the FDIC grandfather previously approved notices and applications, because institutions have relied on the current rule in approving the structure of those programs. To the extent the FDIC does not grandfather previously approved notices and applications, the FDIC should provide a reasonable compliance period of not less than two years. During this time, banks should continue to be able to reflect existing programs as non-brokered on their call reports until and unless the FDIC makes a determination on re-filed applications. This compliance period would allow banks to continue to carry out their existing arrangements in reliance on existing notices and approvals, while preparing to comply with the new regime by gathering information from third parties and building out the operational capabilities necessary to submit onerous notices and applications.
    - We note that the current rule provided a nine-month extended compliance period during which banks could continue relying on previous FDIC interpretations as they prepared to comply with the then-new rule.[42] Because the Proposal, as opposed to the current rule, would only allow banks to submit a notice or application, we believe a longer compliance period is warranted here.
- Incorporate a "good faith" standard with respect to any information the FDIC requests on an application or notice;
    - We recommend that the FDIC reaffirm the expectation that banks in good faith are permitted to rely on a submitted application until and unless the FDIC determines the program is not eligible.
- Clarify that, with respect to sweep arrangements that use additional third parties, a third party is not deemed to be involved in the sweep arrangement (and therefore only notice, not an application is required), if the third party only performs operational tasks related to the arrangement;[43]

[42] 86 Fed. Reg. at 6759.

[43] Relatedly, we suggest that the FDIC also clarify that a third party performs only operational tasks related to the arrangement if, based on the bank's good faith determination, the third party's involvement would not cause deposits gathered under the arrangement to be reported as brokered on the bank's Call Reports.

- Allow IDIs to report deposits as non-brokered on their Call Reports while a notice or application is pending with the FDIC; and

- Impose a maximum amount of time, which may not be extended, after which a notice or application is deemed approved if the FDIC has not otherwise acted upon it. After such time, the notice filer or applicant should be notified by the FDIC that the period of time for the FDIC's review has expired and that the notice filer and applicant may continue to consider such deposits as non-brokered, including for Call Reporting purposes. Further, the FDIC must provide affirmative notice of an approved application, either through a regularly maintained public notice (the website), or direct notice to filers.

D. Additional issues for consideration.

1. *The final rule should retain an exception for exclusive deposit placement arrangements*.

In the preamble to the current brokered deposit rule, the FDIC explained that third parties with exclusive deposit placement arrangements were "less likely to move [] customer funds to other IDIs in a way that makes the deposits less stable."[44] Without engaging with the current rule's reasoning, the Proposal would eliminate the exception from the definition of deposit broker for exclusive arrangements based on the single example of Voyager and hypotheticals about less than well capitalized IDIs obtaining all of their funding from a single third party.[45] Anecdotes and hypotheticals do not support the FDIC rapidly reversing its interpretation of the statutory term "deposit broker" without further data-driven analysis.

Accordingly, we recommend the final rule retain the exception for exclusive deposit placement arrangements. We also note that contrary to the FDIC's hypothetical, the scope of the exclusive deposit placement exception is narrow in practice as the exception requires truly exclusive relationships while most market participants have arrangements with multiple IDIs.

2. *The final rule should retain the Enabling Transactions PPE*.

The Proposal would remove the Enabling Transactions PPE but does not provide any evidence to support that removal.[46] In our view, the Enabling Transactions PPE is consistent with the plain text of the statute, which exempts from the definition of deposit

---

[44] 86 Fed. Reg. at 6745.
[45] 89 Fed. Reg. at 68245, 68253.
[46] As noted by FDIC Director McKernan, "in proposing to eliminate the enabling transactions test, the [Proposal] offers no discussion of the risks of these deposits." FDIC, Statement by Jonathan McKernan, Director, FDIC, Board of Directors, on the Proposed Brokered Deposit Restrictions (July 30, 2024).

broker, "an agent or nominee whose primary purpose is not the placement of funds with depository institutions."[47] For example, as FDIC Vice Chairman Hill noted "the primary purpose of a prepaid card network is to provide customers a mechanism to make payments, whereas placing deposits is an ancillary, but necessary, part of the business."[48]

As the FDIC's published list of companies that have submitted notices related to the 25% Test and Enabling Transactions PPE makes clear, a significant number of market participants, and therefore IDIs, rely on the Enabling Transactions PPE.[49] We do not believe that the FDIC should upend established market practice and create uncertainty without adequately justifying its new approach through a rigorous, data-driven analysis. Therefore, we recommend the FDIC retain the enabling transactions PPE. If it does not retain the enabling transactions PPE, the FDIC should, at a minimum, grandfather current relationships that rely on the enabling transactions PPE.

3. *The final rule should include a streamlined process for additional relationships to qualify for PPEs.*

The Proposal would also require IDIs to submit onerous applications to accept deposits that would be considered non-brokered from third parties that wish to rely on a PPE other than those designated in the Proposal.[50] We recommend that the FDIC instead adopt a streamlined process for IDIs and third parties to rely on additional PPEs to reflect changes in law and market conditions.

* * *

---

47 12 U.S.C. §1831f(g)(2)(I).

48 FDIC, Statement by Vice Chairman Travis Hill on the Notice of Proposed Rulemaking on Brokered Deposit Restrictions (July 30, 2024), available *here*.

49 FDIC, List of companies that have submitted notices for a Primary Purpose Exception (PPE) under the 25% or Enabling Transactions tests (Mar. 15, 2024), available *here*.

50 Proposed 12 CFR 337.6(a)(5)(iv)(I)(2).

Thank you for considering these comments. Please feel free to contact the undersigned (KFromer@fsforum.com) with any questions.

Respectfully submitted,

Kevin Fromer
President and CEO
Financial Services Forum