MEMORANDUM TO:	Board of Directors Federal Deposit Insurance Corporation
FROM:	Bret D. Edwards Director, Division of Resolutions and Receiverships
DATE:	March 21, 2019
SUBJECT:	Notice of Proposed Rulemaking: Amendments to 12 C.F.R. Part 370, Recordkeeping for Timely Deposit Insurance Determination

RECOMMENDATION

Staff recommends that the FDIC's Board of Directors (the "Board") adopt and approve for publication in the Federal Register a notice of proposed rulemaking (the "NPR" for the "proposed rule") to amend 12 C.F.R. part 370, Recordkeeping for Timely Deposit Insurance Determination ("Part 370," or the "Rule"). The proposed rule would make certain substantive revisions to Part 370 to clarify the Rule's requirements, make technical corrections, and ensure consistency with the proposed changes. The proposed rule, if adopted, would better align the Rule's burdens on covered institutions with the resultant benefits which enhance the FDIC's ability to meet its statutory obligations and policy objectives.

DISCUSSION

1. *Background*

The Board adopted Part 370 in 2016 to facilitate prompt payment of FDIC-insured deposits in the event that a large insured depository institution ("IDI") fails. Part 370 requires each IDI with two million or more deposit accounts (each a "covered institution" or "CI") to (1) configure its information technology ("IT") system to be capable of calculating the insured and uninsured amount in each deposit account by ownership right and capacity, for use by the FDIC in making deposit insurance determinations in the event of the IDI's failure, and (2) maintain

complete and accurate information needed by the FDIC to determine deposit insurance coverage with respect to each deposit account, except as otherwise provided.[1] Staff has been communicating regularly with CIs, trade associations, and other interested parties since the promulgation of Part 370 in 2016 and now proposes amending the Rule to better balance the benefits of the Rule with the burdens, provide limited relief where appropriate, and improve clarity.

2. *Proposed Amendments*

A. Elective Extension of the Initial Compliance Date

CIs must implement the IT system and recordkeeping capabilities set forth in Part 370 before their initial compliance date, which is the date that is three years after the later of the effective date or the date on which an IDI becomes a CI.[2] Part 370 took effect on April 1, 2017, with an initial compliance date of April 1, 2020 for IDIs that became CIs on the effective date.[3] Some of these CIs would benefit from additional time to implement the IT and recordkeeping requirements of the Rule. Staff proposes to amend the Rule to provide these CIs an option to extend their April 1, 2020 compliance date by up to one year (to as late as April 1, 2021) upon notification to the FDIC. The notification would need to be provided to the FDIC prior to the original April 1, 2020 compliance date and state the total number of, and dollar amount of deposits in, deposit accounts for which the covered institution expects its IT system will not be able to calculate deposit insurance coverage as of the original April 1, 2020 compliance date. This information would help the FDIC understand the extent to which the covered institution's

[1] 81 Fed. Reg. 87734 (Dec. 5, 2016).
[2] 12 C.F.R. §§ 370.6(a), 370.2(d).
[3] *Id.*; 12 C.F.R. § 370.2(d).

capabilities could be utilized prior to the extended compliance date should those capabilities be needed.

B. Compliance

Certification of compliance and deposit insurance summary report. The Rule currently requires the chief executive officer or the chief operating officer of the CI to certify that the institution is fully compliant with the requirements of Part 370 by the compliance date and annually thereafter. Staff proposes to clarify the standard to which this certification of compliance is made, which would be to the best of the executive's "knowledge and belief after due inquiry." CIs and their representatives have expressed concern that, as written now, the executive could be held liable for a violation of law should a deficiency in compliance be discovered after he or she certifies to compliance. This proposed change would clarify that the executive certify that it is his or her informed opinion that the certification is accurate.

Effect of changes to law. Future changes to law could impact a CI's compliance with the requirements of Part 370 by, among other things, changing deposit insurance coverage and related recordkeeping and calculation requirements. These changes in law may be made with immediate effect, yet CIs may need time to improve or update deposit account records or reconfigure their IT systems. Therefore, staff proposes to add a new paragraph (d) to § 370.10 to provide that a CI will not be in violation of Part 370 as a result a change in law that alters the availability or calculation of deposit insurance for a period specified by the FDIC following the change in law.

Merger. Part 370 does not expressly address mergers. Under the current Rule, a CI is required to comply with the requirements of Part 370 on and after its compliance date without regard for complications that could be caused by merger. Staff proposes to add a new paragraph

(e) to § 370.10 to provide a one-year grace period to remedy deficiencies in compliance resulting directly from a merger involving a CI. In cases where this one-year period is not sufficient, a CI would be able to request a time-limited exception for additional time to integrate deposit accounts or IT systems.

C. Voluntary Compliance

The proposed rule would add a mechanism for voluntary compliance with Part 370. Staff proposes to expand the definition of "covered institution" to include any other IDI that voluntarily opts into coverage by delivering written notice to the FDIC. Such an IDI would be considered a CI as of the date on which the FDIC receives the notification, and its compliance date would be the date on which it submits its first certification of compliance and deposit insurance coverage summary report pursuant to § 370.10(a). Staff believes that the requirements of the Rule should not be enforced upon such a CI until after it submits a certification of compliance and deposit insurance coverage report. The primary purpose for this proposed change is to enable an IDI that is not covered under Part 370 but is covered under 12 C.F.R. § 360.9 to voluntarily comply with Part 370 and be released from § 360.9 pursuant to the release provision in § 370.8(d). This would enable a banking organization with different subsidiary banks covered by one or the other of Part 370 or § 360.9 to develop a single unified deposit recordkeeping IT system that is compliant with Part 370 rather than § 360.9.

D. Deposit accounts with "transactional features"

Purpose for definition and need for revision. The proposed rule changes the definition of accounts with transactional features and alters the requirements for actions that CI's must take with regard to these accounts. The transactional features definition is used to identify the subset of alternative recordkeeping accounts (for which the covered institution is not required to

maintain all records required for a deposit insurance determination) that may contain funds to which depositors need daily access. Part 370 requires CIs make provision for timely delivery and processing of information needed for deposit insurance determinations for these accounts.

CIs have expressed concerns that the current definition is over-inclusive. An account has transactional features, under this definition, if it can be used make transfers to "third persons or others" by any of a long list of methods. This definition includes accounts that can only be used to make transfers to other accounts of the depositor or account holder at other institutions. It also includes, as accounts with transactional features, custodial accounts that support cash management or prepaid card programs, where the day-to-day transactions by beneficial owners were initiated through clearing or processing accounts maintained by program sponsors at other institutions. This created the impression that the FDIC intended that all accounts other than CD accounts had transactional features.

Staff believes that the FDIC intends the transactional features definition capture only alternative recordkeeping accounts for which an insurance determination within 24 hours following appointment as receiver is essential to fulfillment of its policy objectives. The proposed rule narrows the transactional features definition by identifying accounts primarily by reference to the third parties who can receive funds directly from the account by methods that are not reflected in the close-of-business account balance on the day of initiation of such transfer. Under FDIC rules, transfers from the bank that are included in the close-of-business account balance for an account will be completed, so any delay in completing the deposit insurance determination for such account will not create delays in processing payments. An account will have transactional features if it can be accessed by the depositor using any method that is not reflected in the close-of-business ledger balance for the account, while an account that can only

be used to make transfers to others by wire transfer – a method that is reflected in the close-of-business balance for the account if initiated prior to the cutoff time – is not an account with transactional features solely as a result of this transfer capability. Additionally, as a result of the recommended changes, accounts at the CI that support cash management or prepaid card activity indirectly (for example, by means of a clearing account maintained by a sponsor at another institution) would no longer necessarily be accounts with transactional features under the definition.

The FDIC is also concerned with accounts that support accounts with transactional features via preauthorized or automatic transfer instructions. The proposed definition of transactional features also includes accounts that feed other accounts at the CI which themselves have transactional features.

Actions required for certain accounts under § 370.5(a). The Rule currently requires that, for deposit accounts with transactional features for which a CI applies the alternative recordkeeping treatment set forth in § 370.4(b)(1), the CI certify to the FDIC that the account holder will provide to the FDIC the information needed for deposit insurance calculation within 24 hours after failure. CIs have expressed concern that this provision imposes a duty on a CI to control the actions that an account holder must take after failure, and that the certifying officer could be liable to the FDIC if an account holder does not take those actions. To reduce this concern, staff proposes to revise paragraph (a) of section 370.5 by removing the certification requirement and instead requiring covered institutions to take "steps reasonably calculated" to ensure that the account holder will provide to the FDIC the information needed for the FDIC to use a covered institution's Part 370-compliant information technology system to accurately calculate deposit insurance available for the respective deposit account within 24 hours after the

failure of the covered institution. This change should clarify that the covered institution is expected to design and implement in its information technology system the capability to use information provided by account holders after the covered institution's failure. This change should also clarify that neither the covered institution nor its employees are responsible for the actions that an account holder does or does not actually take to supply information after the covered institution's failure.

Covered institutions would have discretion to determine the methods by which this requirement may be accomplished, but a covered institution would need to satisfy two specific requirements at a minimum. First, a covered institution would need a contractual arrangement with account holders that obligates those account holders to deliver information needed for deposit insurance calculation to the FDIC in a format compatible with the covered institution's information technology system immediately upon the covered institution's failure. Second, a covered institution would need to provide a disclosure that informs account holders that the account holder's delay in delivery of information to the FDIC, or submission in a format that is not compatible with the covered institution's information technology system, could result in delayed access to deposits while the deposit insurance determination is pending.

Exceptions to § 370.5(a) requirements. Section 370.5(b) provides an enumerated list of accounts that a CI need not address in the actions required pursuant to § 370.5(a). Staff proposes to make two substantive revisions to this list. First, the proposed rule would expand the exception for mortgage servicing accounts under § 370.5(b)(1) to include all deposits in such an account. Under the current rule, mortgage servicing accounts are excepted only to the extent that they are comprised of principal, interest, taxes, and insurance. CIs have represented to the FDIC that deposits for other purposes, such as reserves, may also be held in mortgage servicers'

accounts. Removing this limitation would facilitate a CIs ability to meet the requirements of proposed § 370.5(a) with respect to those accounts.

Second, the proposed rule would provide an exception for deposit accounts maintained for the benefit of others to the extent that the deposits in that deposit account would be insured in one of three deposit insurance categories related to trusts (i.e. formal revocable trusts insured as described in 12 C.F.R. 330.10, irrevocable trusts insured as described in 12 C.F.R. 330.12, or irrevocable trusts insured as described in 12 C.F.R. 330.13). The FDIC recognizes that an account holder that places deposits with a CI on behalf of beneficial owners of those deposits may not be able to immediately provide to the FDIC all of the information needed to calculate the total amount of coverage available for deposits insured in any one of these three deposit insurance categories should the CI fail. It may take some time for an account holder to obtain such information from a trustee, who in turn may need time to review the relevant trust document and confirm the status of the trust's beneficiaries and the nature of those beneficiaries' interests in the assets of the trust at the time of the CI's failure. After the information is submitted by the account holder, the FDIC may also need to review trust documentation to verify eligibility for deposit insurance and calculation of the amount of coverage available. Completion of deposit insurance determination for these deposit accounts would occur after the required information is provided by the account holder and the timing for that information submission is within the account holder's discretion and control.

E. Recordkeeping Requirements

Alternative Recordkeeping Requirements for Certain Trust Accounts. Part 370 currently provides CIs the option of meeting the alternative recordkeeping requirements set forth in § 370.4(b)(2) rather than the general recordkeeping requirements set forth in § 370.4(a) for certain

types of trust deposit accounts insured in two of the three deposit insurance categories for trust deposits (specifically, formal revocable trust deposit accounts insured as described in 12 C.F.R. § 330.10 and irrevocable trust deposit accounts insured as described in 12 C.F.R. § 330.13). CIs must meet the general recordkeeping requirements with respect to trust deposit accounts insured in the deposit insurance category for irrevocable trust deposit accounts for which the CI is trustee that are insured as described in 12 C.F.R. § 330.12 ("DIT accounts"). Staff recognizes that the CI as trustee would need to be able to monitor for changes in facts that impact deposit insurance coverage afforded to the trust and update the deposit account records when such changes occur in order for the CI's IT system to accurately calculate deposit insurance coverage within the first 24 hours after failure should the CI be placed in receivership. Representatives of CIs have explained to FDIC staff that updating deposit account records continuously could be overly burdensome or impracticable in some cases, and that there may be a significant lag between the time at which a change occurs, the time at which the CI as trustee becomes aware of the change, and the time at which the CI can update its deposit account records accordingly for purposes of Part 370. FDIC staff acknowledges that CIs face challenges in meeting the general recordkeeping requirements for these accounts and proposes revising § 370.4(b)(2) to include DIT accounts as another category of deposit accounts for which a CI may apply the alternative recordkeeping requirements rather than the general recordkeeping requirements. The NPR solicits comment on this proposed revision to enable FDIC staff to gain a better understanding of the adverse impact of delay on the ability to access and use deposits in a DIT account while the deposit insurance determination is pending.

Recordkeeping Requirements for Deposits Resulting from Credit Balances on an Account for Debt Owed to the Covered Institution. Staff proposes to add a new subsection to § 370.4 to

provide a different recordkeeping option for a particular type of deposit found at CIs. CIs have described a recordkeeping problem that occurs when a borrower of a CI has a credit balance on a debt owed to a CI. For example, if a bank borrower has a positive balance in a loan account after receiving a credit to the account, then that credit amount would be recognized as the customer's "deposit" at the CI. In accordance with § 3(*l*)(3) of the FDI Act, such an overpayment on a debt owed to a CI would constitute a deposit; the FDIC must include (and aggregate, if necessary) such a deposit in order to perform a deposit insurance determination in the event of a CI's failure.[4] The CIs explained that the requisite information regarding the ownership of the deposit, the amount of the deposit as well as other relevant information such as a unique identifier, would be maintained on a CI's loan platform rather than on any of its deposit systems. Moreover, the deposit platforms are not linked or integrated in any way with a CI's various loan platforms. The CIs asserted that it would be prohibitively expensive for them to integrate or link the various loan platforms with their deposit systems.

In order to address the CIs concerns, staff is proposing to add a new paragraph (d), which would require that immediately upon a CI's failure, the CI's IT system(s) be capable of restricting access to (i) any credit balance reflected on a customer's account associated with a debt obligation to the CI or (ii) an equal amount in the customer's deposit account at the CI. Over the closing weekend, if access to the credit balance is not restricted, then the credit cardholder, for example, would be able to charge expenses to the credit card account which would, in effect, eliminate the credit balance. The elimination of the credit balance represents a payment of deposit insurance. Section 370.4(d)(2)(i) would require the CI to be able to generate a file within 24 hours of failure for all credit balances related to open end loans (revolving credit

[4] 12 USC 1813(*l*)(3).

lines) such as credit card accounts and HELOCs. The 24-hour requirement would only apply to consumer loan accounts where the customer or borrower has the ability to draw on the credit line without the prior approval or intervention of the CI. With respect to closed end loan accounts with overpayments, § 370.4(d)(2)(ii) would require the CI to be able to generate a file *promptly* after the CI's failure. The credit balance on a closed end loan account would not be readily available to the customer prior to the final deposit insurance calculation; consequently, there would not be as much urgency to receive and process the file in order to complete the deposit insurance determination.

F. Relief

Exception Requests. Staff proposes to revise section 370.8(b) to clarify the required elements of a CI's exception request. This proposed revision would expressly allow submission of an exception request from one or more of the Rule's requirements by more than one CI, jointly. While Part 370 currently does not preclude this, staff is proposing this revision to expressly permit it because some scenarios under which a grant of exception is appropriate are common to multiple CIs. Submission of a joint exception request should enable CIs to better manage resources, and it should enable the FDIC to streamline review of common exception requests. Each covered institution would still be required to submit the institution-specific data required to substantiate the request as required under current § 370.8(b).

Publication of FDIC's response to exception requests. Staff proposes to add a new paragraph, § 370.8(b)(2), to provide that the FDIC will publish in the Federal Register a notice of its response to each exception request. This change would facilitate transparency and enable CIs to better understand the types of requests that the FDIC would grant or deny and the reasons

therefor. The FDIC's notice of exception would not disclose the identity of the requesting CI(s) and any confidential or material nonpublic information.

Certain Exceptions Deemed Granted. Staff proposes a new paragraph, § 370.8(b)(3), that would allow a CI to notify the FDIC that, based on substantially similar facts and the same circumstances as presented in the notice published by the FDIC of relief granted to another CI, the CI is electing to use the same exception. Such exception would be considered granted subject to the same conditions stated in the FDIC's published notice unless the FDIC informs the CI to the contrary within 120 days after receipt of the CI's complete notification letter. Under this proposed change, the CI's notification letter would need to include the information required under § 370.8(b)(1), cite the applicable notice of exception published pursuant to § 370.8(b)(2), and demonstrate how the CI's exception is based upon substantially similar facts and the same circumstances as described in the applicable notice published by the FDIC. Staff believes that this proposed change would provide CIs with more flexibility and clarity with regard to the exception request process. This proposed change would also allow the FDIC to better manage its resources by minimizing time spent processing exception requests that are based on the substantially similar facts and the same circumstances as exception requests that were previously granted by the FDIC.

G. Technical Modifications

Staff also proposes to make technical amendments to certain provisions of Part 370 to clarify the Rule's requirements, make technical corrections, and ensure consistency with the proposed changes.

CONCLUSION

Staff recommends that the Board approve the notice of proposed rulemaking and authorize its publication in the Federal Register.

CONCUR:

for Charles Yi
General Counsel

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ATTACHMENTS

A – Proposed Board Resolution

B – Notice of Proposed Rulemaking for Publication in the *Federal Register*