

BROKERED DEPOSIT AFFILIATE-SUBSIDIARY
MODERNIZATION ACT OF 2018

DECEMBER 21, 2018.—Committed to the Committee of the Whole House on the State
of the Union and ordered to be printed

Mr. HENSARLING, from the Committee on Financial Services,
submitted the following

R E P O R T

together with

MINORITY VIEWS

[To accompany H.R. 6158]

[Including cost estimate of the Congressional Budget Office]

The Committee on Financial Services, to whom was referred the bill (H.R. 6158) to amend the Federal Deposit Insurance Act to exclude affiliates and subsidiaries of insured depository institutions in the definition of deposit broker, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

PURPOSE AND SUMMARY

Introduced by Representative Scott Tipton on June 20, 2018, H.R. 6158, the “Brokered Deposit Affiliate-Subsidiary Modernization Act of 2018” amends the Federal Deposit Insurance Act (12 U.S.C. 1831f) (FDIA) to exempt funds collected through an insured depository institution’s affiliate or subsidiary from the definition of “deposit broker.”

BACKGROUND AND NEED FOR LEGISLATION

Congress adopted the definition of “deposit broker”¹ in 1989² with the passage and enactment of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) [P.L. 101–73]. Congress later adopted in 1991 additional limitations on brokered deposits. Both provisions were included in legislation to address the savings and loan crisis and neither provision has been revised since they were adopted. The legislation was intended to limit the ability of weak depository institutions to use brokered deposits to grow rapidly, though there were conflicting views on the need for it. Brokered deposits are considered higher risks as the deposits have a higher probability of being withdrawn at short notice than core deposits³ because investors are seeking short-term, high interest rate investment opportunities, which some view as an artificial increase in an institution’s capital. Consequently, banks holding brokered deposits are required to have additional safeguards and are assessed higher deposit-insurance premiums as a result.

Through the Federal Deposit Insurance Corporation’s (FDIC) staff interpretations, the FDIC has traditionally given the broadest possible reading to the definition of “deposit broker” and the narrowest possible reading to various statutory exemptions.⁴ The staff interpretations do not reflect changes to the law, technology, and the marketplace over the past 25 years.

TECHNOLOGICAL DEVELOPMENTS IN FINANCIAL SERVICES

There have been significant advancements in financial services industry technology since the adoption of the “deposit broker” definition. The introduction of online banking and mobile payment products have dramatically changed the manner and geographical territories in which banks generate deposits and interact with their customers. Some banks have an online-only presence or fintech-type subsidiaries that offer deposit accounts to consumers and small businesses. New brokered deposit products, as well, have entered the market. One such product is the deposit account “sweep” program offered by many securities brokers. These sweep programs, which frequently include a transfer of excess customer cash balances to the securities broker’s affiliated bank, currently account for more than \$1 trillion of deposits in the banking system.⁵ A sweep program transfers the excess cash balances into either an uninsured money market fund or an FDIC insured bank deposit to provide additional yield and insurance coverage on those funds. The FDIC has acknowledged in both its 2011 Study on Core and

¹ Deposit brokers provide intermediary services for banks and investors, with each deposit broker operating under their own guidelines for obtaining deposits.

² 12 U.S.C. § 1831f(g)(1).

³ Core deposits are defined in the Uniform Bank Performance Report to include demand deposits, all Negotiable Order of Withdrawal (NOW) accounts, automatic transfer service (ATS) accounts, money market deposit accounts (MMDAs) other savings deposits, and time deposits under \$250,000.

⁴ See FDIC, “Guidance on Identifying, Accepting, and Reporting Brokered Deposits Frequently Asked Questions.” (Dec. 2014). Available at <https://www.fdic.gov/news/news/financial/2015/fil15002a.pdf>.

⁵ <https://www.americanbanker.com/opinion/uncertainty-chilling-broker-dealer-sweep-deposit-market>.

Brokered Deposits⁶ and the Liquidity Coverage Ratio⁷ regulations that deposits received by a bank through an affiliated broker's sweep program are more stable than other types of deposits at banks. According to the FDIC's study on brokered deposits:

In all, sweep deposits from affiliates appear to pose fewer problems compared to brokered deposits in general. These deposits would not appear to foster growth other than during an initial growth period, are not rate responsive (although they may be responsive to other investment opportunities) and may not leave when a bank is under stress.⁸

During the financial crisis data also shows that banks saw a net inflow of sweep deposits from brokerage customers as they de-risked out of securities holdings. This counter-cyclical effect increased, rather than decreased, stability for these banks in a time of uncertainty. Despite these findings, the FDIC has consistently treated deposits from sweep programs as brokered deposits. The Brokered Deposit Affiliate-Subsidiary Modernization Act addresses this issue by exempting funds collected through an affiliate or subsidiary, including employees of an affiliate or subsidiary, from the definition of "deposit broker." This change recognizes that customers of a bank's affiliates view themselves as having a relationship with the entire firm and acknowledges the stability of deposits that originate from customers of a bank's subsidiary or other affiliate.

HEARINGS

The Subcommittee on Financial Institutions held a hearing examining matters relating to H.R. 6158 on September 27, 2016.

COMMITTEE CONSIDERATION

The Committee on Financial Services met in open session on September 13, 2018, and ordered H.R. 6158 to be reported favorably to the House without amendment by a recorded vote of 34 yeas to 17 nays (recorded vote no. FC-211), a quorum being present.

COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. An amendment offered by Ranking Member Waters was not agreed to by a recorded vote of 20 yeas to 31 nays (Record vote no. FC-210). A motion by Chairman Hensarling to report the bill favorably to the House without amendment was agreed to by a recorded vote of 34 yeas to 17 nays (Record vote no. FC-211), a quorum being present.

⁶Federal Deposit Insurance Corporation, "Study on Core Deposits and Brokered Deposits" (July, 2011). Available at <https://www.fdic.gov/regulations/reform/coredeposit-study.pdf>.

⁷<https://www.fdic.gov/regulations/laws/rules/2000-5300.html>.

⁸FDIC, *supra* note 7, at 55.

Record vote no. FC-210

Representative	Yea	Nay	Present	Representative	Yea	Nay	Present
Mr. Hensarling		X		Ms. Maxine Waters (CA)	X		
Mr. McHenry		X		Mrs. Carolyn B. Maloney (NY)	X		
Mr. King		X		Ms. Velázquez	X		
Mr. Royce (CA)				Mr. Sherman	X		
Mr. Lucas		X		Mr. Meeks			
Mr. Pearce				Mr. Capuano			
Mr. Posey		X		Mr. Clay			
Mr. Luetkemeyer		X		Mr. Lynch	X		
Mr. Huizenga		X		Mr. David Scott (GA)	X		
Mr. Duffy		X		Mr. Al Green (TX)	X		
Mr. Stivers		X		Mr. Cleaver			
Mr. Hultgren		X		Ms. Moore	X		
Mr. Ross		X		Mr. Ellison			
Mr. Pittenger				Mr. Perlmutter	X		
Mrs. Wagner		X		Mr. Himes	X		
Mr. Barr		X		Mr. Foster	X		
Mr. Rothfus		X		Mr. Kildee	X		
Mr. Messer		X		Mr. Delaney	X		
Mr. Tipton		X		Ms. Sinema	X		
Mr. Williams		X		Mrs. Beatty	X		
Mr. Poliquin		X		Mr. Heck	X		
Mrs. Love		X		Mr. Vargas	X		
Mr. Hill		X		Mr. Gottheimer			
Mr. Emmer		X		Mr. Gonzalez (TX)	X		
Mr. Zeldin		X		Mr. Crist	X		
Mr. Trott		X		Mr. Kihuen	X		
Mr. Loudermilk		X					
Mr. Mooney (WV)		X					
Mr. MacArthur		X					
Mr. Davidson		X					
Mr. Budd		X					
Mr. Kustoff (TN)		X					
Ms. Tenney		X					
Mr. Hollingsworth		X					

Record vote no. FC-211

Representative	Yea	Nay	Present	Representative	Yea	Nay	Present
Mr. Hensarling	X			Ms. Maxine Waters (CA)		X	
Mr. McHenry	X			Mrs. Carolyn B. Maloney (NY)		X	
Mr. King	X			Ms. Velázquez		X	
Mr. Royce (CA)				Mr. Sherman	X		
Mr. Lucas	X			Mr. Meeks			
Mr. Pearce				Mr. Capuano			
Mr. Posey	X			Mr. Clay			
Mr. Luetkemeyer	X			Mr. Lynch		X	
Mr. Huizenga	X			Mr. David Scott (GA)	X		
Mr. Duffy	X			Mr. Al Green (TX)		X	
Mr. Stivers	X			Mr. Cleaver			
Mr. Hultgren	X			Ms. Moore		X	
Mr. Ross	X			Mr. Ellison			
Mr. Pittenger				Mr. Perlmutter		X	
Mrs. Wagner	X			Mr. Himes		X	
Mr. Barr	X			Mr. Foster		X	
Mr. Rothfus	X			Mr. Kildee		X	
Mr. Messer	X			Mr. Delaney		X	
Mr. Tipton	X			Ms. Sinema	X		
Mr. Williams	X			Mrs. Beatty		X	
Mr. Poliquin	X			Mr. Heck		X	
Mrs. Love	X			Mr. Vargas		X	
Mr. Hill	X			Mr. Gottheimer			
Mr. Emmer	X			Mr. Gonzalez (TX)		X	
Mr. Zeldin	X			Mr. Crist		X	
Mr. Trott	X			Mr. Kihuen		X	
Mr. Loudermilk	X						
Mr. Mooney (WV)	X						
Mr. MacArthur	X						
Mr. Davidson	X						
Mr. Budd	X						
Mr. Kustoff (TN)	X						
Ms. Tenney	X						
Mr. Hollingsworth	X						

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the findings and recommendations of the Committee based on oversight activities under clause 2(b)(1) of rule X of the Rules of the House of Representatives, are incorporated in the descriptive portions of this report.

PERFORMANCE GOALS AND OBJECTIVES

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee states that H.R. 6158 will exempt funds collected through an insured depository institution's affiliate or subsidiary from the definition of "deposit broker."

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX EXPENDITURES

In compliance with clause 3(c)(2) of rule XIII of the Rules of the House of Representatives, the Committee adopts as its own the estimate of new budget authority, entitlement authority, or tax expenditures or revenues contained in the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

CONGRESSIONAL BUDGET OFFICE ESTIMATES

Pursuant to clause 3(c)(3) of rule XIII of the Rules of the House of Representatives, the following is the cost estimate provided by the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, December 20, 2018.

Hon. JEB HENSARLING,
*Chairman, Committee on Financial Services,
House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 6158, the Brokered Deposit Affiliate-Subsidiary Modernization Act of 2018.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Sarah Puro.

Sincerely,

KEITH HALL,
Director.

Enclosure.

H.R. 6158—Brokered Deposit Affiliate-Subsidiary Modernization Act of 2018

Summary: H.R. 6158 would amend the definition of brokered deposits, which banks typically receive from financial brokers or other banks rather than directly from customers. Those deposits are used by the Federal Deposit Insurance Corporation (FDIC) to calculate its assessments of deposit insurance for banks with assets over \$10 billion. CBO estimates that enacting the bill would reduce the collection of those assessments, which are classified as offset-

ting receipts. A reduction in offsetting receipts has the effect of increasing direct spending; CBO estimates those increases in direct spending would total \$1.5 billion over the 2019–2028 period.

Because enacting the bill would affect direct spending, pay-as-you-go procedures apply. The bill would not affect revenues.

CBO estimates that enacting H.R. 6158 would not increase net direct spending or on-budget deficits by more than \$5 billion in any of the four consecutive 10-year periods beginning in 2029.

H.R. 6158 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA).

Estimated cost to the Federal Government: The estimated budgetary effect of H.R. 6158 is shown in the following table. The costs of the legislation fall within budget function 370 (commerce and housing credit).

	By fiscal year, in millions of dollars—											2019–2023	2019–2028
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028			
INCREASES IN DIRECT SPENDING													
Estimated Budget Authority	0	100	125	150	175	175	175	200	200	200	200	550	1,500
Estimated Outlays	0	100	125	150	175	175	175	200	200	200	200	550	1,500

Basis of estimate: H.R. 6158 would change the amount of receipts collected by the FDIC for deposit insurance by expanding the definition of who is exempt from treatment as a deposit broker and who is considered an employee of a bank under the law. For deposits at institutions with assets over \$10 billion the FDIC currently charges an assessment of between zero and 10 basis points for brokered deposits that exceed 10 percent of domestic deposits; those charges are on top of the base assessment rate of 3 to 30 basis points. Thus, the bill would affect how much banks with assets of over \$10 billion pay to the FDIC for deposit insurance.

Under current law, only people who are directly employed by an insured depository institution and are paid a salary by the institution are exempt from being considered deposit brokers. (Deposit brokers are people who place brokered deposits at banks.) Under H.R. 6158, the definition of an employee would expand to include any person who receives compensation in any form from the insured depository institution or its affiliates—usually a brokerage house connected under a corporate umbrella. Under that definition people who are not directly employed by either banks or their affiliates also could be considered employees, and thus would be exempt from treatment as a deposit broker.

The magnitude of budgetary effects would depend on how financial institutions react to the new definition of an employee. CBO expects that the broader definition in the bill would reduce assessments paid by banks to the extent that they change their organization or compensation to take advantage of the new definition. Some banks may choose not to change their corporate structure or employee compensation methods because they may prefer their current organization and methods or because deposit insurance assessments represent a small part of their annual costs. Other banks have expressed a desire to have more deposits from people who are currently considered deposit brokers but who would be exempt from the definition under the bill. H.R. 6158 would provide a financial incentive for banks to change how brokered deposits are han-

dled, but CBO expects that the probability that banks with brokered deposits would adjust their business models to reduce the FDIC assessments would equal 50 percent.

Using information from the FDIC, CBO estimates that in 2018 banks paid about \$250 million in assessments based on their level of brokered deposits. Using the growth rate for assessments incorporated in CBOs April 2018 baseline estimates for the FDIC, CBO expects that those assessments will grow to about \$400 million per year by 2028 and would total about \$3 billion over the 2020–2028 period. (CBO expects any changes would affect receipts beginning in 2020.) As a result, CBO estimates that assessments would decrease by an average of \$150 million per year over the 2019–2028 period and that implementing the bill would increase direct spending by \$1.5 billion over that period.

Uncertainty: CBO aims to produce cost estimates that generally reflect the middle of the range of the most likely budgetary outcomes that would result if the legislation was enacted. For this estimate, spending could be higher or lower because:

- Banks could choose to change their employment or compensation arrangements for brokered deposits for reasons that are unrelated to deposit insurance assessments and those changes would affect the amount of assessments they pay.
- The FDIC also could interpret the legislative language more broadly or more narrowly than CBO did, which would change the level of brokered deposits affected by the legislation, the types of compensation and employment relationships that are exempt from the brokered deposits definition, and thus the amount of assessments paid under the bill.

Pay-As-You-Go considerations: The Statutory Pay-As-You-Go Act of 2010 establishes budget-reporting and enforcement procedures for legislation affecting direct spending or revenues. The net changes in outlays that are subject to those pay-as-you-go procedures are shown in the following table.

CBO ESTIMATE OF PAY-AS-YOU-GO EFFECTS FOR H.R. 6158, THE BROKERED DEPOSIT AFFILIATE-SUBSIDIARY MODERNIZATION ACT OF 2018, AS ORDERED REPORTED BY THE HOUSE COMMITTEE ON FINANCIAL SERVICES ON SEPTEMBER 13, 2018

	By fiscal year, in millions of dollars—												
	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028	2019– 2023	2019– 2028	
NET INCREASE IN THE DEFICIT													
Statutory Pay-As-You-Go Effect	0	100	125	150	175	175	175	200	200	200	550	1,500	

Increase in long-term direct spending and deficits: CBO estimates that enacting H.R. 6158 would not increase net direct spending or on-budget deficits by more than \$5 billion in any of the four consecutive 10-year periods beginning in 2029.

Mandates: H.R. 6158 contains no intergovernmental or private-sector mandates as defined in UMRA.

Estimate prepared by: Federal costs: Kim Cawley; Mandates: Rachel Austin.

Estimate reviewed by: H. Samuel Papenfuss, Deputy Assistant Director for Budget Analysis; Theresa A. Gullo, Assistant Director for Budget Analysis.

FEDERAL MANDATES STATEMENT

This information is provided in accordance with section 423 of the Unfunded Mandates Reform Act of 1995.

The Committee has determined that the bill does not contain Federal mandates on the private sector. The Committee has determined that the bill does not impose a Federal intergovernmental mandate on State, local, or tribal governments.

ADVISORY COMMITTEE STATEMENT

No advisory committees within the meaning of section 5(b) of the Federal Advisory Committee Act were created by this legislation.

APPLICABILITY TO LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of the section 102(b)(3) of the Congressional Accountability Act.

EARMARK IDENTIFICATION

With respect to clause 9 of rule XXI of the Rules of the House of Representatives, the Committee has carefully reviewed the provisions of the bill and states that the provisions of the bill do not contain any congressional earmarks, limited tax benefits, or limited tariff benefits within the meaning of the rule.

DUPLICATION OF FEDERAL PROGRAMS

In compliance with clause 3(c)(5) of rule XIII of the Rules of the House of Representatives, the Committee states that no provision of the bill establishes or reauthorizes: (1) a program of the Federal Government known to be duplicative of another Federal program; (2) a program included in any report from the Government Accountability Office to Congress pursuant to section 21 of Public Law 111-139; or (3) a program related to a program identified in the most recent Catalog of Federal Domestic Assistance, published pursuant to the Federal Program Information Act (Pub. L. No. 95-220, as amended by Pub. L. No. 98-169).

DISCLOSURE OF DIRECTED RULEMAKING

Pursuant to section 3(i) of H. Res. 5, (115th Congress), the following statement is made concerning directed rule makings: The Committee estimates that the bill requires no directed rule makings within the meaning of such section.

SECTION-BY-SECTION ANALYSIS OF THE LEGISLATION

Section 1. Short title

This section cites H.R. 6158 as the “Brokered Deposit Affiliate-Subsidiary Modernization Act of 2018”

Section 2. Exclusion of affiliates and subsidiaries of insured depository institutions in the definition of deposit broker

This section amends Section 29(g) of the Federal Deposit Insurance Act by updating definitions.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, and existing law in which no change is proposed is shown in roman):

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, and existing law in which no change is proposed is shown in roman):

FEDERAL DEPOSIT INSURANCE ACT

* * * * *

SEC. 29. BROKERED DEPOSITS.

(a) **IN GENERAL.**—An insured depository institution that is not well capitalized may not accept funds obtained, directly or indirectly, by or through any deposit broker for deposit into 1 or more deposit accounts.

(b) **RENEWALS AND ROLLOVERS TREATED AS ACCEPTANCE OF FUNDS.**—Any renewal of an account in any troubled institution and any rollover of any amount on deposit in any such account shall be treated as an acceptance of funds by such troubled institution for purposes of subsection (a).

(c) **WAIVER AUTHORITY.**—The Corporation may, on a case-by-case basis and upon application by an insured depository institution which is adequately capitalized (but not well capitalized), waive the applicability of subsection (a) upon a finding that the acceptance of such deposits does not constitute an unsafe or unsound practice with respect to such institution.

(d) **LIMITED EXCEPTION FOR CERTAIN CONSERVATORSHIPS.**—In the case of any insured depository institution for which the Corporation has been appointed as conservator, subsection (a) shall not apply to the acceptance of deposits (described in such subsection) by such institution if the Corporation determines that the acceptance of such deposits—

- (1) is not an unsafe or unsound practice;
- (2) is necessary to enable the institution to meet the demands of its depositors or pay its obligations in the ordinary course of business; and
- (3) is consistent with the conservator's fiduciary duty to minimize the institution's losses.

Effective 90 days after the date on which the institution was placed in conservatorship, the institution may not accept such deposits.

(e) **RESTRICTION ON INTEREST RATE PAID.**—

- (1) **DEFINITIONS.**—In this subsection—
 - (A) the terms “agent institution”, “reciprocal deposits”, and “well capitalized” have the meanings given those terms in subsection (i); and

(B) the term “covered insured depository institution” means an insured depository institution that—

(i) under subsection (c) or (d), accepts funds obtained, directly or indirectly, by or through a deposit broker; or

(ii) while acting as an agent institution under subsection (i), accepts reciprocal deposits while not well capitalized.

(2) PROHIBITION.—A covered insured depository institution may not pay a rate of interest on funds or reciprocal deposits described in paragraph (1) that, at the time that the funds or reciprocal deposits are accepted, significantly exceeds the limit set forth in paragraph (3).

(3) LIMIT ON INTEREST RATES.—The limit on the rate of interest referred to in paragraph (2) shall be—

(A) the rate paid on deposits of similar maturity in the normal market area of the covered insured depository institution for deposits accepted in the normal market area of the covered insured depository institution; or

(B) the national rate paid on deposits of comparable maturity, as established by the Corporation, for deposits accepted outside the normal market area of the covered insured depository institution.

(f) ADDITIONAL RESTRICTIONS.—The Corporation may impose, by regulation or order, such additional restrictions on the acceptance of brokered deposits by any institution as the Corporation may determine to be appropriate.

(g) DEFINITIONS RELATING TO DEPOSIT BROKER.—

(1) DEPOSIT BROKER.—The term “deposit broker” means—

(A) any person engaged in the business of placing deposits, or facilitating the placement of deposits, of third parties with insured depository institutions or the business of placing deposits with insured depository institutions for the purpose of selling interests in those deposits to third parties; and

(B) an agent or trustee who establishes a deposit account to facilitate a business arrangement with an insured depository institution to use the proceeds of the account to fund a prearranged loan.

(2) EXCLUSIONS.—The term “deposit broker” does not include—

(A) an insured depository institution *or any affiliate or subsidiary of such insured depository institution*, with respect to funds placed with that depository institution;

(B) an employee of an insured depository institution *or any affiliate or subsidiary of such insured depository institution*, with respect to funds placed with the employing depository institution;

(C) a trust department of an insured depository institution, if the trust in question has not been established for the primary purpose of placing funds with insured depository institutions;

(D) the trustee of a pension or other employee benefit plan, with respect to funds of the plan;

(E) a person acting as a plan administrator or an investment adviser in connection with a pension plan or other employee benefit plan provided that that person is performing managerial functions with respect to the plan;

(F) the trustee of a testamentary account;

(G) the trustee of an irrevocable trust (other than one described in paragraph (1)(B)), as long as the trust in question has not been established for the primary purpose of placing funds with insured depository institutions;

(H) a trustee or custodian of a pension or profitsharing plan qualified under section 401(d) or 403(a) of the Internal Revenue Code of 1986; or

(I) an agent or nominee whose primary purpose is not the placement of funds with depository institutions.

(3) INCLUSION OF DEPOSITORY INSTITUTIONS ENGAGING IN CERTAIN ACTIVITIES.—Notwithstanding paragraph (2), the term “deposit broker” includes any insured depository institution that is not well capitalized (as defined in section 38), and any employee of such institution, which engages, directly or indirectly, in the solicitation of deposits by offering rates of interest which are significantly higher than the prevailing rates of interest on deposits offered by other insured depository institutions in such depository institution’s normal market area.

[(4) EMPLOYEE.—For purposes of this subsection, the term “employee” means any employee—

[(A) who is employed exclusively by the insured depository institution;

[(B) whose compensation is primarily in the form of a salary;

[(C) who does not share such employee’s compensation with a deposit broker; and

[(D) whose office space or place of business is used exclusively for the benefit of the insured depository institution which employs such individual.]

(4) EMPLOYEE.—*For purposes of this subsection, the term “employee”—*

(A) means an individual who receives compensation in any form from an insured depository institution or an affiliate or subsidiary of such insured depository institution; and

(B) includes a registered representative of a broker or dealer that is an affiliate or subsidiary of an insured depository institution.

(h) DEPOSIT SOLICITATION RESTRICTED.—An insured depository institution that is undercapitalized, as defined in section 38, shall not solicit deposits by offering rates of interest that are significantly higher than the prevailing rates of interest on insured deposits—

(1) in such institution’s normal market areas; or

(2) in the market area in which such deposits would otherwise be accepted.

(i) LIMITED EXCEPTION FOR RECIPROCAL DEPOSITS.—

(1) IN GENERAL.—Reciprocal deposits of an agent institution shall not be considered to be funds obtained, directly or indirectly, by or through a deposit broker to the extent that the

total amount of such reciprocal deposits does not exceed the lesser of—

(A) \$5,000,000,000; or

(B) an amount equal to 20 percent of the total liabilities of the agent institution.

(2) DEFINITIONS.—In this subsection:

(A) AGENT INSTITUTION.—The term “agent institution” means an insured depository institution that places a covered deposit through a deposit placement network at other insured depository institutions in amounts that are less than or equal to the standard maximum deposit insurance amount, specifying the interest rate to be paid for such amounts, if the insured depository institution—

(i)(I) when most recently examined under section 10(d) was found to have a composite condition of outstanding or good; and

(II) is well capitalized;

(ii) has obtained a waiver pursuant to subsection (c);

or

(iii) does not receive an amount of reciprocal deposits that causes the total amount of reciprocal deposits held by the agent institution to be greater than the average of the total amount of reciprocal deposits held by the agent institution on the last day of each of the 4 calendar quarters preceding the calendar quarter in which the agent institution was found not to have a composite condition of outstanding or good or was determined to be not well capitalized.

(B) COVERED DEPOSIT.—The term “covered deposit” means a deposit that—

(i) is submitted for placement through a deposit placement network by an agent institution; and

(ii) does not consist of funds that were obtained for the agent institution, directly or indirectly, by or through a deposit broker before submission for placement through a deposit placement network.

(C) DEPOSIT PLACEMENT NETWORK.—The term “deposit placement network” means a network in which an insured depository institution participates, together with other insured depository institutions, for the processing and receipt of reciprocal deposits.

(D) NETWORK MEMBER BANK.—The term “network member bank” means an insured depository institution that is a member of a deposit placement network.

(E) RECIPROCAL DEPOSITS.—The term “reciprocal deposits” means deposits received by an agent institution through a deposit placement network with the same maturity (if any) and in the same aggregate amount as covered deposits placed by the agent institution in other network member banks.

(F) WELL CAPITALIZED.—The term “well capitalized” has the meaning given the term in section 38(b)(1).

* * * * *

MINORITY VIEWS

H.R. 6158, the “Brokered Deposit Affiliate-Subsidiary Modernization Act of 2018,” would exempt affiliates or subsidiaries, as well as their employees, of depository institutions from the Federal Deposit Insurance Corporation’s (“FDIC”) limitations on brokered deposits to the extent they make deposits for their customers with their own affiliated banks.

Some brokerages that are affiliated with a bank offer cash management accounts (also referred to as “sweep accounts” or “sweep deposits”) to customers who keep cash in their brokerage accounts. These deposits would otherwise be considered brokered deposits and subject to the limitations under the Federal Deposit Insurance Act (12 U.S.C. 1831f). However, the FDIC has previously provided various administrative exemptions for these kind of sweep accounts, with certain limitations.¹ In its current form, H.R. 6158 would completely exempt these kinds of sweep accounts without any limitations.

Unlike core deposits from traditional bank customers that are typically more stable and a less costly source of funding, brokered deposits are viewed as riskier because a broker generally pools deposits from many small investors and negotiates a higher rate for the pooled certificates of deposit. The concept of brokered deposits came out of the savings and loan (“S&L”) crisis of the 1980s when risky institutions bid for deposits in the open market to shore up their balance sheets. This was considered “hot money” and unreliable as a funding base because they could be quickly withdrawn by the broker. Although restrictions were put in place, the Government Accountability Office (“GAO”) found that, similar to the S&L crisis, brokered deposits contributed to several bank failures in the 2008 financial crisis. In a report, GAO wrote that, “The failed banks also had often pursued aggressive growth strategies using nontraditional, riskier funding sources and exhibited weak underwriting and credit administration practices. . . . the use of brokered deposits, a funding source carrying higher risk than core deposits, were associated with an increased likelihood of failure for banks across all states during the period.”²

In a report required by Section 1506 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the FDIC examined the various benefits and considerations with sweep accounts. The agency wrote:

The FDIC recognizes in the examination process that sweep deposits from affiliates can be a stable source of

¹ For example, see William F. Kroener, III, General Counsel, FDIC, “Advisory Opinion—Are funds held in “Cash Management Accounts” viewed as brokered deposits by the FDIC?” (Feb. 2005), available at: <https://www.fdic.gov/regulations/laws/rules/4000-10350.html>.

² GAO, “Financial Institutions: Causes and Consequences of Recent Bank Failures,” (Jan. 2013), available at: <https://www.gao.gov/products/GAO-13-71>.

funding for financially sound institutions offering a market rate. . . . banks with an affiliate sweep program can seek a “primary purpose exception” under which a limited percentage of sweep deposits will not be considered brokered. . . . In all, sweep deposits from affiliates appear to pose fewer problems compared to brokered deposits in general. . . . While other sweeps from affiliates do not present all of the problems that traditional brokered deposits present, they pose sufficient potential problems—particularly due to their volume, dependence on the business success and strategy of an affiliate, the affiliate’s control over the deposits, and whether the deposits will leave banks once investment opportunities improve—that they should continue to come under the purview of the statute.”³

H.R. 6158 seeks to address reasonable concerns. However, in bypassing a legislative hearing on the bill, we believe the Committee was not able to fully review the bill or the appropriateness of the bill’s proposed solution. Furthermore, the day after the Committee voted to report H.R. 6158 to the full House, the FDIC announced a new initiative to conduct a comprehensive review of the current brokered deposit rules,⁴ which may ultimately result in improvements that may more appropriately address the issues the bill purports to fix.

For these reasons, we oppose H.R. 6158.

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³FDIC, “Core and Brokered Deposit Study as Mandated by Section 1506 of the Dodd Frank Wall Street Reform and Consumer Protection Act,” (July 2011), available at: <https://www.fdic.gov/regulations/reform/coredeposits.html>.

⁴FDIC Press Release, “FDIC Seeks Comment on the Treatment of Reciprocal Deposits,” (Sep. 13, 2018), available at: <https://www.fdic.gov/news/news/press/2018/pr18060.html>.