Supporting Statement

SWEEP Accounts: Disclosure of Status as "Deposit"
Within the Meaning of 12 U.S.C. 1813(l)
(Part 1 – Interim rule with request for comments)

INTRODUCTION

The FDIC is seeking approval of an interim rule requiring all insured depository institutions to prominently disclose to customers whether swept funds are deposits and the status of swept funds if the institution failed. The FDIC is adopting the interim rule concurrently with its adoption of a related final rule.

Upon the failure of an FDIC insured depository institution, the FDIC must determine the total insured amount for each depositor. 12 U.S.C. 1821(f). To make this determination, the FDIC must ascertain the balances of all deposit accounts owned by the same depositor in the same ownership capacity at a failed institution as of the day of failure.

In January of this year the FDIC published a proposed rule composed of two parts ("proposed rule").[1] The first part proposed FDIC practices for determining deposit and other liability account balances at a failed insured depository institution. The second part proposed requirements for the largest insured depository institutions to adopt mechanisms that would, in the event of the institution's failure: (1) provide the FDIC with standard deposit account and other customer information; and (2) allow the placement and release of holds on liability accounts, including deposits.

The comment period for the proposed rule ended on April 14, 2008. Based in part on the comments received on the proposed rule, the FDIC has decided to finalize the proposed rule by issuing two separate rulemakings: (1) the interim rule, (a) covering part one of the proposed rule, and (b) proposing a disclosure requirement regarding the insured status of sweep accounts; and (2) a separate final rule, covering part two of the proposed rule ("Large Bank Modernization Final Rule"). The subject of this Supporting Statement is the proposal set forth in the interim rule to implement a new disclosure requirement regarding the insured status of sweep accounts.

The term "sweep accounts" generally refers to contractual, automated transfers of funds by insured depository institutions from a deposit account to a non-deposit account or investment vehicle. The interim rule addresses how the FDIC will treat sweep accounts upon an insured institution failure. The result is that, in many cases, the swept funds will not be treated by the FDIC as deposit obligations of the failed institutions. This means that the swept funds will not be eligible for deposit insurance coverage and will not be afforded status as a deposit under the depositor preference statute.

Except as noted, the FDIC practices defined in the interim rule represent a continuation of long-standing FDIC procedures in processing such balances at a failed depository

[1] 73 FR 2364 (Jan.14, 2008).

institution. The interim rule applies to *all* insured depository institutions and is the subject of this Supporting Statement.

A. JUSTIFICATION

1. Circumstances and Need

Circumstances.

The interim rule would require, subject to an extended delayed effective date, depository institutions offering sweep products to disclose whether the swept funds are deposits for insurance purposes and, if not, how these funds would be treated in the event of failure.

Need for a Rule.

The FDIC is concerned that the treatment of swept funds in the event of failure is not clearly understood by sweep customers. A better understanding of this treatment by sweep customers is important to avoid misconceptions which may arise in the event of failure. While many institutions currently provide some disclosures to sweep customers, the FDIC believes the significance of the consequences to depositors of some sweep transactions necessitates consistent disclosures by institutions providing sweep services. In this context, it is particularly important for institutions to disclose to sweep customers that the completion of some sweep transactions may result in their funds being subject to treatment as general creditor claims.

Limitations of current processes.

Currently, there are no affirmative, consistent disclosure requirements regarding the insured status of sweep accounts.

Delayed Implementation

Insured depository institutions have until July 1, 2009 to fully implement the disclosure requirements.

2. Use of Information Collected

The disclosures this rule would require are important because the completion of some sweep transactions may result in customers' funds being subject to treatment as general creditor claims. A better understanding of this treatment by sweep customers is important to avoid misconceptions which may arise in the event of a failure.

3. Use of Technology to Reduce Burden

Not applicable.

4. Efforts to identify duplication

Not applicable.

5. Minimizing Burden on Small Entities

The interim rule imposes a disclosure requirement on all insured depository institutions offering one or more sweep account products. This requirement is subject to an extended delayed effective date to allow the FDIC to consider specific comments on the disclosure requirement before insured depository institutions must comply with it. Preliminarily, the FDIC believes the disclosure requirement in the interim rule will not have a substantial impact on a substantial number of small banking organizations, mainly because such entities are much less likely than larger insured depository institution to offer sweep-account products. Such products are typically offered by insured depository institutions serving large commercial and institutional customers.

6. Consequences of Less Frequent Collections

Not applicable.

7. Special Circumstances

None.

8. Consultation with Persons outside the FDIC

The FDIC received twenty-one comments in response to parts one and two of the proposed rule. A summary of the comments regarding the treatment of sweep accounts is set forth below. Through this interim rule, the FDIC is soliciting comments regarding the disclosure requirements applicable to sweep accounts.

Treatment of sweep account arrangements in general
Commenters supported at a very general level the establishment of a regulation intended to resolve the legal confusion brought about by the decision in *Adagio.* Commenters recommended that the FDIC limit any regulation to addressing only the legal confusion raised in *Adagio*. One banking trade group suggested this could be done by language to "explicitly provide that all automated sweep arrangements that are codified in contract will be recognized as part of the day's business and reflected in end-of-day ledger balances, regardless of when the transactions are processed." Another banking trade association noted its "greatest concerns relate to the FDIC's

extensive new proposals relating to the treatment of sweep products. Sweep transactions have been an extensively used business practice for decades, enabling banks to secure substantial funding at reasonable costs and their customers to achieve their financial objectives. Any proposal that disrupts the existing treatment and expectations of institutions and their customers vis-à-vis sweeps would potentially impair the viability of sweeps with very serious and unpredictable consequences."

To provide consistent treatment among the various sweep products, several commenters suggested the FDIC should do away with the internal versus external distinction between sweep transactions as well as the Class A versus Class B distinction. "We urge the FDIC to eliminate these unnecessary distinctions, to the extent that the FDIC proceeds with rulemaking around sweeps at all, and treat similar sweep products the same, despite different methods used by banks for processing the necessary transfers and posting the relevant accounts."

9. Payment or Gift to Respondents

No payments are made to respondents.

10. Confidentiality

No individual bank or customer information will be made available outside the FDIC.

11. Questions of a sensitive nature

No questions of a sensitive nature are involved.

12. Estimate of Annualized Burden and Associated Costs

Estimated Number of Respondents: 1,170 to 1,970.
Estimated time per response: 25 – 49 hours per respondent.
Estimated Total Annual burden: 28,870 – 84,400 hours.

Background/General Description of Collection: The interim rule contains collections of information pursuant to the Paperwork Reduction Act (44 U.S.C. 3501 et seq.) ("PRA"). In particular, the interim rule requires, subject to an extended delayed effective date, depository institutions offering sweep products to disclose whether the swept funds are deposits for insurance purposes and, if not, how these funds would be treated in the event of failure.

Estimated costs: Compliance with the disclosure requirement will require insured depository institutions offering sweep products, which do not currently provide adequate disclosures, to modify their sweep account documentation, including customer account statements, to include new language indicating whether swept funds are a deposit for insurance purposes and, if not, how such funds would be treated in the event of failure. Further, additional documentation may be provided to sweep customers as part of a statement mailing on a one-time basis. Implementation cost will be mitigated by the delayed effective date of this requirement. Sweep account documents must be reprinted periodically in any case, and the cost of including the disclosure requirement should be minimal. Further, most insured depository institutions already make certain disclosures to customers, and the new requirements would simply replace these disclosures. After implementation, on-going cost should be negligible. Future printings of sweep account documentation will have to be conducted in any case to replenish stock, and the disclosure requirement should not add to the cost of such printings given its brief nature. Customer account statements would continue to be provided according to normal business practices. Further, staff training must be conducted periodically, and the disclosure requirement should not materially add to the length or complexity of this training.

13. Capital Start-up and Operation /Maintenance Costs

Implementation costs will vary based on the size, nature and scope of the depository institutions sweep programs. It is estimated that compliance costs for the very largest and super-regional banking organizations are between $25,000 and $50,000 while smaller regional organizations were placed at $10,000 to $20,000. Other large organizations (those with at least $2 billion in total assets) were assigned a cost estimate of $1,500 to $3,000. Costs for community banks were estimated to be between $1,000 and $2,000. Under these assumptions, the overall disclosure costs are estimated to be between $1.73 million and $3.46 million at the lower end of the number of institutions believed to be engaging in sweep operations (1,170). If as many as 1,970 depository institutions maintain sweep operations the total costs are estimated to range between $2.53 million and $5.06 million.

Based on the above cost estimates the number of hours needed to meet the disclosure requirements per institution is calculated as follows. $1.73 million ÷ 1,170 institutions = $1,480 per institution. Assuming an hourly cost of $60 for employee time generates the minimum time estimate of 25 hours per institution. The upper range of cost the cost estimate is $2,960 which is equivalent to 49 hours ($3.46 million ÷ 1,170 institutions ÷ $60 hourly employee cost = 49 hours). Total hours are estimated at a minimum as: ($1.73 million ÷ $60 hourly employee cost = 28,870 hours) and at the upper range as: ($5.06 million ÷ $60 hourly employee cost = 84,400 hours).

14. Annualized cost to the Federal Government

None.

15. Reason for Change in burden

Not applicable.

16. Publication

There will be no publication.

17. Display of Expiration Date

Not applicable.

18. Exceptions to certification

No exceptions.

B. STATISTICAL METHODS

Not applicable.