

BANKING & FINANCIAL SERVICES ECONOMIC RECOVERY

FDIC TRANSACTION ACCOUNT GUARANTEE PROGRAM – TRANSITION TO NEW STRUCTURE

by John K. Lawrence
September 2010

At its Board of Directors meeting on September 27, the Federal Deposit Insurance Corporation (“FDIC”) confirmed that its Transaction Account Guarantee (“TAG”) program will expire as scheduled on December 31, 2010. The expiry of the TAG will coincide with the effectiveness of a new temporary deposit insurance program contained in the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). The terms of the new program, embodied in a proposed regulation, are not the same as the expiring TAG program, and will require insured banks and savings banks to provide customer notices.

Background

The TAG was created by the FDIC in October, 2008, as part of the Federal government’s emergency response to the crisis in the financial services sector. The TAG represented a temporary program to provide unlimited deposit insurance for specified forms of transaction accounts held at those insured depository institutions (“IDI”) that chose to participate. In the intervening two years, the FDIC has modified the terms of the TAG and extended its duration.

Currently, the TAG applies to noninterest bearing transaction accounts, interest-bearing negotiable order of withdrawal (“NOW”) accounts paying interest at 0.25% per annum or less, and so-called Interest on Lawyers Trust Accounts (“IOLTA”) held at participating IDIs. The TAG regulations specify that it will expire on December 31, 2010.

Dodd-Frank Act’s New Structure

In Section 343 of the Dodd-Frank Act, Congress amended the Federal Deposit Insurance Act to create a separate, statutory form of temporary deposit insurance for holders of noninterest bearing transaction accounts, as defined. This insurance, which comes into force on December 31, 2010, is unlimited in amount, and will continue through December 31, 2012. The FDIC regards the Dodd-Frank Act program as intended by Congress to supersede TAG, and has proposed a regulation to effect a transition from TAG to the new statute. The Dodd-Frank Act program differs from the TAG in several important respects.

The temporary deposit insurance under Dodd-Frank will apply at all IDIs. Unlike under the TAG, no action, either to opt-in or to opt-out, will be required by any IDI. Moreover, unlike the TAG, no additional deposit insurance assessment will be made to banks for the temporary Dodd-Frank deposit insurance coverage.

The temporary Dodd-Frank deposit insurance will not apply, however, to all the types of accounts that are currently eligible for TAG coverage at participating IDIs. In the Dodd-Frank Act, Congress restricted the coverage to transaction accounts with respect to which interest is neither accrued nor paid. The proposed rule announced by the FDIC follows the statutory restriction.

As a result, those low-interest-bearing NOW accounts and IOLTA accounts at IDIs participating in the TAG which are now covered by the TAG temporary insurance will lose that unlimited amount coverage after December 31, 2010. After that date, those accounts will be included in the calculation of the general Federal deposit insurance maximum applicable to each depositor, which is now \$250,000.

Notice Requirements

In view of those differences, the FDIC is concerned about customer confusion. As a result, the proposed regulation would require several notices to be given by IDIs. First, every IDI that offers noninterest-bearing transaction accounts, whether or not participating in TAG, would be required to post a prescribed lobby notice in each office and on its website, if it offers Internet deposit services. The text of the notice explains the effect of Section 343 of the Dodd-Frank Act.

Institutions which currently participate in TAG would be required to furnish a further, individual, notice to each depositor holding a low-interest NOW account or IOLTA. These notices, which would be required to be mailed not later than December 31, 2010, would explain that NOW accounts and IOLTAs currently covered in full by deposit insurance under TAG will no longer be insured in full, but will instead be insured under the general insurance rules up to a maximum of \$250,000. The FDIC proposal suggests that electronic mail would be permissible as the means of delivery for those depositors who ordinarily receive account information in that manner.

In addition to those transition notices, the proposed regulation would create a new, continuing notice requirement. Any IDI that offers account products in which funds are automatically transferred, or “swept,” from one account to another, or that modifies account terms in such a way as to result in funds no longer being eligible for full insurance coverage, would be required to furnish a written notice clearly advising affected depositors that such actions will affect their deposit insurance coverage. This notice requirement is proposed in anticipation of the effect of Section 627 of the Dodd-Frank Act, which will permit IDIs to pay interest on demand deposit accounts, effective in July, 2011. Thus, if an IDI were to modify the terms of its demand deposit accounts to permit payment of interest, it would be required to notify affected customers that the account would no longer qualify for unlimited deposit insurance as a noninterest-bearing transaction account.



The FDIC has requested comments on the proposed rule. They must be submitted by October 15, 2010. Although the rule is only in proposed form, the stated intention of the FDIC to permit TAG to expire is clear. Accordingly, institutions may wish to prepare for the required notices and staff training needed to ensure a smooth transition to the new arrangements for customers.

FOR MORE INFORMATION, CONTACT:



John K. Lawrence is a member in Dickinson Wright's Detroit office and can be reached at 313.223.3616 or jlawrence@dickinsonwright.com.