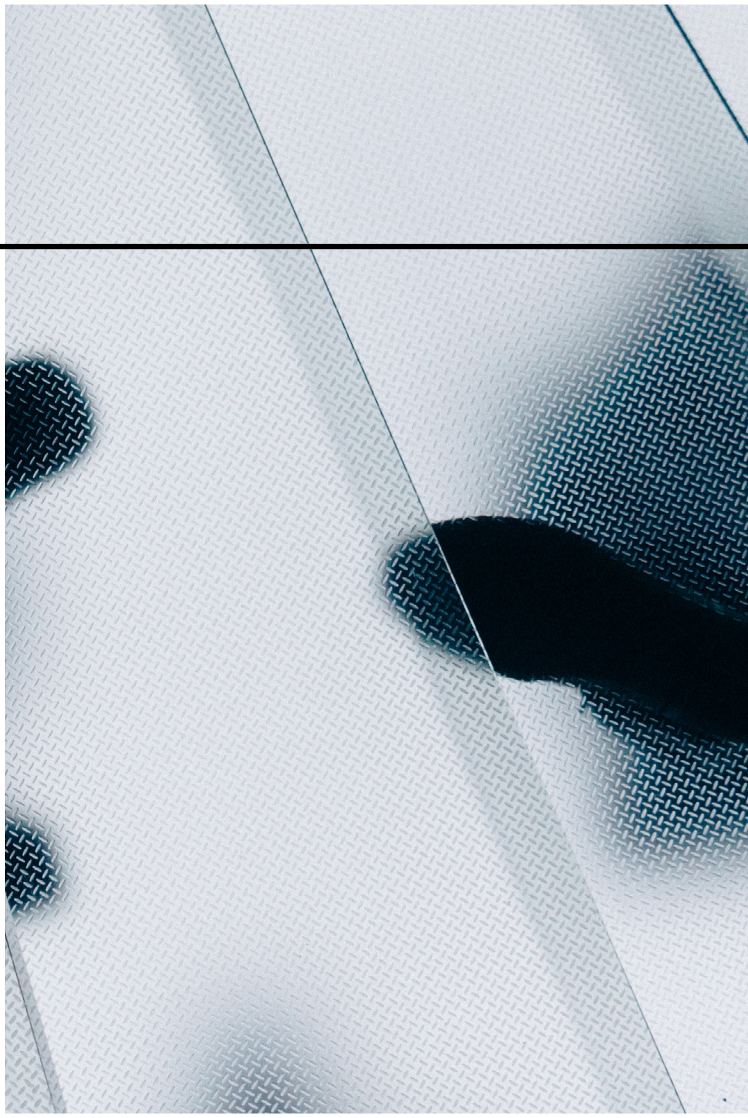
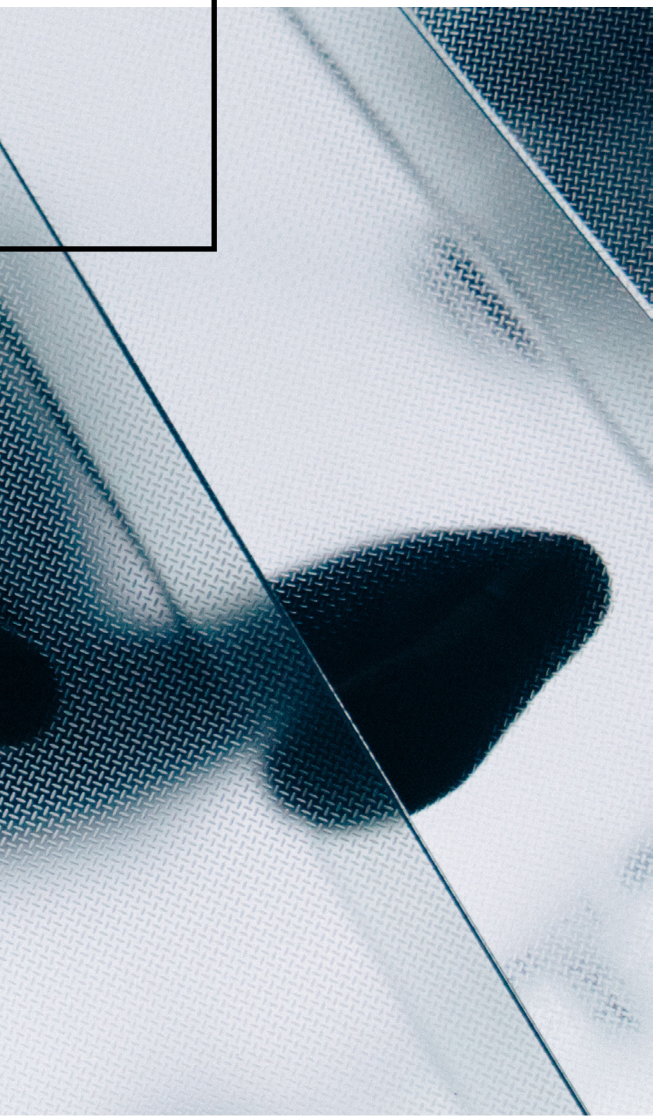
FDIC

RECORDKEEPING FOR TIMELY INSURANCE DEPOSIT DETERMINATION

CAPCO

White Paper





Introduction

More than 400 banks have failed since 2009. In nearly every case, the Federal Deposit Insurance Corporation (FDIC) has played a critical role in the successful resolution of the failed institutions. If the FDIC cannot facilitate the sale of failed bank to a healthy bank, the FDIC promptly pays the failed institution's depositors the full amount of their insured deposits. Depositors' ability to rely on the FDIC for protection provides financial stability and maintains confidence in the U.S. banking system.

The FDIC strives to pay depositors within one business day of a bank failure. For some time, the FDIC has been concerned that the size and complexity of the largest banks would preclude it from maintaining this level of efficiency . Deposit insurance coverage is necessarily based on an individual bank's data. In large banks, the relevant data is frequently maintained in multiple information technology systems, and the insurance coverage calculations may be complicated (e.g., with certain types of accounts) or delayed (e.g., when data is missing). To mitigate this risk of delayed payment, the FDIC issued a new rule in February 2017 specifying recordkeeping and compliance requirements..

The new rule – Recordkeeping for Timely Deposit Insurance Determination – has significant implications for affected banks. The rule specifies that banks must reach compliance by April 1, 2020, and large banks will likely need the entire three years to address the requirements fully. This white paper provides information on the rule, presents a framework for response and outlines how Capco and FIS are uniquely positioned to support this effort.

Overview and implications

Currently, the FDIC estimates deposit insurance required for banks based on their call report submissions that contain information on deposit balances and covered accounts. The new rule effectively shifts responsibility for deposit insurance calculations from the FDIC to the largest banks by requiring banks to assess their deposit accounts, understand and appropriately handle beneficial ownership and calculate the insurance coverage needed. This shift will provide FDIC with the confidence that they are adequately covered and that they can make payments to depositors promptly should one of these complex institutions fail. Additionally, banks and customers will have improved visibility of insured and uninsured funds, because deposit insurance coverage will be known on an ongoing basis.

Banks with two million or more deposit accounts need to:

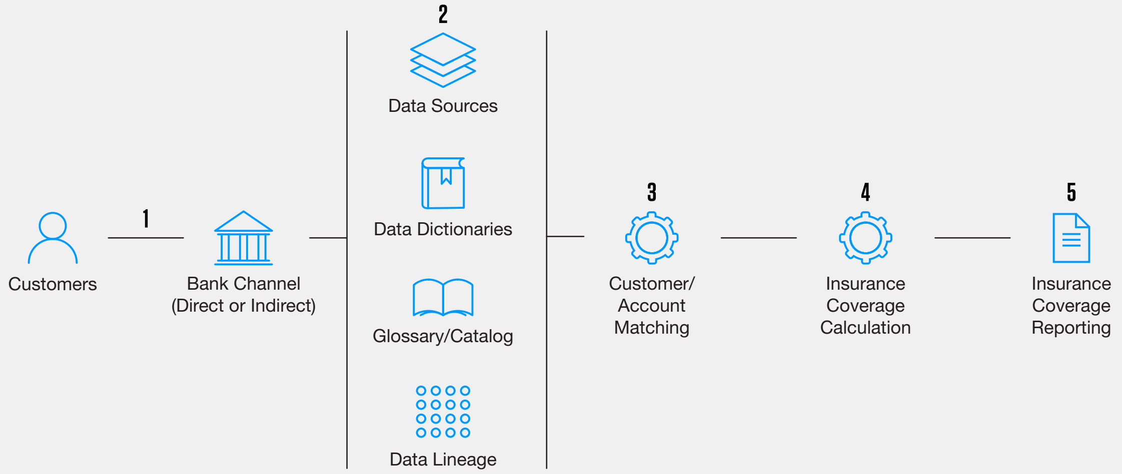
- Capture all necessary data and make sure that it is current and accurate. This includes data captured on new accounts, as well as identifying and bridging data gaps for existing accounts.
- Configure their information technology systems to calculate deposit insurance coverage according to FDIC rules.
- Ensure supporting documentation and physical records (e.g., signature cards) are complete and accurate for all potentially relevant accounts.
- Meet alternative recordkeeping requirements for certain accounts (e.g., deposit accounts held in a trust) and certify that the needed information would be provided to the FDIC in the event of a failure.[2]

To envision the impact of the rule, consider its essence: the ability to calculate a customer's deposit insurance coverage on any given day. This encompasses:

- Identifying the customer and all insured deposit accounts accurately
- Understanding beneficial ownership to establish data gathering requirements
- Collecting necessary data at account opening
- Obtaining current account balances and applying FDIC rules for deposit insurance coverage (e.g., taking into account full and partial ownership)
- Producing reports and data files according to FDIC requirements

To enable this, large banks will likely need to consider changes to processes, procedures and systems. Figure 1 illustrates potential changes across the bank, from the point of customer interaction through operations.

2 - FDIC Final Rule, 12 CFR Part 370, 11/15/2016



	Requirement	Challenge / Opportunity
1	Whether opening a new account or changing an existing account, appropriate customer information and documentation is collected.	Need to address imaging in both direct and indirect channels. Additional complexity with third parties.
2	Information and documentation is stored efficiently and securely. Data is available for all required activities.	Significant effort given the multitude of data-related projects that most banks have in flight.
3	Ongoing matching of covered accounts to customers is performed to maintain a current view of coverage.	Challenges typically include multiple systems of record, data availability and data quality.
4	Insurance coverage is calculated based on current account balances. Testing and other related procedures are facilitated.	Entirely new capability for which vendor and custom options may be considered.
5	Regulatory and management reports are automatically produced.	In addition to required reporting, new value-added information and services (e.g., insurance coverage alert) may be enabled.

Figure 1 - Conceptual Future State

Ongoing compliance will require rigor. Compliance includes annual certification of implementation and testing by either the CEO or COO and annual submission of a deposit insurance coverage report. Furthermore, the FDIC will conduct periodic on-site inspections and tests to confirm that each bank's IT systems can calculate deposit insurance coverage accurately in the event of failure.

Multiple factors make it challenging for banks to develop a solid plan, let alone actually reach compliance. Figure 2 presents a summary of these challenges.

A substantial part of the three-year implementation timeframe will be needed to address technology-related changes; deposit systems, applications and related interfaces will all need to be modified. A significant effort may be needed to address data gaps. Lastly, changes to certain business processes will require time to implement, particularly where training needs to happen.

The work and time involved underscores the need for banks to rapidly define a plan and begin implementation.

Complex Operations

Need to access multiple sysyems for accounts and relationships (e.g., different application for domestic and international).

Need to address storage and retrieval of customer-related documentation.

Customer Expectations

Potential impact to customer relationship when addressing information gaps.

Change in customer experience when opening new accounts.

Resource Constraints

Multiple risk and regulatory projects in parallel that take considerable amount of subject matter expert (SME) time.

SMEs pulled in multiple directions between ongoing responsibilities and special initiatives.

Costly IT Development

Increased importance of accurate and comprehensive common customer identifier.

New data elements (ownership right and capacity codes).

Insurance calculation capability.

Continuous updates among all parties.

Regulatory Pressure

Continuously evolving regulatory environment.

Linkages to other requirements, e.g., KYC.

Desire for Agility

Integration among multiple legacy systems.

Integration with third parties.

Real time deposit insurance status and account updates.

Figure 2 - Common Challenges for Large Banks

Framework for response

Capco believes there are three components to a successful response:

1. A **structured approach** to scoping and managing this compliance initiative.

2. A strategic and holistic view of **managing data**.

3. A comprehensive evaluation of **technology and systems** to identify the appropriate solution.

STRUCTURED APPROACH

Banks that attempt to address the rule with a loosely defined approach are accepting multiple risks, e.g.:

- Incomplete analysis may yield incorrect or missing business requirements.

- Definition of a suboptimal solution could result in future enhancements and projects.

- Incomplete data or poor data quality may create errors in calculating deposit insurance coverage.

- Missed automation opportunities could lead to manual workarounds.

These risks collectively contribute to the biggest risk of all: inability to manage compliance with the FDIC rule effectively and efficiently.

Capco assists clients with a wide range of transformation efforts, including compliance initiatives. We utilize a structured approach that has proven to deliver expected results on time and within budget. Aspects of our approach include:

- Definition of the compliance strategy.

- Analysis of issues and options, leading to definition of requirements.

- Detailed technology analysis and planning.

- Effective program management through deployment.

MANAGING COMPLIANCE DATA

Data management is a critical capability for all financial institutions, and effective management of data can ease the burden of managing ongoing compliance and even turn compliance into a strategic activity.

Most banks fail to reach the full potential of strategic compliance data management for a variety of reasons, for example: demands from operating a complex technology environment, ongoing flow of new regulations and requests from regulators, and insufficient resources to define and manage an integrated technology/data strategy.

In our experience, this type of compliance initiative only reaches full success if it logically relates to all other initiatives, or at minimum all interdependent or related initiatives. If each initiative essentially stands alone, duplication inevitably results and leads to a complex cost-inefficient environment. A comprehensive data supply chain solution is central to achieving compliance within the prescribed timeframe and to maintaining an efficient compliance program.

TECHNOLOGY ANALYSIS

Ideally, a solution to this rule will fully automate all relevant processes and activities. Specific capabilities that should be examined carefully include: insurance coverage calculation, data management, document management and reporting. Most banks will need to compare detailed requirements with current and planned functionality and determine how to close gaps.

Large banks should be able to define alternative solutions that have different tradeoffs. Confidence in the final recommendation – and typically the speed with which it will be approved – depends on the quality of the analysis. We recommend to clients a comprehensive and methodical analysis of data and technology that yields a strong fact base and supporting logic for any recommendations. In situations where new technology is being considered, we suggest conducting a vendor scan to explore the cost/benefit of adding a new system or application.

How Capco can help

Capco and FIS are uniquely positioned to assist large banks with this new rule. First and foremost, we bring deep expertise and experience that starts with a **special relationship with the FDIC**. The FIS Center of Regulatory Intelligence provides the latest intelligence, thought leadership, and leading-edge regulatory insight into risk and compliance issues facing the financial services industry. Additionally, FIS has managed resolutions and receiverships for financial institutions, including FDIC Bridge and Deposit Insurance National Bank events.

Second, we bring **deep experience with core systems and data**. Our ongoing risk and compliance work gives us a detailed understanding of how banks can align compliance, technology and data strategies. Furthermore, for banks utilizing FIS core systems, we have unparalleled knowledge of the platforms. We continually monitor compliance requirements and work with clients to revise our systems appropriately.

Third, we have **strong transformation and implementation capabilities**. We focus solely on delivering change within financial services, so our resources bring deep domain expertise. Our clients trust us with their critical and strategic initiatives, and we pride ourselves on our record of successful delivery.

Lastly, we are mindful of our clients' need to operate quickly, yet cost-effectively. We bring several **accelerators, tools and templates** to each initiative to launch programs quickly and proceed with high confidence that all issues are being addressed and that the final solution will be the best possible one.

Appendix

Achieving compliance with the newly finalized rule on Recordkeeping for Timely Deposit Insurance Determination is no small task. Specific activities – including defining and capturing key data elements, reconciling those elements with other enterprise data and performing the deposit insurance coverage calculations – are net new and need to be integrated with banks' ongoing operations and compliance efforts. Banks should consider a comprehensive data supply chain solution to gather information, streamline activities and support execution of the bank's overall compliance strategy in the most efficient manner possible to meet the new regulatory requirements.

Rule Section	Selected Details
Covered Institutions	Banks with 2 million or more deposit accounts (as measured on FDIC Call Reports) for two consecutive quarters preceding the effective date (or thereafter). 38 banks covered as of June 30, 2016. A bank may apply for exemption if in policy and operation it does not take deposits from accountholders that in aggregate surpass the maximum coverage amount. A bank may seek relief from compliance if it falls below the threshold for three consecutive quarters.
IT System Requirements	Required functions include: • Accurate calculation of deposit insurance coverage for each account. • Generation and retention of output in the FDIC-specified format and layout. • In the event of failure, restriction of access to deposits in an account until the FDIC has made its insurance coverage determination. And • Debiting from each account the amount that is uninsured (i.e., adjusting account balance so only insured deposits are made available). The functions must be capable of being executed within 24 hours of FDIC designation as receiver.
General Recordkeeping Requirements	In deposit account records, the information must include a unique identifier for each: • Account holder. • Beneficial owner (if different from account holder). • Grantor and each beneficiary, if deposit account held in connection with an informal revocable trust (e.g., payable-on-death accounts, in-trust-for accounts). • Grantor and each beneficiary, if deposit account held by covered institution as trustee of an irrevocable trust. The information must include the applicable ownership right and capacity code as specified by the FDIC.

Alternative recordkeeping requirements	For accounts whereby the covered institution does not maintain the information needed to meet the general requirements (e.g., brokered accounts, deposits in trusts), the minimum information includes: • Unique identifier of account holder. • Pending reason code as specified by FDIC. For revocable/irrevocable trusts for which the covered institution does not maintain the information to calculate insurance coverage, the minimum information includes: • Unique identifier of account holder. • Unique identifier of grantor if account has transactional features. • Pending reason code as specified by FDIC.
Implementation	The compliance date is three years after the effective date of the rule (FDIC anticipates effective date of April 1, 2017, which sets the compliance date at April 1, 2020). Provision for applying for an extension exists, and the FDIC may potentially grant an extension that is conditional or time-based. The FDIC may accelerate the implementation date for an individual institution under certain conditions (e.g., undercapitalized, excessive risk, liquidity stress) and in consultation with the institution's banking agency.
Relief From Compliance	A covered institution may apply for exemption if it demonstrates that it does not take deposits from any account holder that would exceed the standard maximum deposit insurance amount. Covered institutions may request exceptions from any specific aspect of the requirements if it can demonstrate circumstances that "make it impracticable or overly burdensome" to meet the requirements. Covered institutions may apply for release from compliance if it has fewer than 2 million deposit accounts for three consecutive quarters after becoming a covered institution.
Communication With FDIC	Within 10 business days of the effective date (or becoming a covered institution), a covered institution must notify the FDIC of the person responsible for implementing the required capabilities.
Compliance	Certification must be submitted to the FDIC on or before the compliance date and annually thereafter: • Certification must confirm implementation and testing for the preceding calendar year and be signed by the CEO or COO. • The deposit insurance coverage report must contain the information and statistics specified by the FDIC. FDIC testing of compliance will begin within a quarter of the initial compliance date and occur no more frequently than a three-year cycle thereafter.
Ownership Right and Capacity Codes	Specific codes have been defined by the FDIC and must be followed.
Output Files	Covered institutions must have the capability to prepare and maintain four files, each with a specific data format: • Customer file • Account file • Account participant file • Pending file The unique customer identifier is paramount as it serves as the link across the four files.

About the authors

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Sandeep Vishnu is a partner at Capco, where he leads the Data & Analytics and Risk & Finance practices for North America. He focuses on risk management, financial analysis, data supply chain, data science, management/regulatory reporting, compliance and operational/control issues for banks, asset managers, insurers and other financial service firms. Over the course of his career, he has developed risk, compliance, information security and data/information management programs for several financial institutions. These have included creating ERM and ORM programs, establishing the office of the CDO, setting up data supply chains for integrated management and regulatory reporting, architecting data quality programs and developing a target operating model for risk, finance, data and technology integration. He has developed trusted advisor relationship with key clients to help formulate, shape and refine "strong" ERM programs and has set up data programs to meet the needs of BCBS239, FRY-14 and CCAR. Capco's data practice focuses primarily on data supply chain (governance, infrastructure, architecture, reconciliation and reporting), (2) analytics and visualization, and big data solution definition and implementation.

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Michael Tao is a managing principal at Capco. He has over 20 years of experience in the financial services industry and has assisted many companies with developing business strategies and with repositioning their operations, infrastructure and organization to maximize performance. His functional expertise includes strategy development, product development, marketing strategy and operations, process design, organizational design and implementation of strategic initiatives.

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ABOUT CAPCO

Capco, an FIS™ company, is a global management consultancy with a focus in financial services including banking and payments, capital markets, and wealth and asset management. We combine innovative thinking with unrivalled industry knowledge to deliver business consulting, digital, technology and transformational services. Our collaborative and efficient approach helps clients reduce costs, manage risk and regulatory change while increasing revenues. Visit us at www.capco.com and follow us on Twitter @Capco.

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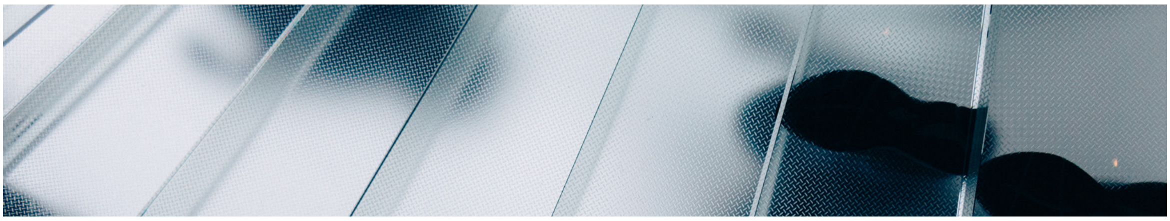

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