Financial Services Management

Transaction-Account FDIC Coverage

Cite
S. 3012, Deposit Security Act

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Website
https://www.manchin.senate.gov/imo/media/doc/deposit_security_act_bill_text.pdf?cb

Impact Assessment

- Bank runs could be less likely, but still possible, especially at IDIs with concentrated exposures to a few large depositors.
- Opt-out provisions are designed to protect community banks from higher premiums but could do so also for the largest IDIs.
- FDIC premiums could significantly go up based on how many IDIs opt out, how the FDIC redesigns its premium-assessment system.

Overview

Bipartisan senators have introduced legislation to provide FDIC coverage for certain noninterest-bearing transaction accounts, a move designed to prevent the stress and potential systemic risk evident when Silicon Valley and Signature Banks failed in March. However, expanding FDIC coverage could increase FDIC premiums, heightening pressure on IDIs and their holding companies in concert with the pending special assessment unless companies that opt out of added coverage do not bear additional costs for IDIs that choose to offer these insured accounts.[1] If many companies opt out to avoid higher premiums, then run risk will not be materially reduced.

Impact

This bill would authorize the FDIC's suggested reform in the wake of the March failures,[2] a proposal aimed at reducing the risk of uninsured-deposit runs and risk to businesses and local governments likely to hold these accounts in the event of IDI failure. However, FDIC coverage for these accounts is unlikely to stem damaging runs at at least some banks with concentrations of very large noninterest-bearing accounts – the actual case at SVB[3] – because the bill caps coverage at $10 million and many deposit accounts that might run are considerably larger.

The goal here is also to force large depositors to exercise caution and assess the condition of any IDI in which large balances are held, but the extent to which depositors

1 See **DEPOSITINSURANCE120**, *Financial Services Management*, May 15, 2023.
2 See **DEPOSITINSURANCE118***, Financial Services Management*, March 15, 2023.
3 See *Client Report* **REFORM221**, May 1, 2023.

with over $10 million balances at a single bank take heed is uncertain in light of the SVB bail-out and those that preceded it is uncertain.

As noted, one effect of heightened FDIC coverage is the additional FDIC premiums. As discussed below, the bill attempts to address this by creating an op-out/opt-in process for IDIs seeking added coverage for eligible noninterest-bearing transaction accounts. Such decisions might well depend on the extent to which accepting coverage comes with added FDIC-coverage premiums, but it is possible that opt-out entities could still bear premium-assessment costs not only in the event of another special assessment, but also if the FDIC's planned rewrite of its premium-assessment system does not provide some form of offset for opt-out banks.[4]

The bill's drafting is also intended to prevent IDIs from using added coverage as a substitute for brokered deposits should the bank's condition worsen. However, the bill as drafted is so restrictive as to opt-out/opt-in decisions that many banks may have difficulty using this option in the event of charges such as bank merger.

What's Next

S. 3012 was introduced on October 4 by Sen. Manchin (D-WV), along with Sens. Braun (R-SD) and Hickenlooper (D-CO). An earlier Senate bill, S. 1572, provides for a two-year transaction guarantee for non-interest-bearing accounts up to $100 million, increases the limit on reciprocal deposits, and expands the FDIC cost criteria in failed IDI purchase-and-assumption transactions. A House bill, H.R. 3243, would guarantee deposits in noninterest-bearing transaction accounts for a single period, conditional on two-thirds of the FDIC and Fed Boards along with the Treasury Secretary's support in consultation with the President. The votes would determine the financial stability risks of the deposits being guaranteed.

Analysis

The bill would apply provisions similar to those noted below for insured banks and savings associations also to credit unions.

A. Coverage

The measure provides FDIC coverage for noninterest-bearing accounts up to $10 million at the time of a bank's failure. Covered accounts must not only be noninterest-bearing, but also have third-party transactional capabilities without any required prior notice of withdrawal.

The $10 million ceiling for insurance would be inflation-adjusted.

B. Opt In/Out

IDIs may decide not to receive this increased coverage if they do so in the thirty days following program establishment; should an IDI rethink this opt-out, it could opt back in no more often than every five years. As noted, the language here appears to limit opt outs but the opt in section is flexible enough to imply opt in and/or out as long as this is within five years. The limitation on opt outs would appear to preclude de novo IDIs from opting out and complicate the prospects for an IDI chartered following bank M&A.

4 See **DEPOSITINSURANCE116**, *Financial Services Management*, October 25, 2022.