A SOUP SPOON FOR TLGP - INTERIM RULE

by Steve Brown

Yesterday we discussed the details of the MMIFF and CPFF programs, each designed to boost the banking system and improve credit conditions. Today we provide a soup spoon, so our community bank readers can taste the FDIC Temporary Liquidity Guarantee Program ("TLGP"). Let's jump right into the "stock-making" of the matter.

TLGP is focused on increasing liquidity in the banking system, it is voluntary, funded through special fees and has a definitive expiration date. TLGP is effective now, all banks have already been automatically enrolled and all have until Nov. 12 to specifically opt-out (or you become a participating entity). Banks that want to opt-out must tell the FDIC (we advise you not do this until you have time to read the final rule). Banks can opt-out of one or both programs and those that do so will be listed on a publicly available website (the FDIC's, but not yet ready). TLGP breaks down into two primary pieces - Debt Guarantee and Transaction Account Guarantee.

The Transaction Account Guarantee ("TAG") provides unlimited coverage for funds held in noninterest bearing transaction accounts and is in addition to and separate from existing deposit limits. Fees for TAG are assessed quarterly at an annualized 10 basis points on balances held in noninterest bearing transaction accounts in excess of the existing deposit limit of $250,000. This is in place now and coverage expires on Jan. 1, 2010 (unless you opt out). Noninterest bearing transaction accounts under TAG are defined as accounts where interest is neither accrued nor paid and the bank does not require advance notice of withdrawal. Note that negotiable order of withdrawal (NOW) accounts and money market deposit accounts (MMDA's) are not covered under this definition, however traditional demand deposit checking or savings accounts are covered. Waiving fees or paying earnings credits does not prevent the account from qualifying. Under TAG, participating banks must prominently disclose in writing at the main office and in branches whether the bank is participating in the program or has opted-out. Finally, there are some unique considerations for sweep accounts. To begin, funds swept from a noninterest bearing (covered) account to an interest bearing account would not be covered and clients must be advised in writing that these actions void the guarantee. In addition, the FDIC will treat funds in sweep accounts the same way it does when an institution fails. In short, that means the FDIC will treat funds as being in the account where they land after the sweep process has completed at day's end. The guarantee remains intact, as long as funds are swept from one noninterest bearing account to another noninterest bearing account.

Our thoughts on the Transaction Account Guarantee under the TLGP: we expect most community banks to stay in this portion, since 10bp is relatively cheap insurance when trying to keep small business customers and their payroll processing accounts; opting-out opens the bank up to unexpected consequences and could lead to a loss of deposits based on fear of nonparticipation; and banks that stay in the program can market the fact that they are in and other banks are not (and they will likely do so) to capture customers worried about safety. Based on these reasons and others, for the Transaction Account Guarantee Program, we suggest community bankers remain in the program.

Keep in mind as well, that all of the above is subject to change, since this all comes from the current FDIC "Interim Rule" and bankers have not yet chimed in with full force. It is expected that the Interim Rule will be published in the public register today or tomorrow, so the comment period will be very tight (given the Nov. 12 opt-out date). To submit a comment, bankers can send an email to Comments@FDIC.gov and type "RIN # 3064-AD37" in the subject line of the message.

Tomorrow we will continue our discussion, as we serve up another bowl of the Debt Guarantee Program under TLGP and try to keep everyone informed of some of its nuances.

All comments are welcome and we are trying to address questions, so feel free to email us back if you wish and we'll try to work it into the publication.

BANK NEWS

E-Loan

After posting an $87mm net loss in 3Q, the once hyper-popular online site will exit the mortgage business. No plans were revealed for the site other than it will continue to service outstanding mortgages and match deposits (CDs). E-Loan's parent, Banco Popular, is in the midst of downsizing.

CP Results

In a bit of irony, after the first period of operation, the Treasury's CP purchase program served to increase 30-day CP rates by 25bp to an average of 2.88%. Since liquidity has been coming back in the market, the Fed's presence served to increase net demand, increasing borrowing costs.

Me Too

US life insurance companies are reportedly working with the Treasury to capture some of the TARP program. Some large life insurance companies have lost more than 50% of their value this month amid investor concerns.

Warning

The Bank of England said the global financial system faces the "most severe instability in living memory," that "the financial system remains under strain" and warned "fallout from hedge funds & insurers pose heightened risk to the financial system."