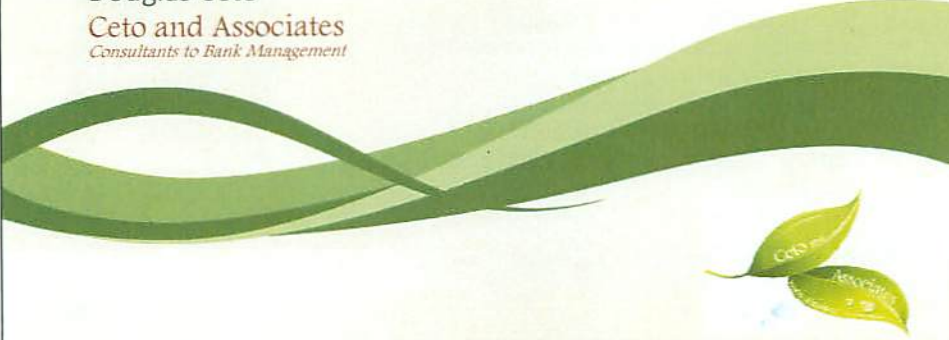


Looking for a way to go "Green"?
Deposit Reclassification Strategy

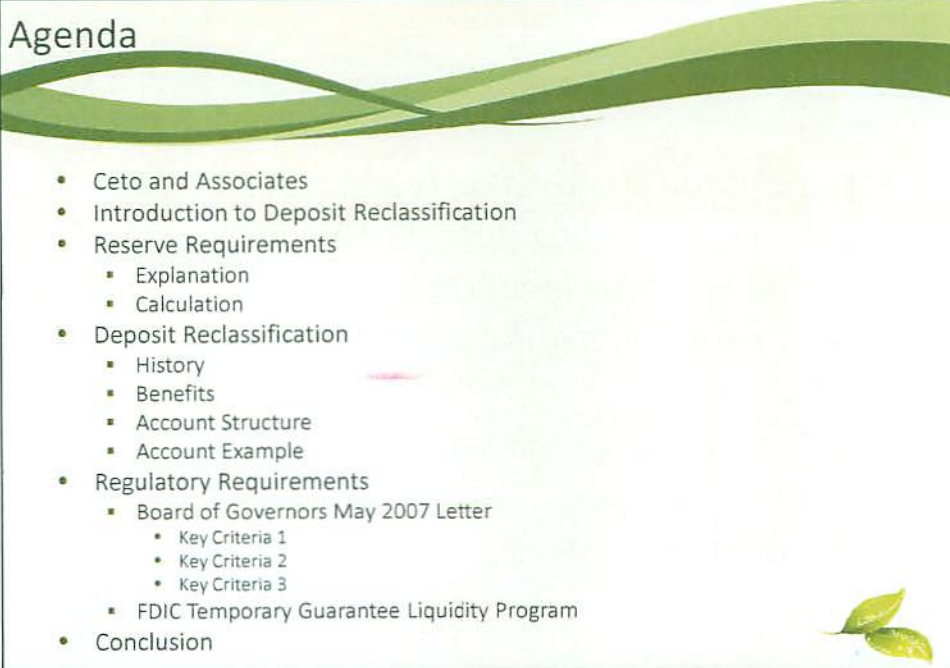
Presented by:
Douglas Ceto
Ceto and Associates
Consultants to Bank Management



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Agenda

- Ceto and Associates
- Introduction to Deposit Reclassification
- Reserve Requirements
 - Explanation
 - Calculation
- Deposit Reclassification
 - History
 - Benefits
 - Account Structure
 - Account Example
- Regulatory Requirements
 - Board of Governors May 2007 Letter
 - Key Criteria 1
 - Key Criteria 2
 - Key Criteria 3
 - FDIC Temporary Guarantee Liquidity Program
- Conclusion



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Ceto and Associates

- Founded in 1994
- A consulting firm based in Atlanta, Georgia
- Develops solutions to provide financial institutions the ability to increase their profitability through the implementation of earning enhancement programs and the optimization of overall operational efficiencies
- Trusted by over 1,500 clients in all 50 states



Douglas Ceto
President



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Introduction

- Deposit Reclassification is a process where a portion of your institution's transaction accounts are reclassified as a savings deposit, which are no longer subject to reserve requirements.
 - Reduce Reserve Requirements
 - Increase liquidity
 - Increase profitability



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Reserve Requirements - *Explanation*

- Regulation D established reserve requirements
- Reserve requirements are the amount of funds that a depository institution must hold in reserve against deposit liabilities (net transaction accounts)
- The dollar amount of a reserve requirement is calculated through applying Federal Reserve Board reserve ratios to an institution's net transaction accounts
- Reserve Requirements can be met with cash, a non-liquid reserve account with your local Federal Reserve Bank (FRB), or a "pass through" account with other financial institutions
- Reserve accounts are not liquid and earn less than the Federal Funds Rate
 - **Required Reserves :**
The *average* target Federal Funds rate over the reserve maintenance period = 1.00%
 - **Excess Reserves :**
The *lowest* target Federal Funds rate for the reserve maintenance period = 1.00%

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Reserve Requirements - *Calculation*

Reserve Requirements

Type of liability	Requirement	
	Percentage of liabilities	Effective date
Net transaction accounts		
\$0 to \$10.3 million	0	1-09-09
More than \$10.3 million to \$44.4 million	3	1-09-09
More than \$44.4 million	10	1-09-09
Nonpersonal time deposits	0	12-27-90
Eurocurrency liabilities	0	12-27-90

Source: The Federal Reserve Board, Reserve Requirements, <http://www.federalreserve.gov/monetarypolicy/reservereq.htm>

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Reserve Requirement - Calculation

FR2900 Form Total Net Transactions = \$55,775,000*

Report of Transaction Accounts, Other Deposits and Vault Cash

Reserve Ratios Applied

\$0 - \$10,300,000 at 0%	\$0
\$10,300,000 - \$44,400,000 at 3%	\$1,023,000
Over \$44,400,000 at 10%	\$1,137,500

Reserve Requirement = \$2,160,500
Less Vault Cash = \$900,000

Required Reserve Balance at FRB = \$1,260,500

* Gross transaction accounts less Due-From Bank Balance and Cash Items in the Process of Collection (from Form FR2900)

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Deposit Reclassification - History

FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20540

NOVEMBER 1, 1994

In 1994, the Federal Reserve Board permitted financial institutions to implement retail sweep programs.

This is an emergency of great interest of July 11, 1994. The Board has determined to permit all FDIC member banks to...
 The Board has determined to permit all FDIC member banks to...
 The Board has determined to permit all FDIC member banks to...

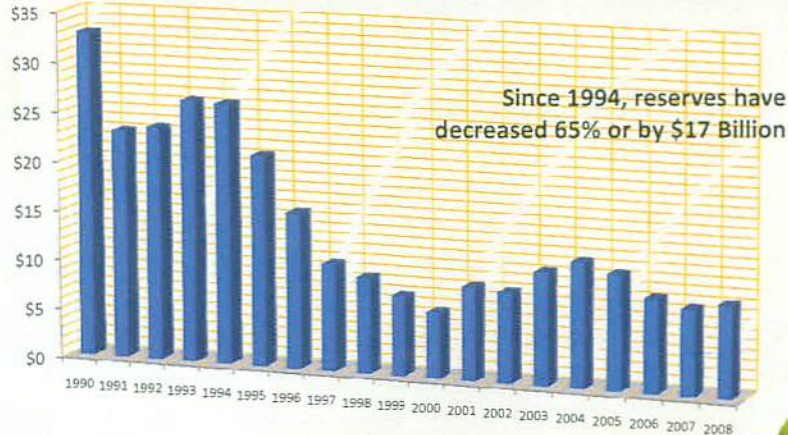
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FEDERAL RESERVE SYSTEM
 BOARD OF GOVERNORS
 FEDERAL RESERVE SYSTEM
 WASHINGTON, D.C. 20540

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Deposit Reclassification - History

Reserve Balances with the Federal Reserve Bank

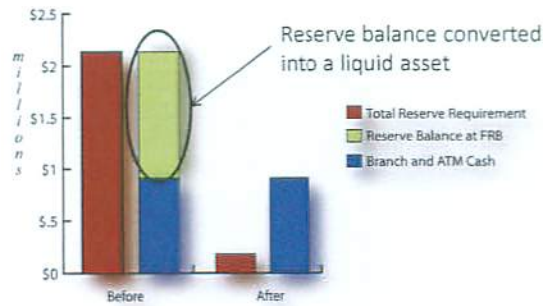


Source: The Federal Reserve Board of Governors, Statistics: Releases and Historical Data, Aggregate Reserves of Depository Institutions and the Monetary Base - H.3, <http://www.federalreserve.gov/releases/h3/> (Data Range: 1/1990 to 8/2008)

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Deposit Reclassification - Benefits

The Impact of Deposit Reclassification



Possible financial benefits from calculation example:
 $\$1,260,500$ (Required Reserve Balance) \times 4.00% (Prime Rate*) = $\$50,420$

*As of 11/7/2008

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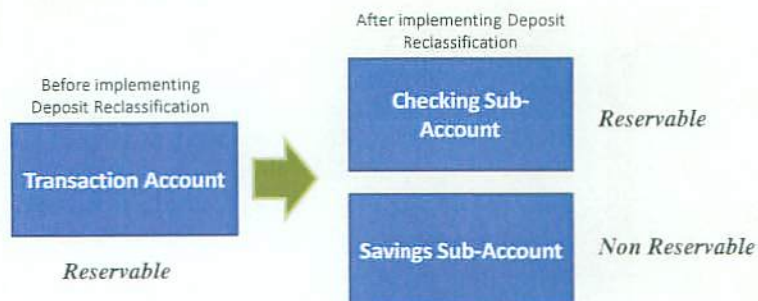
Deposit Reclassification - *Benefits*

- Deposit Reclassification
 - Reduces reserve requirements enabling the institution to reclaim their reserve balance
 - Assets reclaimed are permanent and grow with transaction deposit growth
 - New liquid assets to loan to your local community or invested in other earning assets
 - Remain competitive against larger, regional, super regional and national banking
 - New regulation permit "Pass Through Correspondents" to keep the interest earned, if they wish.
 - Larger incentive to reduce branch and ATM cash levels

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Deposit Reclassification – *Account Structure*

- Change in the structure of a financial institution's transaction account



- Change is completely invisible to the customer

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Deposit Reclassification – Account Structure

- The Checking Sub-Account
 - Holds only an estimated portion used by the customer
 - Covers daily activity by the customer
 - Has unlimited activity
 - Subject to reserve at FRB

- The Savings Sub-Account
 - Holds an estimated portion not normally used by customer
 - Transfers funds to the Checking Sub-Account when the Checking Sub-Account has been depleted
 - Limited to six transfers count
 - Not subject to FRB reserves

- Sub-Account transfers are invisible to the customer



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Deposit Reclassification - Account Example

Day 1

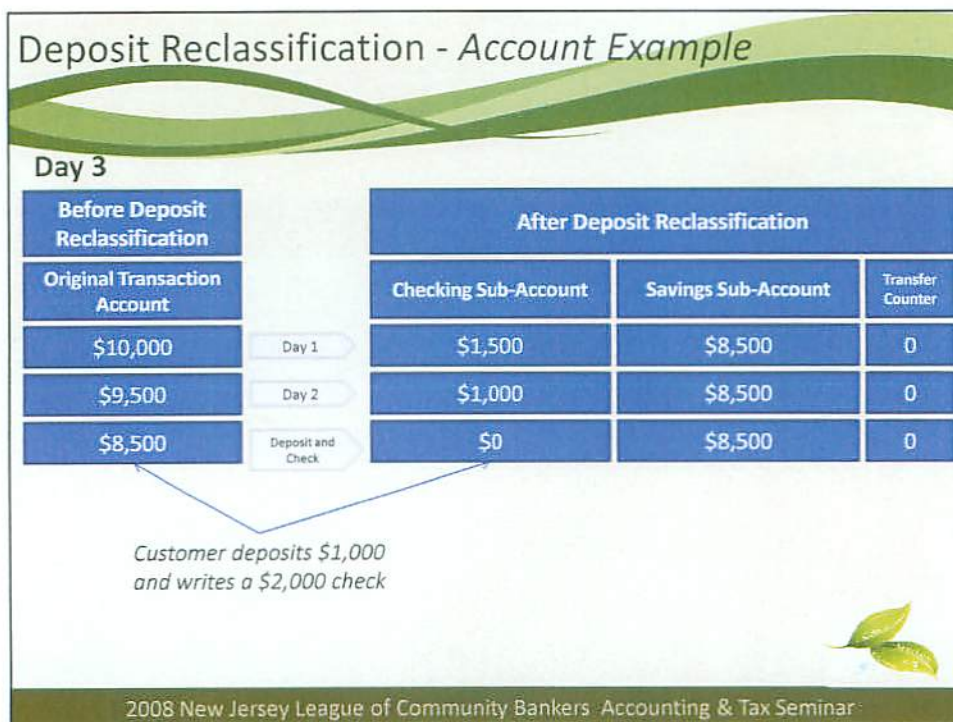
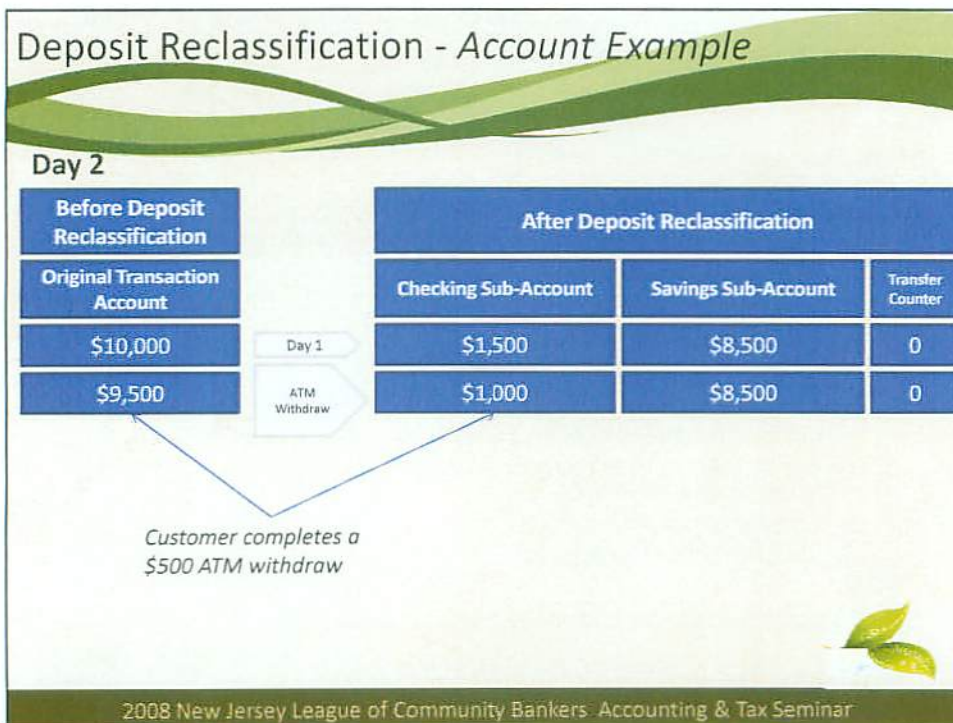
Before Deposit Reclassification	After Deposit Reclassification		
Original Transaction Account	Checking Sub-Account	Savings Sub-Account	Transfer Counter
\$10,000	\$1,500	\$8,500	0

Threshold of 15%/85%

Creation of sub-accounts and Transfer Counter



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Deposit Reclassification - Account Example

Day 4

Before Deposit Reclassification		After Deposit Reclassification		
Original Transaction Account		Checking Sub-Account	Savings Sub-Account	Transfer Counter
\$10,000	Day 1	\$1,500	\$8,500	0
\$9,500	Day 2	\$1,000	\$8,500	0
\$8,500	Day 3	\$0	\$8,500	0
\$6,000	Checks and ATM Withdraw	\$900	\$5,100	1

Customer writes 6 checks for a total of \$2,000 and completes an ATM withdraw of \$500

Transfer incremented



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Deposit Reclassification - Account Example


Day 28

Before Deposit Reclassification		After Deposit Reclassification		
Original Transaction Account		Checking Sub-Account	Savings Sub-Account	Transfer Counter
\$10,000	Day 1	\$1,500	\$8,500	0
\$9,500	Day 2	\$1,000	\$8,500	0
\$8,500	Day 3	\$0	\$8,500	0
\$6,000	Day 4	\$900	\$5,100	1
\$3,000	Day 28	\$3,000	\$0	6




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Regulatory Requirements – May 2007 Letter



**BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM**
WASHINGTON, D. C. 20561


NATIONAL CREDIT CORRESPONDENCE
TO THE BOARD



May 2007


Board staff has received a number of inquiries about the requirements for a retail sweep program to comply with the Board's Regulation D ("Reserve Requirements of Depository Institutions"). In a "retail sweep program," a depository institution transfers funds between a customer's transaction accounts and that customer's savings deposit accounts up to an amount per month by means of prearranged or automatic transfers, typically in order to reduce transaction account reserve requirements while providing the customer with access to the funds. The following is a summary of previously issued staff opinions and informal staff guidance with respect to the requirements of an acceptable retail sweep program.

Staff opinions from the Board's Legal Division have established three key criteria for retail sweep programs to comply with Regulation D:




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Regulatory Requirements – Key Criteria 1



**BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM**
WASHINGTON, D. C. 20561

NATIONAL CREDIT CORRESPONDENCE
TO THE BOARD



May 2007

Board

Regulation D

Key Criterion 1


“(1) A depository institution must establish by agreement with its transaction account customers two legally separate accounts: a transaction account (a NOW account or demand deposit account) and a nontransaction account (usually a savings deposit account, also sometimes called a “money market deposit account” or “MMDA”.)”

Key Criterion 1

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Regulatory Requirements – *Sub-Account Creation and Disclosure*

- The financial institution is changing the customer transaction account from a single transaction account to a checking and savings sub-account
- Disclosure
 - must explain the change in clear and concise language
 - must be received by all current transaction account holders
 - must be included in all new account agreements



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Regulatory Requirements – *Key Criteria 2*



FEDERAL RESERVE SYSTEM
REGULATIONS, 12 CFR

12 CFR

Part 101

Section 101.11

101.11.1

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Regulatory Requirements – Funds Movement and Official Books and Records


- Funds must be moved at account level
- The movement of funds must exist in the financial institution’s official books and records
 - Form FR2900 and Quarterly Reporting (Call Report, NCUA 5300, TFR)
- Reclassified totals must be reported before the close of business

Before Deposit Reclassification		After Deposit Reclassification		
Original Transaction Account		Checking Sub-Account	Savings Sub-Account	Transfer Counter
\$10,000	Day 1	\$1,500	\$8,500	0



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Regulatory Requirements – Key Criteria 3



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WASHINGTON, D.C. 20540


Nov 2007

“(3) The maximum number of preauthorized or automatic fund transfers (“sweeps”) from a savings deposit account in a retail sweep program is limited to not more than six (6) per month.”

1. A depository institution shall establish a separate sub-account to receive the funds transferred from a sweep program to the depository institution’s “retail sweep program account” in FR 2021.11.

2. The depository institution shall establish a separate sub-account to receive the funds transferred from a sweep program to the depository institution’s “retail sweep program account” in FR 2021.11.

3. The depository institution shall establish a separate sub-account to receive the funds transferred from a sweep program to the depository institution’s “retail sweep program account” in FR 2021.11.



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Regulatory Requirements - *Temporary Liquidity Guarantee Program (TLGP)*

- FDIC announced program that fully insures non-interest bearing checking accounts
- How does this affect Deposit Reclassification?
 - Swept funds are guaranteed by FDIC
 - "...treatment funds swept into noninterest-bearing savings account will be guaranteed by the Transaction Account Guarantee Program."



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Implementation

- Deposit Reclassification
 - Typically implemented within 45 days
 - Implementation requires a total of 5 hours of staff time
 - Reserve reduction is typically seen within 3-6 weeks
 - Return on investment is normally about 6 months or less



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Conclusion

Would your bank make a PERMANENT loan to a borrower at an interest rate of 1.00%?

- The obvious answer is "No"
- Deposit Reclassification is still highly beneficial now and in the future... even when interest is paid on reserve balances.



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