

Insights

BROKERED DOESN'T HAVE TO MEAN BROKEN – NAVIGATING COMPLEXITIES OF BROKERED DEPOSITS

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By: Keaton J. Miller

Brokered deposits occupy a unique place in bank funding: widely used, strategically valuable, and nevertheless scrutinized. Banks often rely on them to supplement local deposit bases, particularly when core deposits slow or fail to keep pace with asset growth. Brokered deposits also carry the benefit of being less susceptible to traditional runs on banks. Customers benefit as well, whether through access to higher rates or extended insurance coverage. Yet regulators have long viewed brokered deposits with skepticism, questioning their stability and reliability as a funding source.

The data underscores their importance. Over half of banks headquartered in Indiana report using brokered deposits, and among the state's 17 largest banks, every single one reports some reliance on them.¹

Regulatory concerns, however, have only intensified. In the wake of the 2023 banking liquidity crisis, examiners are paying closer attention to funding sources and the composition of bank balance sheets. Recent attempts to tighten rules around brokered deposits were ultimately withdrawn, but the regulatory gaze has not softened.²

Adding to the challenge, determining what qualifies as a "brokered deposit" is anything but straightforward. Today's rules are layered with definitions within definitions and are riddled with exceptions. What may seem to be a straightforward deposit of funds can, under the regulation, trigger unexpected categorization and heightened compliance risk.

What Even is a Brokered Deposit?

Banks often entirely overlook the intricacies involved in determining whether a deposit is considered brokered. A straightforward approach is typically taken, only classifying a deposit as brokered if it is sourced through a party that self-identifies as being a deposit broker. This fails to capture the complexity and broad scope of the regulatory definition, potentially excluding numerous deposits that, legally, should be categorized as brokered.

Banks should begin a brokered deposit analysis any time a deposit is obtained, directly or indirectly, from anyone other than the depositor themselves.³

It is then necessary to analyze that third party to determine whether they meet the definition of a deposit broker. A deposit broker is a person who falls into one of four categories:⁴

1. Any person engaged in the business of placing deposits of third parties with insured depository institutions.⁵
2. Any person engaged in the business of facilitating the placement of deposits of third parties with insured depository institutions.⁶
3. Any person engaged in the business of placing deposits with insured depository institutions for the purpose of selling interests in those deposits to third parties.
4. An agent or trustee who sets up a deposit account to facilitate a business arrangement with a bank to use the proceeds of the account to fund a prearranged loan.

If the third party placing or facilitating the deposit falls into one of the four categories above, banks must then determine whether one of nine exceptions apply.⁷ The most common of these nine exceptions is the "primary purpose exception," which exists for agents or nominees whose *primary purpose* is not the placement of funds with depository institutions.⁸ There are fourteen business relationships listed by regulation as expressly meeting the primary purpose exception.⁹ If a bank wants a business relationship other than the fourteen listed to be considered under the primary purpose exception, approval must be obtained from the FDIC.¹⁰

To complicate the matter, brokered deposit definitions are also expanded for banks that are not well-capitalized when rates of interest on accounts are significantly higher than prevailing rates.¹¹ Also, certain reciprocal deposits are not considered brokered deposits up to certain caps.¹²

Regulatory Review

Regulators will primarily review brokered deposits in the context of liquidity and funds management examinations. The FDIC's examination manual notes:

*"[S]ome institutions have used brokered deposits to fund unsound or rapid expansion of loan and investment portfolios, which has contributed to weakened financial and liquidity positions over successive economic cycles. The overuse and failure to properly manage brokered deposits by institutions have contributed to failures and losses to the Deposit Insurance Fund."*¹³

As a threshold matter, brokered deposits need to be properly categorized, as banks are responsible for accurately reporting the deposits on their Call Reports. During examinations, regulators will determine whether banks are relying upon primary purpose exceptions to exclude certain deposits involving third parties and assess the bank's Call Report filing documentation supporting the bank's reliance on the primary purpose exception.¹⁴

Once properly categorized and documented, regulators will consider brokered deposits as part of the bank's overall liquidity and funds management risk. Undue reliance on brokered deposits can result in unsafe and unsound conditions, leading to regulatory actions. Additionally, banks that are adequately capitalized must seek approval prior to accepting brokered deposits.¹⁵ Banks that are undercapitalized are prohibited from accepting brokered deposits.¹⁶ Due to these restrictions, regulators may review banks' proper categorization and

documentation of brokered deposits more closely if the institution is less than well-capitalized.

It is also important to note that a bank's FDIC insurance assessment is based in part on its brokered deposit ratio.¹⁷

Action Plans for Banks

Banks should begin managing the risks of brokered deposits by having a policy on brokered deposits.¹⁸ The policy should set forth whether the bank intends to use brokered deposits, what limits the bank has on brokered deposits, and who is responsible within the bank for managing the procedures and risks.

Even if a bank does not intend to accept brokered deposits, procedures should be adopted in order to ensure they are properly identified. Best practice involves a centralized decision maker for conducting a "brokered deposit" analysis. Front-line bankers should be trained to refer potential brokered deposits to this centralized point of contact.

Banks should also ensure they are analyzing and weighing the impact of a potential loss of brokered deposits. In a stressed scenario, where the bank becomes adequately or undercapitalized, the bank may be prohibited from retaining brokered deposits. This of course has important implications with respect to liquidity planning and stress testing.

For questions regarding brokered deposits, including assistance categorizing certain deposits, development of policies, applications by adequately capitalized banks seeking permission to utilize brokered deposits, or companies seeking a primary purpose exception, please contact Keaton Miller, or any member of the Krieg DeVault's Financial Institutions team.

¹ 3/31/2025 Call Report Data.

² The FDIC proposed new rules in August 2024 to eliminate certain exceptions to brokered deposit definitions but ultimately withdrew the proposed rule in March 2025.

³ 2 C.F.R. 337.6(a)(2) defines a brokered deposit as a deposit that is obtained, directly or indirectly, from or through the mediation or assistance of a deposit broker.

⁴ 2 C.F.R. 337.6(a)(5)(i)

⁵ 12 C.F.R. 337.6(a)(5)(ii) states that a person is engaged in the business of placing deposits of third parties if that person receives third party funds and deposits those funds at more than one insured depository institution. 12 C.F.R. 337.6(a)(5)(iv) states that being "engaged in the business" also necessitates the person having a business relationship with third parties, and as part of that relationship, placing deposits with insured depository institutions on behalf of the third parties.

⁶ 2 C.F.R. 337.6(a)(5)(iii) states that a person is engaged in the business of facilitating the placement of deposits of third parties with insured depository institutions, by, while engaged in business, with respect to deposits placed at more than one insured depository institution, engaging in one or more of the following activities: (A) The person has legal authority, contractual or otherwise, to close the account or move the third party's funds to another insured depository institution; (B) The person is involved in negotiating or setting rates, fees, terms, or conditions for the deposit account; or (C) The person engages in matchmaking activities. Matchmaking activities are defined

under 12 C.F.R. 337.6(iii)(C). 12 C.F.R. 337.6(a)(5)(iv) states that being "engaged in the business" also necessitates the person having a business relationship with third parties, and as part of that relationship, facilitating the placement of deposits with insured depository institutions on behalf of the third parties.

⁷ 2 C.F.R. 337.6(a)(5)(v)(A)-(I)

⁸ 12 C.F.R. 337.6(a)(5)(v)(I)(i)-(xiv)

⁹ 12 C.F.R. 337.6 (a)(5)(v)(I)(1)

¹⁰ 12 C.F.R. 337.6(a)(5)(v)(I)(2)

¹¹ 12 C.F.R. 337.6(a)(5)(vi)

¹² 12 C.F.R. 337.6(e)

¹³ <https://www.fdic.gov/resources/supervision-and-examinations/examination-policies-manual/risk-management-manual-complete.pdf>

¹⁴ <https://www.fdic.gov/resources/supervision-and-examinations/examination-policies-manual/risk-management-manual-complete.pdf>

¹⁵ 12 C.F.R. 303.243(a)(1)

¹⁶ *Id.*

¹⁷ 12 C.F.R. 327.16(a) defines Brokered Deposit Ratio as the ratio of the difference between brokered deposits and 10 percent of total assets to total assets.

¹⁸ Banks should also consider the implications to their BSA/AML policies and procedures when accepting brokered deposits.

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