Federal Reserve Bank of Dallas

Borrower-in-Custody (BIC) Program Requirements

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Introduction

Borrower-In-Custody (BIC) arrangements allows eligible depository institutions (DIs) to pledge a variety of loan types to the Federal Reserve Bank of Dallas (Dallas Fed). The participating DI maintains custody and servicing of the loans, thus avoiding the need to send loan documentation directly to the Dallas Fed. Additional information on collateral eligibility, valuation, and pledging can be found in the Federal Reserve Bank Discount Window (FRB Discount Window) website under Collateral.

Eligibility

All DIs that are eligible to establish a Discount Window relationship are eligible to request a BIC arrangement. DIs requesting to establish a new BIC arrangement will be required to submit a formal BIC Application package. Eligible DIs are required to have completed Operation Circular 10 (OC-10) agreement documents on file with the Dallas Fed prior to applying for a BIC arrangement. For information on loan collateral eligibility, DIs should refer to the eligible BIC loan type categories chart on the pledging collateral discount window webpage and the acceptance criteria for loans on the collateral eligibility discount window webpage.

BIC Application Process

New BIC Applicants

Eligible DIs looking to establish a new BIC arrangement with the Dallas Fed should contact the Credit Risk Management department by calling the toll-free line or emailing the department's mailbox. A Credit Risk Analyst will meet with the DI to discuss the BIC program and provide the required application documents.

The process to pledge loans requires a significant amount of effort to complete and DIs should remain in contact with their assigned analyst and provide the requested information in order to complete the application request in a timely manner. The Dallas Fed aims to complete the application process within 30 days of receiving all completed and acceptable application documents. If approved, the Dallas Fed will provide the DI an approval letter and an updated statement of collateral holdings. Additionally, an initial BIC inspection of the DI will be performed within 6-12 months of approval for most institutions. The Dallas Fed generally requires a BIC inspection prior to approval for DIs that are exhibiting deteriorating financial conditions.

BIC Program Required Documents

- BIC Application
  - The BIC application covers various key elements of compliance with the BIC program including the amount and attributes of the loans to be pledged.
- BIC Certification Questionnaire
  - The BIC Certification Questionnaire attests to the controls and procedures in place to safeguard the pledged loans and related documentation. To be considered for the BIC program, a DI must complete and submit an initial certification, and thereafter, an updated certification on a periodic basis.
  - It is a requirement that an auditor sign the BIC Certification Questionnaire. In the case where the DI does not have an internal audit department, a director or a senior level officer that is not directly responsible for Discount Window borrowing or collateral pledging may sign the form.

- Electronic Loan Collateral Questionnaire (if applicable)
    - If the institution originates loans that are digitally signed and stored electronically, and/or signed on paper and then imaged and stored electronically with the paper original destroyed, an Electronic Loan Collateral Questionnaire must be completed. It is expected that the institution has reasonable processes and procedures in place, governing the use of electronic collateral. **Prior approval** is required to pledge electronic loan collateral. Refer to the Electronic Loan Collateral Guidelines (below) for further details.
- BIC Pledge File and Cover Letter
    - The BIC Pledge file (collateral schedule) is the monthly file detailing the loans, with key data elements, that the DI is pledging to the Dallas Fed as part of the BIC program. For file formatting and specifications please see here. The Cover Letter is a signed attestation that the data in the BIC pledge file is complete and accurate and must be signed by an individual who is authorized to pledge collateral per the OC-10 Official Authorization List.
- Third Party Custodian Agreement (if applicable)
    - If the primary legal documents, including Certificate of Titles, are held by a third-party custodian, including subsidiaries or affiliates, the Form of Agreement for Third-Party Custodian to Hold Collateral must be completed and can be found in the OC-10 Agreements page.
- DI's Internal Loan Policy
    - An analyst will review the DI's loan policy to ensure its practices are in compliance with BIC program requirements.
- Internal Risk Ratings Definitions (if applicable)
    - The Dallas Fed relies on the internal risk ratings assigned by the pledging DI to determine the acceptability of commercial loans (C&I, CRE, Ag, etc.). The DI's internal risk ratings will be mapped to the Federal Reserve's "minimal", "normal", and "excessive" credit quality standards used in valuing loan collateral. This process could result in some loans classified as "Pass" by the DI being deemed ineligible.
    - After the initial acceptance of the DI's internal risk ratings, DIs are required to immediately inform the Dallas Fed of any changes in its loan rating system, including credit quality definitions and rating scale structure.
- Documents Related to Perfection of Security Interest
    - UCC-1 Financing Statement
        - Upon receipt of the BIC Application, the Dallas Fed will file a UCC-1 Financing Statement in order to perfect a security interest in the pledged collateral. DIs that are members of and pledge collateral to a Federal Home Loan Bank (FHLB), bankers bank, or a corporate credit union should be aware that a blanket lien may already be filed against its assets. DIs should also know what loan types are pledged to the FHLB or corporate credit union and take the necessary steps to prevent any potential double pledging of collateral to the Dallas Fed. If the Dallas Fed is not in senior lien position, we will seek to execute an agreement with the senior lienholder to subordinate their interest in the pledged loans.
    - DIs will need to contact their respective FHLB, bankers bank, or corporate credit union to initiate the subordination process. The DI should inform them of their intent to pledge loan assets as collateral to the Dallas Fed and ask for an agreement to be drafted.

- Independent Audit Report
    - DIs are required to provide the most recent audit of the lending function with the application package.
    - On an ongoing basis, the Dallas Fed requires DIs to conduct and provide an audit report of their BIC collateral prepared by an internal or external auditor. The frequency of the audit report should not exceed a period of 24 months. The audit must include a review and assessment of the DI's compliance with the BIC requirements. The DI shall immediately notify the Dallas Fed of any irregularities discovered during any audits. A complete audit report, including any findings and management's response and corrective action plan, should be sent along with the periodic BIC Certification Questionnaire.

Adding New Loan Categories to an Existing BIC

To add additional loan categories, institutions will need to submit a form to request additional loan category pledges. These new loans will need to be vetted through a similar process to a new BIC application. The form can be obtained from Discount Window staff. If approved, the addition of new loan types will require an existing loan listing file to be edited and re-mapped in our collateral application. This process can take up to two weeks.

Other existing BIC documentation would need to be revisited to include the additional pledges:

- Intercreditor/Subordination Agreement (If applicable)
- BIC Certification
- Internal Risk Ratings
- New BIC Cover Letter
- New BIC Pledge Microsoft Excel® file-loan listing

Collateral Reporting and Monitoring

Collateral Reporting

A DI must provide a BIC Pledge Cover Letter and a collateral schedule in the automated loan data (ALD) format each month or on a more frequent basis as deemed necessary by the Dallas Fed. ALD is the Federal Reserve's process for recording loan pledges at the individual loan detail level in its Collateral Management System (CMS). Within the collateral schedule file, a separate tab within the Microsoft Excel® based workbook is required for each separate loan type (e.g., commercial loans, commercial real estate, home equity loans, etc.). All pledge submissions should be submitted within the first 10 business days of each month; zero collateral value may be assigned to DIs that do not submit its collateral reporting in a timely manner. An analyst will provide a sample Microsoft Excel® and/or text-based collateral schedule file as a recommended formatting for both in-scope and out-of-scope DIs in the application documents. If DI is unable to replicate the sample format, contact the Dallas Fed to determine an acceptable format.

The Dallas Fed requires that DIs use one of the following secure methods for transmitting information or documentation pertaining to pledged BIC loan collateral: Federal Reserve Secure Message Center, Intralinks, or by email with Mandatory Transport Layer Solution (TLS). All pledge submissions should be sent to the Dallas Fed's BIC mailbox at the following e-mail address: dal.discount.window@dal.frb.org.

Collateral Reporting Format

Each BIC participant will be classified as in-scope or out of scope for purposes of providing periodic collateral reporting. Once an institution meets the criteria of being in-scope, it remains in-scope. Any DI that has not yet met the criteria of being in-scope is considered an out-of-scope institution. The definition of in-scope is found under the File Specifications section of the pledging collateral discount window webpage. File formats should not be changed between submissions without prior approval from the Dallas Fed.

- In-Scope DIs
    - In-scope institutions will send a plain text file of vertical pipe (|) separated fields containing the required loan fields on loans pledged as collateral. Detailed information can be found at the following link: In-Scope File Format Specifications and Definitions.
- Out-of-Scope DIs
    - Out-of-scope institutions will send either a fixed formatted text file or Microsoft Excel® spreadsheet. For those DIs who want to submit a Microsoft Excel® spreadsheet, please contact the Dallas Fed for further instructions and a mapping template.

Collateral Monitoring

In addition to the monthly reporting process described above, a BIC Pledge Cover Letter and updated collateral schedule must be submitted to the Dallas Fed at any time the outstanding principal balance of the pledged collateral declines by 10 percent or more from the date of the most recent collateral schedule submitted. As such, DIs are required to have effective monitoring over the institutions' loan portfolios pledged to the Dallas Fed. At a minimum, weekly monitoring is required. If your DI pledges a pool of loans for which the outstanding balance frequently fluctuates, daily monitoring may be more appropriate. Failure to properly monitor for and notify the Dallas Fed of declines of 10 percent or more between reporting dates may result in the termination of BIC privileges.

The email accompanying an intra-month pledge should clearly indicate that there was a decline of 10 percent or more from the previous submission and provide a brief explanation of what caused the decline. If a decline of 10 percent or more coincides with the regular monthly pledge, please indicate this and the reason in the accompanying email.

The Dallas Fed will make every effort to promptly process collateral schedule updates. DIs can access real-time collateral information using the Account Management Information (AMI) system. DIs may also subscribe to email delivery of collateral statements (see Statement of Collateral Holdings section).

Loan Data Integrity Guidance

For a detailed listing of the data fields and how to report them, please refer to the in-scope and out-of-scope file formatting and specifications here. The following tips are aimed to help DIs avoid common loan data quality issues within the collateral schedule:

- Exclude loans that mature within 15 days of the principal as of date.
- Exclude loans that have a maturity date that is before the principal balance as of date.
- Commercial loans: loans are not accepted if more than 30 days past due.
- Consumer loans: loans are not accepted if more than 60 days past due.

Ongoing Collateral Maintenance Requirements

Storage of Loan Collateral

All loan documentation must be appropriately stored. Original hardcopy documents are to be stored in a fire-resistant environment with controlled access. Electronic loan documents are to be stored in an environment with appropriate access controls and backup (refer to Electronic Loan Collateral Guidelines below). Loan documents are generally maintained in an area where access is restricted to specific individuals and use of files is recorded. For auto and other loans considered chattel paper (generally collateralized through a Certificate of Title), the location of titles must be maintained at the location designated in the most recently approved BIC certification.

A DI must immediately contact the Dallas Fed if documentation relating to the pledged loans are damaged due to a flood, fire, or any other reason. The Dallas Fed will work with the DI to determine the extent of the damage and may make appropriate adjustments to the value of the collateral.

Legal Documents

The payment document is the loan document where the underlying debtor promises to pay the DI, usually the promissory note or loan/lease agreement. Pledging institutions must possess the original or authoritative copy of the payment document, and it may be in original hardcopy/wet signature format, or if the institution is approved, in electronic loan collateral format. If the legal documents were originated by another party (e.g., syndications, participations, and/or acquired loans), other documents may be acceptable, but these situations may be complex and require additional due diligence and approval by the Dallas Fed.

Electronic Loan Collateral

If the institution plans to image and destroy original hardcopy/wet signature payment documents and store these electronically in the future, they should refer to the Electronic Loan Collateral Guidelines below for further information and guidance. Approval is required prior to pledging alternate forms of payment documents.

Credit and Collateral Documents

For loans secured by Certificates of Titles, the original hardcopy or electronic form held by an approved custodian must clearly indicate the security interest of the pledging institution. The availability of credit and collateral documents, whether original hardcopies, images of, or copies of certain credit and collateral documents, are required. Credit and collateral documentation are not required to be in the same location as the payment documents as designated in the most recently approved BIC certification; however, if requested by the Dallas Fed, they must be readily available.

Loan Collateral Identification Requirements

Pledged loans must be clearly identified as collateral for the Dallas Fed. This is accomplished by the following:

- Segregating hardcopy loans pledged to the Dallas Fed from those not pledged and posting a highly visible sign in the area where the pledged loans are physically located, with wording such as "These loans are pledged to the Federal Reserve Bank of Dallas."
- If hardcopy pledged loans are not physically segregated from non-pledged loans, an electronic notation, consisting of a numeric and/or alpha code, to flag pledged loans should be placed on the institution's loan trial system. Additionally, a highly visible sign stating that "Some of these loans are pledged to the Federal Reserve Bank of Dallas, as notated in the loan trial system" should be posted where the pledged loans are physically located.

- Placing an electronic indicator for e-loans that are stored in an eVault. Institutions must clearly designate or label all electronic loan collateral as being pledged to Federal Reserve Bank of Dallas. For further information, refer to the Electronic Collateral Guidelines below.

Relocation of Collateral

Removal of collateral documentation in the normal course of business is acceptable (e.g., servicing, credit review, etc.) provided the documents are tracked and returned after use. The institution's internal procedures must clearly document this process.

For removal and relocation of collateral that is not considered in the normal course of business (e.g., establishing new BIC location), the Dallas Fed requires written notice at least 30 days prior to the movement of physical collateral. If electronic loan collateral is pledged, notification must be provided at least 45 days prior to movement. The written notice must be emailed to dal.discount.window@dal.frb.org and should include the following:

- Date of relocation and estimated time in transit.
- Method of relocation (e.g., third party or internal staff).
- Controls in place to ensure the safeguard of collateral during transit to the new collateral location.
- Description of the new collateral location and controls in place to ensure compliance of the BIC Program requirements.

Periodic BIC Certifications and Inspections

After the DI's initial BIC inspection, each BIC participant can expect periodic certifications and on-site/ virtual BIC inspections. Typically, the certification process will be completed after each full-scope examination of the DI. When required, a Dallas Fed analyst will contact the DI and provide a new certification questionnaire, and it is the responsibility of the DI to submit an updated and signed certification questionnaire (including auditor signature) in a timely manner.

The DI will also be notified if a BIC inspection is required via a written notice approximately 3-6 weeks prior to the scheduled review date. Frequency of BIC inspections are typically after every third examination cycle and in-scope DI validations will occur no less frequent than every three years; however, the Dallas Fed may perform more frequent inspections/in-scope data validations if warranted by a DI's financial condition or if issues are identified related to asset quality or loan administration.

On-site inspections entail Dallas Fed staff reviewing the premises and pledged loans, establishing that the collateral is clearly and properly identified as pledged to the Federal Reserve Bank of Dallas, and ensuring that the administration of the BIC program meets program requirements. Virtual inspections entail the same process as on-site inspections; however, Dallas Fed staff will perform the inspection remotely. For virtual inspections, the institution will submit the required documentation via Intralinks.

Generally, Dallas Fed staff expects:

- Loans to be properly housed, complete, and in good order.
- Loans be clearly identified on the premises, and in the loan trial system (if applicable) as pledged to the Federal Reserve Bank of Dallas.
- Current principal balance, maturity, risk rating, and other information should be accurately reported on the monthly pledge listing.
- Personnel responsible for reporting and servicing of the pledged loans should be aware of the institution's participation in the BIC program and the associated requirements.

A sample of loans selected from the pledge listings will be reviewed during on-site or virtual inspections. It is expected that key personnel be available throughout the inspection to address any questions or issues. A wrap-up meeting will be conducted to discuss the findings of the inspection. This meeting will cover the results of the inspection, including exceptions found, recommendations, and required course of action. Within 30 days of the conclusion of the inspection (which may include a short remediation period), a letter confirming the results of the review will be sent to the institution. Should the inspection uncover breaches of BIC program or OC-10 requirements, the Dallas Fed may institute additional risk controls, such as an additional collateral haircut, and for serious issues that have not been addressed in a timely manner, the institution's participation in this program may be terminated.

Termination of BIC Arrangement

The participating DI may terminate the BIC arrangement by giving written notice of termination. When notice is given by the participating institution, the notice is effective when received by the Credit Risk Management department. The Dallas Fed reserves the right to terminate the institution's participation in the BIC program without prior notice. The rights and liabilities of the parties under the BIC arrangement survive any termination of the BIC arrangement until all obligations of the Borrower to the Dallas Fed have been satisfied in full. The Credit Risk Management department may inform the institution's primary regulator of the BIC arrangement termination. It is the participating institution's responsibility to request, in writing, the termination of the Dallas Fed's lien.

Electronic Loan Collateral Guidelines

Electronic Loan Collateral

Electronic loan collateral consists of loans that are created and exist in the following manner:

- Signed with a digital signature and stored electronically and not on paper, or
- Signed on paper and then imaged and stored electronically with the paper original destroyed.

Loans are not considered electronic loan collateral if the payment document (i.e., promissory note, loan/lease agreement) is in paper form even if the other transaction documents, modifications, or extensions are in electronic form. Additionally, electronic loan collateral does not include loans with payment documents that are signed on paper and then imaged for convenience or contingency purposes with the paper original retained. Contact the Dallas Fed with questions about whether loans are considered electronic loan collateral.

Prior Approval Required

DIs require prior approval from the Dallas Fed to pledge electronic loan collateral. DIs interested in pledging electronic loan collateral should review these guidelines and determine that they can comply with its requirements. DIs may only pledge electronic loan collateral consisting of the collateral categories marked on the Electronic Collateral Questionnaire and approved by the Dallas Fed. If a DI is interested in pledging electronic loan collateral categories that have not been previously approved, it will need to contact the Dallas Fed and at a minimum, complete a new Electronic Collateral Questionnaire to account for the new electronic loan collateral categories. The Dallas Fed may request that the DI provide an opinion or letter from legal counsel regarding the enforceability of the electronic loan collateral under applicable laws.

Safeguards and Procedures

DIs must comply with the following policies, procedures, and practices in order to pledge electronic loan collateral to the Dallas Fed.

- **General Procedures.** DIs must have policies and procedures for the origination, processing, and storage of the electronic loan collateral records (records). Records must be generated, processed and stored in a manner that ensures that each record accurately reflects the final form of the agreement executed by the parties. Institutions must regularly review and test their procedures for managing records. DIs are responsible for ensuring that all records originated by a third-party comply with the origination, processing, and storage requirements in these guidelines.
- **Authorized Access.** DIs must maintain appropriate software safeguards such as passwords and access rights to protect the integrity of records. Such safeguards must include, among other features, controls to allow only authorized personnel to modify and delete records.
- **Reserve Bank Access.** The Dallas Fed may require institutions to provide analysts with access to records at any time. DIs must have processes for transferring Records to the Dallas Fed or otherwise making records accessible, if required.
- **Contingency Plan.** DIs must have a contingency plan to prevent the loss of records, including a regular schedule for replicating records to serve as back-up copies. If servers storing records or back-up copies are located offsite, DIs must have sufficient physical security and other safeguards to protect the records.
- **Authoritative Copies.** For each electronic obligation that is pledged, the payment document should only have one authoritative copy. An authoritative copy is the readily identifiable master copy of the agreement. Each non-authoritative copy of the payment documents should be readily identifiable as a copy.
- **Controls.** DIs must have sufficient safeguards to prevent the pledge, sale, or transfer of the electronic loan collateral, including electronic mortgage notes and chattel paper, to third parties while they are pledged to the Dallas Fed.
- **Labeling.** DIs must clearly designate or label all electronic loan collateral as being pledged to the Federal Reserve Bank of Dallas. If possible, DIs should segregate the electronic loan collateral from other loans and leases not pledged to the Dallas Fed.
- **Licensing.** Records cannot have licensing conditions that would prohibit, limit, or inhibit, in any form, the Dallas Fed, any assignee, or the purchaser of a liquidated portfolio of collateral, from using the records for any customary business purposes. Limitations may include requirements to pay a fee for the records' use or require approval by a third party.

Storage Providers

DIs must comply with the requirements if it is pledging electronic loan collateral with records stored on the platform of a cloud service provider or any other third-party storage provider (storage provider).

- **Approval.** DIs must receive approval from the Dallas Fed to store records with a Storage Provider. The Dallas Fed may require Storage Providers to execute and deliver a third-party custodian agreement.
- **Safeguards.** Storage Providers must have safeguards to protect records from data loss. Storage providers must maintain their servers in secure facilities and have a contingency plan to prevent data loss from physical damage, power failure and other physical and electronic threats.
- **E-Vault.** If an Institution stores records in an electronic vault ("eVault"), the DI may not grant any party, other than itself or the Dallas Fed, control of the records. An eVault is a system or tool, whether internal or provided by a third party, that enables a secured party or purchaser to establish control of electronic loan collateral in accordance with the Uniform Commercial Code (UCC), Uniform Electronic Transactions Act (UETA) or Electronic Signatures in Global and National

Commerce Act (E-Sign Act). DIs must have controls in place to ensure that no electronic loan collateral stored in an eVault is pledged, sold, or transferred to a third party and that no third party may establish control of the electronic loan collateral while it is pledged to the Dallas Fed. The Dallas Fed may require that DIs grant the Dallas Fed control of electronic loan collateral stored in an eVault. All electronic loan collateral that is pledged and stored in an eVault must clearly indicate that it is pledged to the Dallas Fed, such as including a legend on the records.

Signatures

This section describes requirements for records that are signed with digital signatures and also records that are originated and signed on paper but now only exist in electronic form.

- **Digital Signatures**. If DIs intend to pledge electronic loan collateral with records that are signed with digital signatures, the digital signatures must be attributable to the signers. Attribution may be achieved through any combination of technological methods, business processes, and surrounding circumstances that produce a level of attribution that is appropriate to the document in question, considering the nature of the document and the identities of the parties involved. A single digital signature cannot be applied to multiple electronic documents simultaneously.
- **Enforceability**. All digital signatures must be enforceable under the E-Sign Act and UETA adopted by the state in which the signature is applied, and all other applicable federal and state laws. Institutions are responsible for ensuring that all notarized signatures are performed in accordance with and are legally valid under the laws and regulations of the state in which the notarized signature is performed.
- **Imaged Records.** If DIs intend to pledge electronic loan collateral with records that are originated and signed on paper but now only exists in electronic form, the DI must have policies and procedures for the destruction of the paper copies in a timely and organized manner. If paper copies need to be retained for a period to validate the imaging process, such copies should not be retained any longer than necessary and should be labeled and operationally controlled in a manner consistent with the physical storage and labeling requirements for paper collateral described above in these requirements. DIs must have processes to ensure the quality of the imaged documents.