



SEC Eases 'Regulatory Drag' on Cash Sweep Programs

By Jill Gregorie April 2, 2020

The Securities and Exchange Commission on Monday worked to eliminate a potential blockage to cash-sweep programs and make it easier for brokerages to transfer money from clients' affiliated bank accounts.

To do so, the regulator's Division of Trading and Markets said it would allow broker-dealers to treat the credit balance being moved from clients' sweep accounts held at an affiliated or third-party bank to their securities accounts as "allowable assets," according to a no-action letter sent Monday to Sifma.

Prior to the relief, such transfers were considered "receivables owed," since those transactions typically take one business day to complete because of operational lags, trade group Sifma wrote in its June 26 request for no-action relief.

Assets categorized as receivables owed need to be excluded when broker-dealers calculate their net worth to meet the SEC's financial responsibility requirements. Allowable assets, meanwhile, don't need to be considered in that calculation.

Under the SEC rules, broker-dealers must compute their net capital every week, and always have a minimum amount of net capital at hand. This helps to ensure that they are sufficiently liquid and can meet liabilities, including customer claims and obligations to creditors.

In addition, some brokerages fund their clients' accounts before the bank transfers the money to them, in part so they can provide a "seamless customer experience," the letter says.

Clients seeking to withdraw cash that's been swept into money market funds are also subject to a delay when they seek to withdraw or transact those funds, Sifma wrote. Broker-dealers often prepay so that their customers can obtain cash before their money fund shares can be redeemed.

Clients cannot access bank sweep accounts directly, and must go through their broker-dealer to obtain the assets swept into them, Sifma notes.

Now, firms will not need to take receivables from bank sweep programs into account when calculating their net worth for the purposes of meeting net capital requirements. They cannot rely on Monday's relief, however, if the sweep program is transacted through a bank that is not FDIC-insured, or if the broker-dealer cannot legally demand payment from the bank.

Clients who can obtain cash from the sweep accounts directly are also exempt, the SEC says.

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The change “may seem very technical,” but it will likely benefit distributors and their clients, says Todd Cipperman, founding principal of Cipperman Compliance Services. The lag in money transfer, and ensuing hit to net capital, has amounted to a “regulatory drag” on cash sweep programs for decades, he says.

It will also be good for clients, since brokerages will be more likely to sweep their credit balances into products where they can earn interest, Cipperman says.

In fact, the relief was a “low-hanging fruit” for the commission, since FDIC-insured banks are contractually committed to delivery the money in a timely fashion, he says.

“You look at it and wonder why it was even a problem in the first place,” he says.

The looser standard will also help smaller broker-dealers because it makes it easier for them to sweep investors’ money into bank accounts managed by third parties, Cipperman says.

“This will allow them to compete with a pretty good product” that may be offered by large institutions such as Fidelity and **Schwab**, he says. Fidelity last week waived distribution fees on a \$157.4 billion money fund that serves as the default cash sweep option for clients, as reported.

Earlier this year, Finra flagged cash-sweep arrangements as an exam priority, and noted that brokerages’ practices “have taken on a greater significance” in the wake of evolving commission structures. The self-regulatory organization is monitoring how firms disclose arrangements, and whether they convey whether clients can opt into alternatives to bank sweep programs.

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