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James P. Sheesley
Assistant Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, D.C. 20429

Re: Federal Deposit Insurance Corporation Proposed Rule, "*Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions*," RIN 3064-AF99

To Whom it May Concern:

TechNet appreciates the opportunity to comment on the Federal Deposit Insurance Corporation's (FDIC) proposed rule, *"Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions*." While TechNet understands the desire expressed in the proposal to improve brokered deposit reporting compliance by providing better clarity for insured depository institutions (IDIs) and third parties, the proposal fails to provide that clarity. It would instead introduce new ambiguities and needless complexity that will make it more difficult for entities to understand whether they meet the definition of deposit brokers. Additionally, the proposed rule's implementation could be significantly costly for IDIs and third parties, burdensome on the FDIC itself, and highly disruptive to the financial technology (fintech) innovation ecosystem. **TechNet therefore urges the FDIC to withdraw the proposed rule.**

TechNet is the national, bipartisan network of technology CEOs and senior executives that promotes the growth of the innovation economy by advocating a targeted policy agenda at the federal and 50-state level. Our membership includes dynamic American businesses ranging from startups to the most iconic companies on the planet and represents over 4.5 million employees and countless customers in the fields of information technology, artificial intelligence, e-commerce, the sharing and gig economies, advanced energy, transportation, cybersecurity, venture capital, and finance.

Central to TechNet's work is the idea that America's innovative technology sector is critical to our economic and national security, and businesses should be empowered to flourish and advance, with appropriate guardrails to protect consumers and markets. Unfortunately, the proposed rule appears to do the opposite, arbitrarily tightening restrictions on third party relationships with IDIs despite no apparent need to do so. Instead, it appears that the proposed rule is the result of a divided

FDIC attempting to return to the brokered deposit regime as it existed prior to the current rule, which was adopted in 2020 and has generally allowed innovation to flourish and consumer experiences to improve.

As outlined in the proposed rule, the FDIC's justifications for undermining the 2020 Final Rule are that: (1) After the current rule took effect, there was a significant decline in brokered deposits, which "can be interpreted as IDIs reclassifying a considerable amount of deposits from brokered to not brokered, as a result of the 2020 Final Rule"[1] and its implementation in 2021; (2) The FDIC believes some of the decline in reported brokered deposits is due to "some IDIs misunderstanding and misreporting deposits under the 2020 Final Rule"[2] in the time since it was made effective; (3) If the decline in brokered deposits following the 2020 Final Rule is due to underreporting of brokered deposits, it could be difficult to "evaluate the extent of reliance on brokered deposits"[3] by IDIs today; and (4) a hypothetical risk that "less than well-capitalized IDIs may seek . . . exclusive deposit placement arrangements as their condition is deteriorating without being subject to the limitations on brokered deposits."[4]

Unfortunately, the justifications presented by the FDIC appear to be highly speculative. For example, while it is true that brokered deposits significantly declined immediately following the effective date of the 2020 Final Rule, the proposed rule itself admits that brokered deposit balances began declining before the 2020 Final Rule's effective date, the decline following the 2020 Final Rule was temporary and deposits rebounded, and reported brokered deposits were 22.5 percent higher in the fourth quarter of 2023 than in the quarter before the 2020 Final Rule took effect.[5] In fact, as the FDIC's Chart 1[6] demonstrates, by the fourth quarter of 2023, reported brokered deposits were approximately where they would have likely been based on the trendline prior to the 2020 Final Rule, regardless of the brief initial decline in reported deposits.

If the 2020 Final Rule caused an epidemic of underreporting of brokered deposits, at most that would appear to be an initial and temporary episode. If IDIs misunderstood or misreported deposits under the 2020 Final Rule, then it appears that they have since achieved better understanding and are now reporting deposits correctly. Further, the potential difficulty in evaluating "the extent of reliance on brokered deposits" depends on legitimate brokered deposits being underreported, which is not demonstrated in the proposal.

The benefits of the proposed rule are likewise uncertain. For example, the FDIC's proposal seeks to eliminate the "25 percent test" and replace it with what is

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[1] 89 Fed. Reg. at 68244.
[2] Id. at 68245.
[3] Id.
[4] Id.
[5] Id. at 68249.
[6] Id. at 68250.

functionally a 10 percent threshold available only to broker-dealers and investment advisers registered with the Securities and Exchange Commission. The selection of a new 10 percent threshold appears to be entirely arbitrary, and the FDIC's rationale is merely that a 10 percent threshold "*may* reduce potential risks to safety and soundness"[7] of the system. There is no evidence provided by the FDIC that any such benefits would occur.

While the alleged harms and benefits of the 2020 Final Rule appear to be speculative, the proposed rule unfortunately includes just as much uncertainty regarding potential compliance costs. The proposal admits that it could sweep in significantly more deposits and that it could "potentially affect IDIs, consumers, and nonbank firms,"[8] but the FDIC is unsure how and to what extent. At least 17 times throughout the proposal, the FDIC admits that it does not have the "data necessary to estimate" the effects of the proposed rule, although it admits that it could cause massive changes, including IDIs restructuring their liabilities and even changing their organizational structures.[9] Further, consumers may be incentivized to change or move their deposits as part of a cascading series of changes to banking and finance. The proposed rule does note, however, that the FDIC expects it to result in a "significant increase" in filings for "primary purpose" exceptions, as the FDIC plans to rescind notices and applications that it has approved since the 2020 Final Rule took effect.[10] In other words, the proposed rule admits that there will be costs and cascading, downstream effects of the rule on the banking system—perhaps very significant ones—but contains virtually no legitimate analysis to determine such costs or whether they are worthwhile.

In short, the justifications for the proposed rule are speculative, as are the costs and potential disruptions that the new rule could cause. Unfortunately, the proposed rule itself also undermines the stated purpose of providing regulatory clarity. There are numerous problems with the proposed rule, but this comment focuses on two: First, the proposed rule would improperly include as deposit brokers those who have a clear primary purpose other than placing deposits, including for enabling transactions, while introducing needless enforcement complexity. Second, the proposed rule improperly treats as a deposit broker anyone who receives fees in exchange for placing deposits, even if they do not meet the other parts of the deposit broker definition.

Eliminating the Enabling Transactions Exception and Revising the Primary Purpose Exception Improperly Expands the Rule and Introduces Needless Complexity

The statute is clear that an entity is not a deposit broker if the entity's primary purpose for its relationship with an IDI is anything other than the placement of

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[7] Id. at 68256.
[8] Id. at 68259.
[9] Id.
[10] Id. at 68260

deposits.[11] Any version of the rule that allows the FDIC to define as a deposit broker any entity with a primary purpose other than placing deposits is beyond the scope of the authority granted to the FDIC by the statute, and is in fact contrary to it. The proposed rule attempts exactly this kind of impermissible expansion by eliminating the enabling transactions exception, and by adding unnecessary phrases to obfuscate the primary purpose exception.

As the proposed rule notes, prior to the 2020 Final Rule, the FDIC did not have a bright line distinguishing deposit placement for the sake of deposit benefits from deposit placement for the purpose of enabling others (such as purchasers of prepaid debit cards) to use those deposits to make purchases.[12] The 2020 Final Rule corrected this, providing that a third party could show that its primary purpose was something other than acting as a deposit broker if it was placing deposits not for typical depositor benefits (interest, fees, etc.) but to utilize the account as a network for enabling purchases. If the third party is only placing deposits in accounts that offer none of those typical benefits—no interest, no fees, and no other remuneration for the depositor—then under the current rule it can simply file a notice and both the FDIC and the IDIs can safely assume that those are not brokered deposits. If the account does come with those depositor benefits, it's still possible under the current rule to rely on the enabling transactions designated exception, but doing so requires applying to and receiving pre-approval from the FDIC.

The proposed rule would eliminate the enabling transactions designated exception altogether. It makes no case for this change, instead just flatly concluding that the FDIC "believes that there is no relevant difference between an agent or nominee's purpose in placing deposits to enable transactions and placing deposits to access a deposit account and deposit insurance."[13] This assertion does not withstand even a rudimentary, common-sense analysis. There is certainly a relevant difference between a third party that provides depositors with access to deposit account features such as interest, mobile banking, and the like, and a third party that uses deposit accounts as the backbone to sell prepaid debit cards that are designed to be used until the account is drained and then discarded. No consumer who purchases such a product is likely to do so primarily because the funds on the pre-paid debit card are held at an FDIC-insured depository institution. In fact, most likely don't think about where the value on the card is stored and view it as similar to a gift card. There's also nothing to suggest that any such activities pose a unique risk to liquidity and sound banking practices.

The proposed rule's elimination of the enabling transactions designated exception is not merely an attempt to give the FDIC a greater role in evaluating individual use cases that present a close call relating to the primary purpose. Rather, the proposed rule is clear that the FDIC does not believe that enabling transactions

[11] 12 U.S.C. § 1831f(g)(2)(I).
[12] 89 Fed. Reg. at 68257.
[13] Id.

would satisfy the "proposed primary purpose exception."[14] In other words, the elimination of the exception is specifically intended to cut off fintechs involving enabling transaction innovations from networks of IDIs. Further, the proposed elimination is inconsistent with other parts of the proposed rule. For example, in the proposal's discussion of reducing the "25 percent test" to a 10 percent threshold, the FDIC notes that "placing less than 10 percent of customer funds at IDIs would be more indicative that the primary purpose for broker dealers and investment advisers in placing customer funds at IDIs is to temporarily safe-keep customer free cash balances (*e.g.*, uninvested funds) that are awaiting reinvestment."[15] The same rationale—that temporary safe-keeping of funds until they can be used to purchase something else, such as a security, is not a brokered deposit—should apply to deposits for the purpose of other enabling transactions as well.

Although the statute is clear that any entity with a primary purpose other than placing deposits at an IDI is not a deposit broker, the proposed rule would add additional layers to the definition, requiring not only that there be a different primary purpose but that the alternative primary purpose with the IDI be a "substantial" one.[16] Under the proposed rule, it appears that the default assumption would be that every relationship that relates to placing deposits at an IDI is for the primary purpose of acting as a deposit broker, with the third party then required to demonstrate an alternative primary purpose to avail itself of an exception. However, with the addition of the new "substantial purpose" language, the proposed rule appears to create a new test with a higher burden than the one in the statute. If the FDIC does not intend this and believes that a "primary purpose" will always be "substantial," then the additional language is unnecessary. In either case, the addition of a new clause about a "substantial" alternative primary purpose adds needless complexity to the rule and will make compliance more difficult and costly.

Receipt of Fees or Other Remuneration is Insufficient to Warrant Treatment as a Deposit Broker

Under the current rule, a person is engaged in "the business of facilitating the placement of deposits" if the person: (i) has legal authority, contractual or otherwise, to close the account or move a third party's funds to another IDI; (ii) is involved in negotiating or setting rates, fees, terms, or conditions for the deposit account; or (iii) engages in matchmaking activities (the "Three-Part Test").[17] The proposed rule would expand this definition, among other things, to include a "person [that] has a relationship or arrangement with an [IDI] or customer where the [IDI] or customer pays the person a fee or provides other remuneration in

[14] Id.
[15] Id. at 68256.
[16] Id. at 68253.
[17] 12 C.F.R. § 337.6(a)(5)(iii).

exchange for deposits being placed at one or more [IDIs]."[18] The proposal states that, even "assuming the third party does not meet one of the other parts of the 'deposit broker' definition," where an IDI pays fees to a third party relating to deposits, the third-party deposits "may be more likely to leave the IDI if another IDI were to offer more favorable terms or pay a higher fee."[19] In other words, the proposed rule asserts that the receipt of a fee or other remuneration in connection with deposits, by itself, is sufficient to treat the deposit as less stable and more susceptible to being moved from one IDI to another. This change alone highlights the flaws in the FDIC's dramatic proposed change to its brokered deposit rules discussed above; a change for which the FDIC offers no supporting evidence and a fundamentally flawed rationale.

Historically, the concern with brokered deposits is that they may be less stable sources of bank funding and therefore create greater risk for IDIs. As the proposed rule explains, brokered deposits raised concerns by regulators and Congress because "(1) such deposits could facilitate a bank's rapid growth in risky assets without adequate controls; (2) once problems arose, a problem bank could use such deposits to fund additional risky assets . . . ; and (3) brokered and high-rate deposits were sometimes considered less stable because at the time, deposit brokers (on behalf of customers), or the customers themselves, were often drawn to high rates and prone to leave the bank quickly to obtain a better rate or if they became aware of problems at the bank."[20] The Three-Part Test was carefully designed to address these risks.

However, when the FDIC updated its brokered deposit regulation in 2020, it did not include the receipt of fees or remuneration as a factor in determining whether a person is a deposit broker. At that time, the FDIC concluded that the receipt of fees or other remuneration, in the absence of a person's authority to move deposits, set rates, or allocate deposits among IDIs, did not create the kinds of risks associated with brokered deposits. The proposed rule, without evidence that the payment of fees to intermediaries has affected the stability of referred deposits, would reverse this position.

The proposed rule cites not even a single example to explain how, in the absence of the criteria in the Three-Part Test, the receipt of fees or other remuneration correlates to the risks associated with brokered deposits. Instead, the proposed rule posits an unstable market in which IDIs are bidding for deposits by paying fees to intermediaries in a manner that results in dramatic swings in deposit availability that threaten IDI safety and soundness. If mere payment of compensation in connection with the administration of a referral program were sufficient to cause such instability, we assume the FDIC would have provided ample evidence of such results. The absence of such evidence is telling.

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[18] 89 Fed. Reg. at 68271 (proposed 12 C.F.R. § 337.6(a)(ii)(E)).
[19] Id.
[20] Id. at 68245.

Receiving a fee or other remuneration does not inherently make a deposit riskier; rather, the increased risk associated with brokered deposits arises from the power of a person to control the movement of deposits on a day-to-day basis. That risk does not exist when IDIs pay a fee to a person for an arrangement in which the person does not have legal authority to close an account or move third party funds to another IDI; have any role in negotiating or setting rates, fees, terms or conditions of a deposit account; or engage in matchmaking. In other words, the receipt of fees cannot "incentiviz[e] referral volume of third-party deposits to" IDIs without satisfying another element of the existing Three-Part Test.

The flaws in the FDIC's rationale for this change are further highlighted by its overreach. For example, the FDIC asserts that the mere receipt of a fee somehow would result in a person being a deposit broker, even if the fee is merely "related to" the placement of deposits because receipt of a fee is somehow evidence that the intermediary is "engaged in the business" of facilitating the placement of deposits.[21] The FDIC asserts this is true even if the fees are merely for "administrative services provided in connection with a deposit placement arrangement."[22]

Not only is compensation for administration unrelated to the risks identified above, but the FDIC itself recognized in the proposed rule that the acceptance of fees, in the absence of the authority to move funds, does not make a deposit riskier. The proposed rule states that a passive listing service that receives fees or remuneration would not be considered a deposit broker because passive listing services do not "receive or deposit third-party funds at one or more IDIs"; do not "have the legal authority to close a deposit account or move third party's funds to another IDI"; and "are not involved in negotiation or setting rates, fees, terms or conditions for the deposit account."[23] In other words, in the absence of meeting the other parts of the definition of a deposit broker, the receipt or payment of fees by a passive listing service, by itself, does not make the associated deposits riskier and does not result in such deposits being considered brokered deposits. The proposed rule is thus inconsistent on this basic element of the rationale for treating receipt of fees automatically as a brokered deposit trigger.

Overall, this change would likely result in a substantial amount of deposits being treated as brokered deposits rather than core deposits, based solely on the receipt of a fee or other remuneration, even where a third party does not otherwise satisfy the Three-Part Test, and thus do not present any of the risks associated with brokered deposits. This change will limit the number of banks that can accept these deposits and increase the cost to banks that are able to accept such deposits (e.g., through higher FDIC insurance premiums). The FDIC acknowledges that the proposed rule is also likely to impact third parties that provide services to customers, who may now be considered deposit brokers, which may result in

[21] Id. at 68252.
[22] Id.
[23] Id.

changes in fees and revenue structure that would have an impact on the cost to consumers.[24] Despite these harms, the proposed change would bring no actual benefit in terms of limiting the risks associated with brokered deposits.

Again, TechNet appreciates the opportunity to comment on the proposed rule, and that the FDIC chose to extend the comment period to allow for more fulsome review by stakeholders. While we understand the stated desire to increase clarity and ensure that brokered deposits are appropriately reported, we believe that the proposed rule would do neither. Instead, the proposed rule would introduce new ambiguity, stretch the rule beyond the statutory authority, and increase compliance costs while adding to the size and scale of government bureaucracy. All of these run the risk of stifling innovation for no tangible benefit, and we urge the FDIC to withdraw the proposed rule.

Sincerely,

Carl Holshouser
Executive Vice President

[24] See, e.g., id. at 68259 ("One likely aggregate effect of the proposed changes is that some deposits currently not reported as brokered would be reported as brokered deposits if the proposal is adopted. This may potentially affect IDIs, consumers, and nonbank firms that may be considered 'deposit brokers' under the proposal."); see also id. at 68261 ("To the extent that consumers utilize deposits currently, or in future periods, which are not classified as brokered, but would be as a result of the adoption of the proposed rule, they might experience changes in interest rates on those funds, or costs associated with placing those funds with different entities.").