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January 16, 2024

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

RE: Recordkeeping for Custodial Accounts; RIN 3064–AG07

Dear Sir:

The Independent Community Bankers of America ("ICBA")[1] appreciates the opportunity to respond to the Federal Deposit Insurance Corporation's ("FDIC") proposed rule aimed at enhancing recordkeeping for custodial accounts, particularly those with transactional features. This initiative is designed to ensure timely deposit insurance determinations in the event of a bank failure. While ICBA supports the FDIC's goals, we have significant concerns about the broad scope of the rule, the challenges of implementation, and the potential for unintended impacts on community banks.

Executive Summary

The proposed rule addresses issues arising from fintech-bank partnerships. However, its overly broad compliance requirements could hinder banks' ability to effectively serve their customers. A more focused and tailored approach is necessary to achieve the FDIC's objectives without imposing undue burdens. ICBA recommends the following:

1. **Narrow the scope of the rule:** FDIC should define "custodial accounts with transactional features" to broaden its exemption of accounts that do not function as transactional substitutes or lack pass-through deposit insurance features.
2. **Prioritize practical and realistic compliance measures:** Requirements for written policies and procedures may shift focus from substantive risk mitigation to bureaucratic processes.
3. **Greater use of dormant Bank Service Company Act authority to address risks posed by fintech companies:** Fintech companies that engage "Banking as a Service" model should bear some direct responsibility to ensure rigorous recordkeeping.

[1] The Independent Community Bankers of America® has one mission: to create and promote an environment where community banks flourish. We power the potential of the nation's community banks through effective advocacy, education, and innovation. As local and trusted sources of credit, America's community banks leverage their relationship-based business model and innovative offerings to channel deposits into the neighborhoods they serve, creating jobs, fostering economic prosperity, and fueling their customers' financial goals and dreams. For more information, visit ICBA's website at icba.org.

Background

In April 2024, Synapse Financial Technologies, a banking-as-a-service ("BaaS") company filed for bankruptcy. Synapse served as an intermediary between fintech companies and banks. Synapse's collapse significantly impacted end-users, where accounts for tens of thousands of U.S. businesses and consumers were frozen. Discrepancies in Synapse's ledgers caused its bank partners to suspend access to these accounts to ensure accurate accounting. This situation left many end-users unable to access their funds, causing financial distress.

Investigations revealed a shortfall between the funds held by partner banks and the amounts owed to depositors, estimated between $65 million and $95 million.

The FDIC's proposal stems from the Synapse bankruptcy, to ensure a similar situation does not arise again, which highlighted significant challenges in third-party deposit arrangements. These arrangements, where non-bank entities pool customer funds into custodial deposit accounts at banks, exposed consumers to confusion about deposit insurance coverage and delays in accessing their funds. To address these risks, the FDIC proposes new recordkeeping requirements for insured depository institutions ("IDI"), mandating that they maintain records identifying beneficial owners, their balances, and ownership categories in a specified electronic format. IDIs would also need to ensure the FDIC has direct and continuous access to these records, implement written compliance policies, conduct independent validation, and certify compliance through senior bank officers.

ICBA Comments

1. **The FDIC should narrow the scope to more exclusively focus on the types of accounts that were at issue under the Synapse bankruptcy**

The proposed rule would define "custodial deposit account with transactional features" as a deposit account: (1) established for the benefit of beneficial owners; (2) in which the deposits of multiple beneficial owners are commingled; and (3) through which beneficial owner(s) may authorize or direct a transfer through the account holder from the custodial deposit account to a party other than the account holder or beneficial owner.

While the FDIC wants to ensure that a repeat of the Synapse bankruptcy is avoided, ICBA is concerned that the proposed definition would cover accounts that were not at issue from Synapse customers' inability to access their accounts. For instance, the definition of "custodial deposit account with transactional features" is so broad that it could encompass products like gift cards, corporate expense cards, and single-load payment devices that do not function as substitutes for transactional accounts. Vice Chair Hill noted this in his statement when voting on this proposal, "[T]he proposal estimates that between 600 and 1,100 banks could be scoped in, even though only a few dozen are heavily engaged in the type of activity at which the proposal is targeted."[2]

While these measures address important concerns, they risk overburdening community banks that are unlikely to engage in the types of activities targeted by the proposal.

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[2] Statement of Vice Chairman Travis Hill, Sept. 17, 2024 Board Meeting, *available at* https://www.fdic.gov/news/speeches/2024/notice-proposed-rulemaking-custodial-deposit-accounts-transaction-features-and

2. Prioritize practical and realistic compliance measures

The compliance requirements outlined in the proposal are particularly onerous. The proposed rule would require IDIs to create internal controls that conduct reconciliations against the beneficial ownership records no less frequently than at the close of business daily. The proposed rule would also require covered IDIs to establish and maintain written policies and procedures to achieve compliance with this rule, provide annual certification, conduct independent testing, and senior official attestation as to the accuracy of the testing.

Daily reconciliation of beneficial ownership records, combined with written policies and independent validation, adds administrative complexity without guaranteeing the accuracy of fintech records. Moreover, the certification requirement for senior executives imposes undue liability and seems unnecessary given the FDIC's existing enforcement tools.

ICBA urges the FDIC to adopt a risk-based approach that exempts community banks with minimal involvement in custodial deposit accounts.

3. Greater use of dormant Bank Service Company Act authority to address risks posed by fintech companies

Another significant concern is the rule's focus on banks rather than directly regulating fintech companies. The rule addresses issues caused by fintechs, such as Synapse Financial Technologies, yet imposes requirements on banks instead of directly regulating fintechs. These companies often operate under a "Banking as a Service" model but lack the tools and oversight authority required for compliance. The FDIC's existing authority under the Bank Service Company Act ("BSCA") could be leveraged to address this issue.

As noted in our response to the FDIC's recent Request for Information on bank-fintech relationships, ICBA recommends that the Agencies explore greater use of their authority under BSCA, which provides the ability to regulate and examine the performance of certain services by a third-party service provider for a depository institution (or for any subsidiary or affiliate of a depository institution that is subject to examination by that agency) to the same extent as if such services were being performed by the depository institution itself on its own premises. Increased utilization of BSCA authority will allow for effective use of Agencies' resources, reduced burden to service providers, shared knowledge of the company's operations, development of a joint supervisory strategy, and generation of a single examination report for the companies and their client-regulated banks.

By regulating and examining third-party service providers as if their services were performed by the bank itself, the FDIC could create a unified supervisory strategy for fintechs serving multiple banks. This approach would reduce the burden on banks while improving oversight of interconnected fintechs.

Conclusion

In conclusion, ICBA supports the FDIC's goal of safeguarding depositors and ensuring timely access to funds. However, the proposed rule's broad scope and compliance demands could unintentionally hinder community banks' operations. By refining the rule's focus, prioritizing practical compliance measures, and leveraging BSCA authority, the FDIC can better address the challenges posed by fintech-bank

partnerships without overburdening the banking ecosystem. ICBA appreciates the opportunity to provide feedback and looks forward to continued collaboration with the FDIC.

If you have any questions or would like additional information, please do not hesitate to contact me by email at Michael.Emancipator@icba.org.

Sincerely,

/s/

Michael Emancipator
Senior Vice President and Senior Regulatory Counsel
Independent Community Bankers of America