January 16, 2024

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

Via Electronic Mail

Re: Recordkeeping for Custodial Accounts (RIN 3064-AG07)

Dear Sir or Madam:

Betterment LLC and its affiliate MTG LLC d/b/a Betterment Securities ("Betterment Securities," and collectively, "Betterment") appreciate the opportunity to respond to the Federal Deposit Insurance Corporation's ("FDIC") notice of proposed rulemaking, *Recordkeeping for Custodial Accounts* (the "Proposed Rule").[1]

Betterment supports the FDIC's focus on ensuring "the completeness, accuracy, and integrity of custodial deposit account records."[2] Axiomatically, deposit insurance helps to stabilize the banking system by instilling confidence in depositors that they will have access to their insured deposits, reducing the likelihood of bank runs.[3] Omnibus deposit accounts held by agents, custodians, or intermediaries for the benefit of a large group of beneficial owners have become an increasingly important source of bank deposits, and are eligible for "pass-through" deposit insurance under Section 330.5 of the FDIC's regulations.[4] Under the FDIC's regulations, the critical requirement for pass-through insurance is that the intermediary maintains, in good faith and the regular course of its business, records that indicate the ownership interest of each beneficial owner.[5] The widely publicized April 2024 bankruptcy of Synapse Financial Technologies, Inc. ("Synapse"), and the inability of the FDIC to make timely pass-through

[1] Recordkeeping for Custodial Accounts, 89 Fed. Reg. 80135 (Proposed October 2, 2024) (to be codified at 12 CFR part 375).

[2] *Id.* at 80136.

[3] *See generally* Matt Levine, "Money Stuff: Synapse Still Can't Find its Money" (November 25, 2024), available at https://news.bloomberglaw.com/tax-insights-and-commentary/matt-levines-money-stuff-synapse-still-cant-find-its-money?context=search&index=0.

[4] 12 C.F.R. § 330.5.

[5] 12 C.F.R. § 330.5(b)(1) and 330.5(b)(2).

deposit insurance determinations because Synapse could not reconcile its ledgers, undermined public confidence in the guarantee of deposit insurance.

We fully support the Proposed Rule's efforts to bolster public confidence in pass-through deposit insurance by (1) promulgating recordkeeping requirements for previously unregulated intermediaries while (2) exempting SEC-registered broker-dealers and registered investment advisers ("RIAs") since these entities are already subject to extensive recordkeeping requirements and regulatory supervision.

I. Betterment

Betterment is an automated, easy-to-use investing platform that supports customers in all stages of their wealth-building journeys. Betterment pioneered the use of technology to provide investment advisory services over the internet to retail investors and is sometimes referred to as a "robo advisor" or "digital investment adviser." This service model lowered costs and expanded access to sophisticated advisory services previously only available to affluent investors. Through our website and mobile application, Betterment helps clients identify savings goals, select managed investing portfolios composed primarily of exchange-traded funds ("ETFs"), use retirement planning tools, and participate in our cash management offering, Cash Reserve, whereby client funds are placed at participating program banks ("Program Banks"). Betterment currently manages over $50 billion on behalf of nearly one million clients, with a median age of around 40.

Betterment LLC is an investment adviser registered with the Securities Exchange Commission ("SEC") and offers its investment management services through a wrap fee program with its affiliate, Betterment Securities, a broker-dealer registered with the SEC and the Financial Industry Regulatory Authority ("FINRA") and a member of the Securities Investor Protection Corporation ("SIPC").

II. Cash Reserve

Cash Reserve is a cash management program offered by Betterment LLC. Through the program, Betterment LLC allocates client deposits to interest-bearing, FDIC-insured deposit accounts at Program Banks.[6] Clients' funds earn a variable interest rate and, subject to certain conditions, are eligible for up to $2 million of FDIC insurance (or $4 million of FDIC insurance for joint accounts) once the funds reach one or more Program Banks (up to $250,000 for each insurable capacity—e.g., individual or joint—at each Program Bank). Betterment Securities serves as custodian for clients' Cash Reserve funds, tracks individual client deposits within the omnibus accounts at Program Banks, and issues account statements. In connection with this offering, Betterment provides disclosures to ensure clients comprehend the distinct roles of

[6] As of January 16, 2024, Betterment had 16 participating Program Banks. See "Cash Reserve Holdings" available at www.betterment.com/cash-portfolio.

Betterment LLC (the RIA), Betterment Securities (the broker-dealer), and the Program Banks in the Cash Reserve program.

We respectfully submit that our business model demonstrates the benefits of bank partnerships with financial technology companies ("fintechs") that are themselves subject to considerable regulation. These partnerships promote innovation and competition without sacrificing robust consumer protections or the stability of the banking system.

III. The Proposed Rule Appropriately Distinguishes Between the Risks Posed by Regulated and Unregulated Entities' Involvement

The Proposed Rule reflects an important concern with consumers' ability to access funds placed at banks in deposit accounts that aggregate funds of multiple customers ("omnibus accounts") in connection with FDIC-insured depository institutions ("IDI")-non-bank company partnerships, or where an unregulated third-party intermediary, such as a fintech, plays a critical role in recordkeeping individual customer ownership interests in an omnibus account.[7] Bank-fintech relationships have grown in recent decades, and customer balances in such programs now represent a meaningful source of funding for depository institutions that participate in bank-fintech programs.[8] Betterment agrees that there are risks associated with recordkeeping for omnibus accounts conducted by unregulated entities, and commends the FDIC's recognition that not all fintech providers are similarly situated with respect to regulatory oversight.

A. Bank-Fintech Offerings Relying on Pass-Through Insurance Benefit both Consumers and the Banking System

Bank-fintech cash management programs that offer pass-through FDIC insurance benefit consumers in numerous ways. There is robust competition between cash management programs offered by a wide range of financial providers (not only fintechs), which seek to differentiate their offerings through the quality of their user experiences and the appeal of their terms. In particular, cash management programs offered through bank-fintech partnerships feature user-friendly interfaces, allow customers to aggregate FDIC insurance across multiple participating partner banks, offer competitive yields that are often substantially higher than those

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[7] "Synapse Bankruptcy: Customers Say They Can't Access Funds" (May 22, 2024), available at https://www.cnbc.com/2024/05/22/synapse-bankruptcy-customer-funds.html. *See also* Request for Information on Bank-Fintech Arrangements Involving Banking Products and Services Distributed to Consumers and Businesses, 89 Fed. Reg. 61577 (Proposed July 31, 2024).

[8] Paul T. Clark, *Just Passing Through: A History and Critical Analysis of FDIC Insurance of Deposits Held by Brokers and Other Custodians*, 32 Rev. Banking & Fin. L. 99, 151 (2012), available at https://www.bu.edu/rbfl/files/2013/09/Just-Passing-Through.pdf.

offered by legacy banks on savings accounts, and can reach customer populations that are often underserved by legacy providers.

These arrangements also benefit participating partner banks. By pre-negotiating their preferred capacity for deposits, partner banks benefit from control and predictability. In addition, partner banks incur far lower acquisition costs for such deposits than they would by having to acquire each customer individually. The ongoing costs of servicing customer deposits held in omnibus accounts is also lower for partner banks given that such costs are ultimately borne by the fintech rather than the bank. Moreover, bank-fintech arrangements can reduce concentration risk in the banking system by allowing smaller regional banks[9] to compete with national banks for customer deposits.[10]

Bank-fintech cash management offerings like Betterment's Cash Reserve can provide deposit stability during periods of stress in the broader financial system.[11] Deposits that banks receive through Cash Reserve tend to be sticky, and Betterment carefully manages overall deposit allocations across participating Program Banks based on pre-negotiated contractual relationships that specify capacity, rates, and fees. Betterment's internal analysis of its Cash Reserve data from March 2023 demonstrates that brokered deposits were not "hot money" during this period of market turmoil: Cash Reserve deposit and withdrawal activity remained remarkably consistent with prior and future periods. Our analysis points to several likely contributing factors. First, by offering Cash Reserve through multiple Program Banks, clients are diversified against the risk of any individual bank's failure. Second, the higher amount of potential FDIC coverage offered by Cash Reserve reduced the likelihood that Betterment customers had uninsured deposits at risk in the event of a bank failure. And third, Betterment maintained – and actually raised – its APY rates during the spring of 2023.[12]

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[9] As of January 16, 2024, nine of the 16 participating Program Banks in the Cash Reserve program are regional banks.

[10] The benefits of bank-fintech arrangements for small banks are reciprocal. See "The New Venture Capitalists: How Community Banks Are Fueling The Growth Of Fintech" (January 23, 2023) available at https://www.forbes.com/sites/ronshevlin/2023/01/23/the-new-venture-capitalists-how-banks-are-fueling-the-growth-of-enterprise-fintech/.

[11] *Bank allies say FDIC brokered deposit plan reflects outdated thinking*, Ebrima Santos Sanneh, American Banker (Aug. 7, 2024), available at https://www.americanbanker.com/news/bank-allies-say-fdic-brokered-deposit-plan-reflects-outdated-thinking (noting a "wealth of recent evidence that deposits sourced through fintech partnerships are actually quite stable.").

[12] Megan Fitzgerald, Danielle Goldenberg, "Betterment Comment Letter Re: Unsafe and Unsound Banking Practices: Brokered Deposits Restriction" (November 20, 2024) at 4, available at *https://www.fdic.gov/federal-register-publications/betterment-megan-fitzgerlad-and-danielle-goldenberg-rin-3064-af99*.

B. Regulated Fintechs are not Subject to the Same Recordkeeping Failure Risks as Unregulated Fintechs

As the Proposed Rule recognizes, certain bank-fintech partnerships are offered through unregulated entities, while others are offered by already-regulated RIAs and/or broker-dealers. Betterment's Cash Reserve offering is an example of a bank-fintech arrangement that is subject to oversight by multiple regulatory bodies, specifically the SEC and FINRA. As an RIA, Betterment LLC's digital advisory services, including with respect to Cash Reserve, are subject to the fiduciary requirements of the Investment Advisers Act of 1940. Additionally, the SEC imposes stringent communication and disclosure requirements on RIAs. Betterment Securities performs funds transfers and recordkeeping subject to the requirements of Securities Exchange Act of 1934 Rule 15c3-3 (the "Customer Protection Rule").[13] Betterment Securities is required by law to segregate customer assets from its own, to record-keep and custody client assets for the benefit of its customers, to set aside net capital reserves based on ratios specified in the Customer Protection Rule, and to have policies and procedures in place to maintain a clear deposit and transaction system of record. Supervisory regulators routinely examine RIAs and broker-dealers for compliance with these requirements, helping to ensure that they will possess the appropriate custodial account records in the event a deposit insurance determination is required.

The Proposed Rule seeks to address important concerns about recordkeeping of omnibus deposit accounts by unregulated entities. Collective confidence in the deposit insurance guarantee (including as it relates to pass-through insurance) has been a fundamental unpinning of the safety and soundness of the banking system since the passage of the Federal Deposit Insurance Act.[14] The highly publicized failure of Synapse and the corresponding delays in customers gaining access to their insured deposits undermined confidence in deposit insurance. Unregulated intermediaries such as Synapse should be subject to a standard set of recordkeeping requirements that facilitate the timely resolution of deposit insurance determinations should they become necessary, which will help to restore public faith in the guarantee of deposit insurance.

We also commend the FDIC's proposed exemption of federally regulated broker-dealers and RIAs from the requirements of the Proposed Rule, in recognition of the considerable oversight to which these entities are already subject.[15] The Proposed Rule's targeted approach will fill gaps in existing regulatory oversight of unregulated entities but avoids painting with an unnecessarily broad brush. By exempting custodial accounts established by RIAs and broker-dealers, the Proposed Rule appropriately avoids introducing duplicative oversight of these regulated entities, which would serve to increase compliance costs without any commensurate benefit to consumers or to safety and soundness.

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[13] 17 CFR § 240.15c3-3.

[14] Clark *supra* note 8, at 100.

[15] 89 Fed. Reg. 80135.

IV. Conclusion

The Proposed Rule will plug needed gaps in the current regulatory oversight of custodial deposit account recordkeeping, to the benefit of both consumers and the banking system. The FDIC wisely exempts already regulated broker-dealer and investment advisers from the proposed requirements. Betterment supports the Proposed Rule and urges the FDIC to adopt it.

Sincerely,

[redacted]

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