November 20, 2024

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

Via Electronic Mail

Re: Unsafe and Unsound Banking Practices: Brokered Deposits Restriction (RIN 3064-AF99)

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, *Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions* (the "Proposed Rule").[1]

The Proposed Rule reflects a concern that brokered deposit arrangements are potentially destabilizing absent sufficient limitations and controls. Betterment shares the FDIC's interest in the safety and soundness of the banking system. However, as demonstrated by Betterment's own cash management offering, we believe deposits that partner banks receive through sweep programs offered by investment advisers and broker dealers do not pose the risks associated with "hot money" articulated in the Proposed Rule. Nor do we believe that the FDIC has set forth a sufficient justification for upsetting the current framework governing brokered deposits, upon which participants in the marketplace have been relying, and which went into effect not even four years ago. If enacted in its current form, the Proposed Rule is likely to have a chilling effect on deposit programs offered through bank-fintech partnerships that benefit consumers and banks alike.

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

[1] Unsafe and Unsound Banking Practices: Brokered Deposits Restrictions, 89 Fed. Reg. 68244 (Proposed August 23, 2024) (to be codified at 12 CFR parts 303 and 307).

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 its 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 and Betterment Securities. Through the program, Betterment LLC allocates client deposits to interest-bearing, FDIC-insured deposit accounts at Program Banks. Clients' funds earn a variable interest rate and 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).[2] Betterment Securities serves as custodian for clients' Cash Reserve funds.

III. The FDIC has not Justified Upsetting the Settled Expectations of the Brokered Deposits Market

The Proposed Rule effectively dials back the clock on the FDIC's 2020 brokered deposits rulemaking (the "2020 Rule").[3] The FDIC designed a framework in the 2020 Rule that supports a robust market for cash deposit programs, particularly deposits placed through bank-fintech partnerships, while also mitigating potential risks of such programs. Banks and their partners rely on the 2020 Rule, and the Proposed Rule would upset market expectations in this sector with detrimental consequences.

A. Deposits Placed Through Investment Advisers and Broker-Dealers can be Stable and Predictable for Banks

Cash sweep programs offered through partnerships with investment advisers and broker dealers unquestionably benefit the banks that enter into such partnerships. 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 customers with

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[2] As of October 30, 2024, Betterment had 16 participating Program Banks. See "Cash Reserve Holdings" available at www.betterment.com/cash-portfolio.

[3] Unsafe and Unsound Banking Practices: Brokered Deposits and Interest Rate Restrictions, 89 Fed. Reg. 6742 (Jan. 22, 2021) (codified at 12 CFR parts 303 and 307).

brokered deposits is also lower for partner banks given that such costs are ultimately borne by the investment adviser or broker dealer offering the sweep program. Moreover, sweep programs can reduce concentration risk in banking by allowing smaller regional banks[4] to compete with national banks for customer deposits.[5]

Cash sweep programs also benefit consumers. There is robust competition between cash sweep 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, sweep arrangements offered through 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 offered by legacy banks on savings accounts, and can reach customer populations that are often underserved by legacy providers.

Cash management offerings like Betterment's Cash Reserve can provide deposit stability during periods of stress in the broader financial system.[6] Deposits that banks receive through Cash Reserve tend to be sticky, and we carefully manage overall deposit allocations across participating Program Banks based on pre-negotiated contractual relationships that specify capacity, rates, and fees. Cash Reserve deposits also tend to be sticky because customers benefit from the ability to stack FDIC insurance, with a highly competitive interest rate as compared to currently offered rates on most traditional savings accounts.[7]

We disagree with the proposal's assertion that brokered deposits "can be highly unstable, with either the third party or the underlying customers moving funds based on market conditions or other factors."[8] To the contrary, reports from March 2023 attributed the banking failures of First Republic, Silicon Valley Bank, and Signature Bank not to significant brokered deposit withdrawals; rather, social media panic and subsequent massive withdrawals of core deposits through digital banking tools fueled the runs on these banks.[9] Technological advancements in

[4] As of October 30, 2024, nine of the 16 participating Program Banks in the Cash Reserve program are regional banks.

[5] 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/

[6] "The brokered deposit proposal . . . ignores a wealth of recent evidence that deposits sourced through fintech partnerships are actually quite stable.'" *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.

[7] *See* Goldberg, Matthew, "What is the average interest rate for savings accounts?" (November 14, 2024), available at https://www.bankrate.com/banking/savings/average-savings-interest-rates/.

[8] S*ee supra* fn. 1 at 68250.

[9] *See* Laurence Darmiento, California regulator cites social media, digital banking as key factors in Silicon Valley Bank's failure, *LA Times* (May 8, 2023), available at https://www.latimes.com/business/story/2023-05-08/california-regulator-cites-social-media-digital-banking-as-key-factors-in-silicon-valley-banks-failure (citing a report by the California Department of Financial Protection and

banking have progressed such that nearly all banking customers can make instant, effectively frictionless withdrawals of core deposits, weakening the assumption that core deposits are stickier than brokered deposits.

Indeed, 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 stress: 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.

B. Financial Services Companies Rely on the 2020 Rule, Including the 25% Test of the Primary Purpose Exception ("PPE")

The Proposed Rule undercuts the reliance interests of the financial services industry and threatens to upset the status quo in unknown ways. It also proposes a PPE threshold that has no rational connection to the underlying statutory exemption. Accordingly, the FDIC should allow the current framework to stand undisturbed.

The Proposed Rule would needlessly penalize cash management programs that currently satisfy the 25% test of the PPE, including Betterment's Cash Reserve offering.[10] Because banks seek to manage the ratio of core to brokered deposits for purposes of maintaining their liquidity ratios and managing their deposit-insurance assessments, banks pre-plan available capacity and the cost of funds at which they are willing to offer that capacity. Returning to the pre-2020 PPE threshold will cause the industry to seesaw back to the old framework after several years of effective reliance on the 2020 Rule, upon which industry participants have performed diligence, built banking relationships, and implemented compliance processes.[11]

The Proposed Rule also includes major changes to the process for obtaining a PPE under the 10% test, and would wipe out all existing PPEs obtained through the notice and application process of the 2020 Rule. The administrative and regulatory burden of reapplying under new rules, with new notice and effectiveness provisions, will be substantial and should be taken into account.

Moreover, abandoning the 25% threshold would further untether the brokered deposits framework from any statutory basis. Namely, the Proposed Rule seeks to justify the 10% threshold based on a requirement that an agent demonstrate that it is acting for a "substantial

Innovation stating that "[w]hile many internal factors made Silicon Valley Bank susceptible to a bank run, both social media and digital banking technology accelerated the volume and speed of the deposit outflows."')

[10] See Public Report of Entities Submitting Notices for a Primary Purpose Exception (PPE) as of 3/15/2024, available at https://www.fdic.gov/resources/bankers/brokered-deposits/public-report-ppes-notices.pdf

[11] "FDIC Whipsaws Industry with Proposed Changes to Brokered Deposits Rules" (August 6, 2024) available at https://www.sewkis.com/publications/fdic-whipsaws-industry-with-proposed-changes-to-brokered-deposits-rules/

purpose" other than to place deposits to achieve FDIC deposit insurance, but that requirement is nowhere to be found in the Federal Deposit Insurance Act.[12] And the Proposal provides no basis for concluding that 10% is the appropriate threshold for determining that a particular activity is the "primary" purpose of an entity. If anything, under the plain meaning of the term "primary," a numerical PPE standard that bears a rational relationship to the underlying statute would simply test whether brokered deposits constitute less than 50% of an agent's assets under administration.

To take Betterment as an example, the primary purpose of Betterment's business is not the placement of funds with banks. Betterment LLC is an investment adviser that offers investment advisory services to retail investors through a wrap fee program. Its affiliate, Betterment Securities, is a broker-dealer that provides execution and custody services to support Betterment LLC's wrap fee program. Betterment's core investment advisory business entails managing investment portfolios. While Cash Reserve is available to clients as part of their broader investment advisory relationship with Betterment, placing deposits is plainly not the "primary purpose" of Betterment's business, nor the focal point of its relationship with clients. This is the case for other investment advisers and broker-dealers as well.

IV. Conclusion

The framework established by the 2020 Rule has helped banks diversify their deposit sources and encouraged competition that benefits consumers. The Proposed Rule would undercut the benefits of this framework without any corresponding benefit to bank safety and soundness. Moreover, there is no plausible justification in the Proposed Rule for upsetting market expectations and reliance interests just four years after the 2020 Rule was promulgated. We respectfully submit that the FDIC should withdraw the Proposed Rule.

Sincerely,

[redacted]

Megan Fitzgerald
Director, Legal

[redacted]

Danielle (Daina) Goldenberg
Legal Counsel

[12] The Federal Deposit Insurance Act excludes from the definition of deposit broker an "agent or nominee whose primary purpose is not the placement of funds with depository institutions." 12 U.S.C. § 1831f(g)(2)(I).