



STATE OF NEW YORK
OFFICE OF THE ATTORNEY GENERAL

LETITIA JAMES
ATTORNEY GENERAL

212.416.8050

January 16, 2025

BY ELECTRONIC SUBMISSION

Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

*Letter with Supporting Comments on Proposed Rule on
Recordkeeping for Custodial Accounts (RIN 3064-AG07)*

Dear FDIC Board:

We, the undersigned attorneys general for New York, California, Colorado, Connecticut, Delaware, the District of Columbia, Illinois, Maine, Maryland, Massachusetts, Michigan, Minnesota, Nevada, New Jersey, Oregon, Pennsylvania, and Vermont (collectively, the “State AGs”) write in measured support of the Federal Deposit Insurance Corporation’s (“FDIC”) proposed rule concerning recordkeeping for custodial accounts,¹ and to urge the FDIC and other federal banking regulators to review with skepticism and enhanced supervision the rapidly growing practice of state and federally chartered banks partnering with nonbank entities that offer banking-like products and services directly to consumers.

The fallout from the Synapse bankruptcy and the decision by Evolve Bank and Trust (“Evolve”)—referred to in the Proposed Rule as an unidentified “IDI”—to freeze deposits in Evolve accounts has been nothing short of a calamity for individual consumers. Tens of millions of dollars belonging to tens of thousands of consumers have been locked up for months, unjustly denying many individual consumers access to wages, income, or benefits.² And the lack of adequate and reliable records that reflect which funds deposited into Evolve accounts by a variety

¹ Federal Deposit Insurance Company, *Notice of Proposed Rulemaking: Recordkeeping for Custodial Accounts*, 89 Fed. Reg. 80135 (Oct. 2, 2024) (hereinafter, the “Proposed Rule”).

² Associated Press, *Abrupt Shutdown of Financial Middleman Synapse has Frozen Thousands of American’s Deposits* (May 22, 2024), available at <https://apnews.com/article/synapse-evolve-bank-fintech-accounts-frozen-07ecb45f807a8114cac7438e7a66b512>.

of nonbank entities who offer direct-to-consumer banking and banking-like products belong to which consumers has prevented the FDIC or any other federal banking regulator from stepping into the void and providing interim relief to suffering individuals.³

The State AGs have serious doubts that the bank partnership model is beneficial to consumers. These concerns are amplified by the State AGs' experiences with noncompliance by nonbank partners who have contractually agreed to assume responsibility for banks' obligations under state or federal consumer protection laws. For example, one State AG investigation revealed that thousands of consumers' bank accounts were illegally restrained and tens of thousands of dollars were illegally removed after a bank contractually transferred responsibility for handling exemptions from debt collection to its nonbank partner.⁴ Other publicly reported matters include partnerships that promoted predatory loans promising consumers that they could make "\$5,000 a month while sitting on your toilet"⁵ and multiple banks entering into consent orders with the FDIC for their repeated failures to appropriately manage risks related to bank partnerships.⁶ These and other experiences raise serious questions about nonbanks' ability to properly ensure compliance with the state and federal consumer protections to which their bank partners are subject. And the State AGs also are aware from their own investigations that it is not at all uncommon for the nonbank partners—which are often relatively small technology companies that have little-to-no experience with compliance and oversight, financial regulations, or customer service beyond in-app communication—to farm out obligations such as complaint intake or dispute resolution to other third parties, meaning that banks' core responsibilities in these areas are not merely one but two steps removed from oversight by the FDIC and other regulators.

Even more troubling is the practice of certain banks that attract consumer deposits or engage in consumer lending primarily through nonbank partners to enter into partnerships for the primary purpose of evading state consumer protection laws by "renting" bank charters and their associated exemptions from those state consumer protections.⁷ While the FDIC has publicly stated that these arrangements cannot evade state consumer protections, the broad interpretation of interest when asserting federal preemption by the FDIC and other federal banking authorities⁸ effectively allows such partnerships to sidestep many state consumer protections by linking those protections to the concept of interest. Several state regulators have had success addressing these

³ Forbes, *Federal Bank Regulators Won't Rescue Fintech Customers Caught in Synapse Bankruptcy* (May 17, 2024), <https://www.forbes.com/sites/emilymason/2024/05/17/federal-bank-regulators-wont-rescue-fintech-customers-caught-in-synapse-bankruptcy/>.

⁴ New York State Office of the Attorney General, *Attorney General James Secures More than \$700,000 from Pathward Bank for Illegally Freezing Bank Accounts and Turning Over Consumer Funds to Debt Collectors* (Apr. 17, 2024), available at <https://ag.ny.gov/press-release/2024/attorney-general-james-secures-more-700000-pathward-bank-illegally-freezing-bank>.

⁵ Financial Times, *Shadow Banking Drives a Rural Kentucky Lender to the Brink* (Aug. 19, 2024), available at <https://www.ft.com/content/eae4b603-e4c0-429c-94c3-5fb8fa034eb3>.

⁶ Consent Order No. FDIC-24-0022b, *In re Thread Bank* (May 21, 2024); Consent Order No. FDIC-23-0041b, *In re Lineage Bank* (Jan. 29, 2024); Consent Order No. FDIC-23-0086b, *In re Choice Fin. Grp.* (Dec. 13, 2023).

⁷ National Consumer Law Center, *Rent-a-Bank Loans*, available at <https://www.nclc.org/topic/rent-a-bank-loans/>.

⁸ See, e.g., FDIC, *Federal Interest Rate Authority*, 85 Fed. Reg. 44146 (Jul. 22, 2020)

evasions directly through enforcement actions against nonbank partners.⁹ But until the FDIC and other federal banking regulators prohibit or restrict the banks that they supervise from facilitating these evasive tactics, consumers will continue to have illegal products pushed on them by nonbanks sheltering under bank charters that they do not hold.

The above is beyond the scope of the Proposed Rule. Thus, without intending to limit or cabin the serious concerns with bank partnerships expressed above, the State AGs write to support the FDIC’s Proposed Rule to strengthen recordkeeping by requiring banks who hold deposits on behalf of nonbank partners to maintain uniform and reliable records of the beneficial ownership of those deposits, including by individual consumers,¹⁰ and to develop internal controls to ensure the accuracy and reliability of those records,¹¹ as a minimum first step to ensuring compliance by banks and their nonbank partners with state and federal consumer protections.

However, while supportive of the end goal of enhanced consumer protection embodied by the Proposed Rule, the State AG’s also are concerned that the Proposed Rule permits banks to rely on their nonbank partners to satisfy the new recordkeeping requirements.¹² Under this carveout, nonbanks—who are not chartered financial institutions and are not in the State AGs’ experience generally subject to routine, “boots on the ground” supervision—can remain responsible for developing and implementing “appropriate internal controls” to ensure accurate deposit records, subject to an annual review by an independent third party.¹³ The State AGs believe it is inadvisable to permit nonbank partners to assume the central responsibilities for recordkeeping and compliance with a Proposed Rule, merely subject to an annual review, when the genesis for the Proposed Rule was the utter failure to maintain accurate records by a nonbank partner in the first place.¹⁴ Indeed, a few months before issuing the Proposed Rule, the FDIC issued a joint statement with the Federal Reserve and the Office of the Comptroller of the Currency highlighting “potential risks related to arrangements between banks and third parties to deliver bank deposit products and services to end users.”¹⁵ In addition to rightly acknowledging that such partnerships

⁹ See, e.g., Assurance of Discontinuance, *In re Duvera Billing Services, LLC d/b/a EasyPay Finance* (May 20, 2024), available at <https://www.mass.gov/doc/easypay-assurance-of-discontinuance/download> (Massachusetts Attorney General); Assurance of Voluntary Compliance, *In re Duvera Billing Services, LLC d/b/a EasyPay Finance* (Jul. 10, 2023), available at <https://oag.dc.gov/sites/default/files/2023-07/AVC%20full%20executed.pdf> (District of Columbia Attorney General); Stipulation and Final Agency Order, *In re Duvera Billing Services, LLC DBA EasyPay Finance* (Apr. 20, 2023), available at <https://coag.gov/app/uploads/2023/04/23.04.20-Final-EasyPay-Settlement-Agreement-fully-executed.pdf> (Colorado Attorney General).

¹⁰ Proposed Rule § 375.3(a), 89 Fed. Reg. at 80152.

¹¹ Proposed Rule § 375.3(b), 89 Fed. Reg. at 80152.

¹² Proposed Rule § 375.3(c), 89 Fed. Reg. at 80152.

¹³ *Id.*

¹⁴ See Martin J. Gruenberg, FDIC Chairman, *Statement on Proposed Rule* (Sep. 17, 2024), available at <https://www.fdic.gov/news/speeches/2024/statement-martin-j-gruenberg-chairman-fdic-notice-proposed-rule-requirements> (explaining that the Proposed Rule was promulgated in response to “significant deficiencies and discrepancies in the records essential to accurately determine individual consumers’ account balances” maintained by Synapse that highlighted “the importance of complete, accurate, and reliable” records).

¹⁵ Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, *Joint Statement on Banks’ Arrangements with Third Parties to Deliver Bank Deposit Products and Services* at 1 (July 25, 2024), available at https://www.fdic.gov/system/files/2024-07/joint-statement-on-third-party-deposit-products_0.pdf (hereinafter, the “Joint Statement”).

pose risks to banks' ability to achieve compliance goals, to manage risks in ways that protect consumers, and to avoid conflicts of interest, the Joint Statement highlights that bank partnerships frequently result in a "lack of sufficient access by a bank to the deposit and transaction system of record and other crucial information and data" that is maintained by the nonbank partner.¹⁶

The concerns expressed by the FDIC and its federal partners in the Joint Statement are shared by the State AGs. Multiple ongoing investigations by the State AGs have revealed that banks who partner with nonbank entities and rely on those nonbanks to maintain key records and other data often have virtually no insight into the facts on the ground related to their nonbank partners' operations. During investigations, the State AGs have asked for records, summaries, or data related to key banking functions and have been told that such information was not readily available to the banks. Examples include a bank holding no transaction-level data when the bank purports to be the "true lender" on loans and a bank's failure to possess actual copies of account restraints, garnishments, or levies directed at its consumers' deposit accounts. The State AGs are skeptical, to say the least, that these deficiencies will be cured by an annual inspection.

The State AGs recognize that the FDIC has expressed concern with the recent, substantial rise of bank partnerships that result in core bank functions being performed by nonbank entities, including through issuance of the Joint Statement.¹⁷ For example, and for very good reasons, the FDIC remains appropriately skeptical of industrial loan company applications that would provide nonbank entities with ready means to avoid state lending laws entirely while also skirting oversight by the Federal Reserve.¹⁸ And the State AGs applaud both the previously referenced consent orders targeting multiple problematic bank partnership practices, as well as the FDIC's downgrade to the performance rating of one of its regulated banks for unfair or deceptive practices that it engaged in while partnering with a nonbank entity to aggressively push absurdly expensive consumer loans that routinely carried APRs in excess of 100%.¹⁹

However, the State AGs remain highly skeptical as to whether the bank partnership model is a positive one for consumers. The State AGs note with concern recent court filings describing investigations by a nonbank whose customers lost access to more than \$100 million that indicate that Synapse and Evolve conspired to misappropriate tens of millions in consumer deposits.²⁰ This raises obvious concerns about the financial incentives in bank partnerships. But more to the point: Should these assertions prove true and Evolve be implicated in misappropriation

¹⁶ *Id.*

¹⁷ *See generally id.* at 2–4 (describing various risks related to banking operations, compliance with state and federal laws, and consumer confusion arising from bank partnerships).

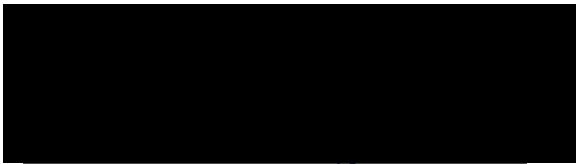
¹⁸ *See* CNBC, *Wal-Mart Will Pull Bank Application, FDIC Says* (Mar. 16, 2007) (statement by then-FDIC chair that "Wal-Mart made a wise choice" regarding withdrawal of ILC application).

¹⁹ Consumer Federation of America, *TAB Bank, Facilitator of Predatory Puppy Loans, Gets Rating Downgrade by FDIC* (Feb. 6, 2023), available at https://consumerfed.org/press_release/tab-bank-facilitator-of-predatory-puppy-loans-gets-rating-downgraded-by-fdic/.

²⁰ *See generally* Complaint, *Yotta Technologies, Inc. v. Evolve Bancorp, Inc. et al.*, No. 24 Civ. 6456 (N.D. Cal. Sep. 13, 2024), ECF No. 1 ("This is a case about a bank that utterly failed in its most basic duty to its customers, misappropriating and/or misplacing tens of millions of dollars in customer funds.").

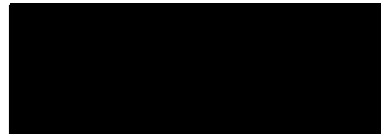
of consumer funds in concert with or facilitated by Synapse, it is not at all clear that the Proposed Rule would have prevented any of the harms that the FDIC cites to justify it in the first place.

For all of the above reasons, the State AGs generally support the Proposed Rule but respectfully comment that the final rule should eliminate banks' ability to assign primary responsibility for recordkeeping and controls to their nonbank partners. The State AGs further urge the FDIC and federal banking regulators to prohibit their regulated banks from engaging in partnership with nonbank entities to evade state consumer protection laws through preemption, and to otherwise restrict or—at minimum—engage in enhanced supervision of all banks that attract consumer deposits predominantly through partnerships with nonbank entities.

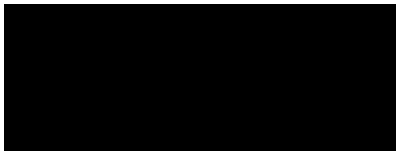


LETITIA JAMES
ATTORNEY GENERAL
STATE OF NEW YORK

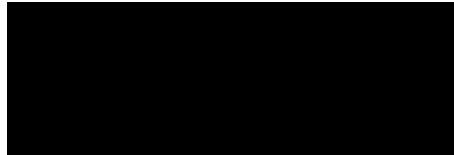
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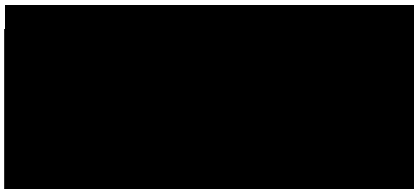
ROB BONTA
ATTORNEY GENERAL
STATE OF CALIFORNIA



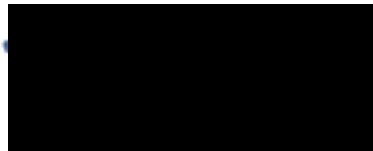
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ATTORNEY GENERAL
STATE OF COLORADO



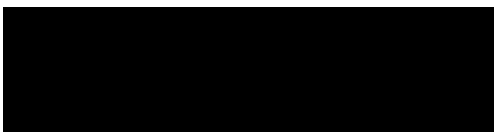
WILLIAM TONG
ATTORNEY GENERAL
STATE OF CONNECTICUT



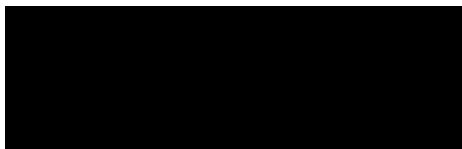
KATHLEEN JENNINGS
ATTORNEY GENERAL
STATE OF DELAWARE



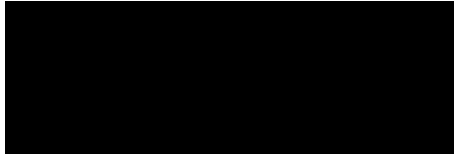
BRIAN L. SCHWALB
ATTORNEY GENERAL
DISTRICT OF COLUMBIA



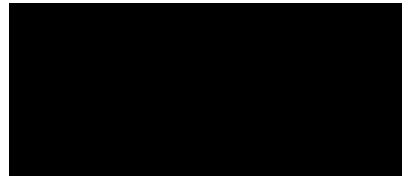
KWAME RAOUL
ATTORNEY GENERAL
STATE OF ILLINOIS



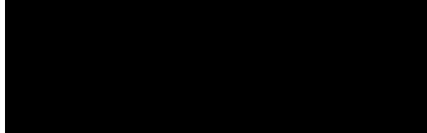
AARON M. FREY
ATTORNEY GENERAL
STATE OF MAINE



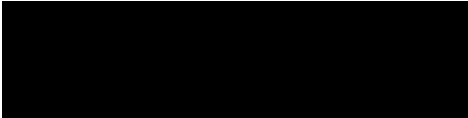
ANTHONY G. BROWN
ATTORNEY GENERAL
STATE OF MARYLAND



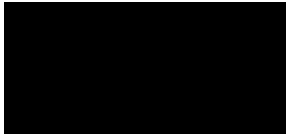
ANDREA JOY CAMPBELL
ATTORNEY GENERAL
COMMONWEALTH OF
MASSACHUSETTS



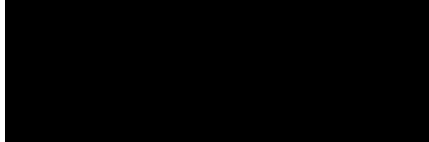
DANA NESSEL
ATTORNEY GENERAL
STATE OF MICHIGAN



KEITH ELLISON
ATTORNEY GENERAL
STATE OF MINNESOTA



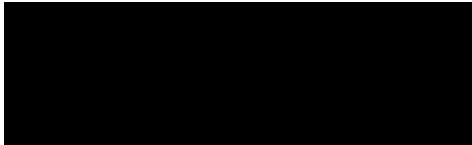
AARON D. FORD
ATTORNEY GENERAL
STATE OF NEVADA



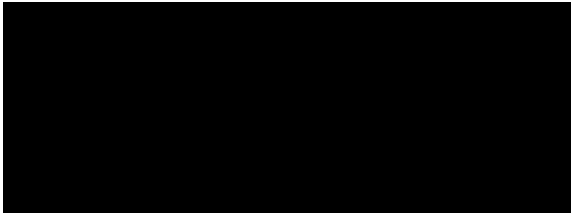
MATTHEW J. PLATKIN
ATTORNEY GENERAL
STATE OF NEW JERSEY



DAN RAYFIELD
ATTORNEY GENERAL
STATE OF OREGON



MICHELLE A. HENRY
ATTORNEY GENERAL
COMMONWEALTH OF
PENNSYLVANIA



CHARITY R. CLARK
ATTORNEY GENERAL
STATE OF VERMONT