INDEPENDENT COMMUNITY BANKERS OF AMERICA, MICHAEL EMANCIPATOR

Proposal and Comment Information

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Submitter Information

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RE: Request for Information on Bank-Fintech Arrangements Involving Banking Products and Services Distributed to Consumers and Businesses; Docket ID OCC-2024-0014; Docket No. OP-1836; RIN 3064-ZA43

Dear Sir or Madam:

The Independent Community Bankers of America ("ICBA")[1] appreciates the opportunity to provide comment in response to the Federal Deposit Insurance Corporation's ("FDIC"), the Office of Comptroller of the Currency's ("OCC") and the Board of Governors of the Federal Reserve System's ("FRB") (collectively, "Agencies) Request for Information ("RFI") on bank-fintech arrangements involving banking products and services distributed to consumers and businesses.

Given their ability to be nimble and responsive, community banks have historically enjoyed a strong lead in customer satisfaction over their larger counterparts. Coupled with the technological skills of fintechs, community banks are well-positioned to blend the strengths of their operations with fintech innovations.

Executive Summary

As bank-fintech partnerships have become more prevalent and increasingly complex, ICBA welcomes the Agencies' engagement on this matter. We believe the comments submitted in response to the RFI will spark renewed policy discussions that will eventually yield a safer and more effective financial services

[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.

ecosystem for all stakeholders, including community banks and their customers. ICBA's recommendations include or address the following considerations:

- **Acknowledged need to evolve supervisory approach.** Whereas previous iterations of third-party risk guidance focused on generic risks associated with traditional bank vendors (payment processors, check providers, etc), this RFI seems to acknowledge the evolution of third-party risk, now including new business models that present unique risks.
- **Shortcomings with the existing model.** With the advent of this model and the newer breed of bank-fintech relationships, certain shortcomings in the existing regulatory model have become apparent, which unintentionally inhibit innovation and growth, thereby fueling market consolidation.
- **Innovation at the Agencies.** The Agencies, themselves, have the ability to innovate and find novel ways to supervise, identify and monitor marketplace innovations, including:
    1. **Frequently Asked Questions;**
    2. **Supervisory Highlights;**
    3. **'Just in time' reviews;**
    4. **Bank Service Company Act exams; and**
    5. **Shared due diligence and standards-setting organizations**

Acknowledged Need to Evolve Supervisory Approach

Although the Agencies finalized the *Interagency Guidance on Third Party Risk* just 16 months ago,[2] and more recently published the *Guide for Community Banks on Third-Party Risk Management* earlier this year,[3] this RFI is well-timed as it provides an opportunity to continually engage stakeholders. Of all the areas under the Agencies' supervision, bank technology is the least likely to remain static and always benefits from ongoing engagement and discussion with industry.

Though scalable and able to be tailored, depending on the criticality or complexity of the third party and/or the third party's product/service, plenty of opportunities exist for the Agencies to develop more applied Guidance. The Agencies now have an opportunity to provide more granular guidance that is categorized and segmented based on the product or service.

ICBA agrees with CFPB Director Chopra and FDIC Board Member McKernan, who both recently acknowledged that there should be more clarity on existing guidance regarding third-party relationships. As Board Member McKernan rightly pointed out, "[the existing guidance is]…really tailored most to the services that a bank obtains as opposed to work through a service provider, or having a service provider that works on behalf of a bank."[4]

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[2] Interagency Guidance on Third-Party Relationships: Risk Management, 88 Fed. Reg. 37920 (Jun 9, 2023), https://www.federalregister.gov/documents/2023/06/09/2023-12340/interagency-guidance-on-third-party-relationships-risk-management

[3] Third-Party Risk Management: A Guide for Community Banks, May 2024, https://www.occ.gov/news-issuances/news-releases/2024/pub-third-party-risk-management-guide-for-community-banks.pdf

[4] Santos Sanneh, Ebrima, "McKernan and Chopra want clearer bank-fintech guidance," Am Banker (Jul 10, 2024), https://www.americanbanker.com/news/mckernan-and-chopra-want-clearer-bank-fintech-guidance

Policymakers that wish to see innovation develop in a regulated and actively supervised manner must understand that permitting bank-fintech partnerships is the best shot at making responsible innovation a reality. Conversely, if the Agencies continue to lay out stricter parameters for banks that partner with fintechs, it is inevitable that fintechs will go about it on their own, sometimes through the route of establishing a non-federally-insured bank, such as a special purpose depository charter.[5] In such a case, the Agencies will have throttled innovation in the banking sector so much as to completely remove it from the system, redirecting it to an alternative ecosystem that does not have the same consumer protections or prudential supervision.

Governor Bowman has hit on this recognition, stating, "[h]ostility to innovation within the banking system often results in activity migrating outside of the banking system. This is not an elimination of the underlying risk of these activities. They remain in the financial system but are often subject to less transparency and less regulation than the same activities conducted by banks."[6]

<u>Shortcomings of the Existing Framework</u>

While ICBA supports the Agencies' recognition that innovation must be allowed within the banking system, there should first be an assessment of the current system's shortcoming and gaps. In brief, ICBA is concerned that unclear examiner expectations cause retreats from innovation, resulting in banks opting for the perceived safety of partnering with legacy third parties.

> **Unclear examiner expectations.** Most financial institutions – large and small - do not typically have the resources in-house to develop cutting-edge technology, but this is most acutely felt by community banks. For example, according to a 2023 Conference of State Bank Supervisors survey, less than one percent of respondents indicated they do not rely on external providers for digital banking products and services.[7] However, reliance on third parties also invites examiner scrutiny, especially when the third party develops novel technologies.
>
> Community banks continue to voice frustration in navigating a regulatory framework that is designed to be more deliberative and process-oriented, rather than nimble and responsive to innovation. While properly designed and tailored regulations certainly help consumers, overly broad or outmoded regulations create uncertainty and do not protect consumers.
>
> Compliance with third-party guidance and responses to examiner scrutiny have themselves become burdens to partnering with fintechs. To head-off any examiner criticism, community banks will sometimes subject fintechs to a full and thorough dose of due diligence, without regard to criticality, interconnectivity, or other factors that might dictate a less encompassing vetting. Alternatively, community banks feel their examiners scrutinize them less when they partner with legacy core service providers, unintentionally creating an incentive system that prioritizes stasis rather than innovation.

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[5] *See e.g.* Wyoming Division of Banking, https://wyomingbankingdivision.wyo.gov/banks-and-trust-companies/special-purpose-depository-institutions

[6] Speech by Gov. Bowman, "Innovation in the Financial System," delivered at the Salzburg Global Seminar on Financial Technology Innovation, Social Impact, and Regulation: Do We Need New Paradigms?," (Jun 17, 2024), https://www.federalreserve.gov/newsevents/speech/bowman20240617a.htm

[7] Conference of State Bank Supervisors, "Community Banking in the 21st Century: 2020 Research and Policy Conference," available at https://www.csbs.org/system/files/2020-09/cb21publication_2020.pdf

Reverting to perceived safety of legacy providers. While some start-up third parties can truly develop cutting-edge technology that can go toe-to-toe with the largest financial institutions, examiner attention to this technology can make the partnership so daunting as to not justify the risk. More than 40 percent of community bank respondents to a CSBS survey said the expectations of bank supervisors regarding due diligence of a third-party provider to some extent impeded the establishment of new relationships with third parties.[8] Due to this scrutiny, along with the associated costs, it is sometimes easier for banks to partner with legacy third parties that receive less scrutiny, such as core service providers.

However, the upside of partnering with a core service provider – less examiner scrutiny, and arguably, less risk – is offset by the downside limitations. There are only a handful of core service providers, creating an oligopoly market whereby the banks have limited bargaining power when negotiating service agreements. As a 2019 Congressional Research Service report found, "only a few large third-party service providers provide the majority of digital products to the financial industry." The report explains how this limited market eventually leads to higher prices for their services, "which small institutions may be less able to pay than larger institutions."[9]

Not only can this lead to a bank that is captive to the service provider, but it can also drain monetary resources that could be better allocated to other technology providers that might better serve the community bank. Further, many core service providers, themselves, are beholden to legacy technology, making it difficult or impossible for them to develop and offer the latest technological advancements.

Agency Policy, Guidance, and Programs can Address these Shortcomings

The shortcomings and gaps in the existing framework, however, present an opportunity for the Agencies to help usher along a new regulatory paradigm in the financial services ecosystem. The Agencies sit at a critical intersection with the ability to provide insight into the needs and risks unique to banks, fintechs, and customers. Through the following recommended changes to their supervisory philosophy, the Agencies can become quicker to offer insight and expectations, more adept to identify burgeoning risks, better in probing for weaknesses, more frequent and broad in communicating those deficiencies, and collaborative in developing solutions to actively supervise novel risks for the potential benefit of improved services and products::

1. Reinstitute ***Frequently Asked Questions*** **as an addendum** to the Guidance;
2. Periodically **publish *Supervisory Highlights*,** similar to the Consumer Financial Protection Bureau's, focused on sharing key examination findings related to bank-fintech partnerships;
3. Explore the use of **'just in time' reviews, enhanced examination of novel technologies, and supervised use of variables;**
4. Utilize dormant authority provided under the **Bank Service Company Act;** and

[8] Conference of State Bank Supervisors, "Community Banking in the 21st Century: 2020 Research and Policy Conference," available at https://www.csbs.org/system/files/2020-09/cb21publication_2020.pdf
[9] Getter, Darryl, "Technology Service Providers for Banks," Congressional Research Service (Jun 20, 2019), https://crsreports.congress.gov/product/pdf/if/if10935

5. Use economies of scale to more effectively **map and monitor** the complex or critical third-party relationships through the **use of shared due diligence and standard setting organizations**.

1. Reinstitute *Frequently Asked Questions* as an addendum to the TPRM Guidance

ICBA encourages the Agencies to reinstitute Frequently Asked Questions ("FAQs") that were previously part of OCC's Guidance on Third-Party Risk. The FAQs were used as a tool that was more responsive than traditional regulation or guidance. Further, the FAQs provided succinct clarity on concrete examples of how the OCC viewed novel issues unique to third parties.

To improve upon the prior version of FAQs, however, ICBA recommends that the Agencies have a standing list of requested questions on the Agencies' websites, or by seeking FAQ ideas on a periodic basis. The Agencies should provide more issue-specific compliance guidance for novel issues that might not be addressed by existing guidance. Rather than waiting until the guidance is reviewed *en masse* to address novel issues, ICBA recommends that the Agencies seek feedback and weigh-in on novel issues as they present themselves. For example, the FAQs provided insight into OCC's view on artificial intelligence, treatment of data aggregators, alternative data, and other issues that were not even contemplated when the guidance was issued several years prior. A revised and reinstituted FAQs would more rapidly provide the industry with reliable guidance, relevant to more timely issues.

2. Periodically publish *Supervisory Highlights*

FDIC Board Member McKernan recently suggested that even some 'black and white' rules of the road could help provide greater clarity. What Board Member McKernan seemed to imply– and what ICBA supports – is for the Agencies to move away from 'regulation through enforcement,'[10] which unfortunately is one of the few ways that industry can infer what the Agencies expect.

Apart from existing regulations and guidance, the industry looks to enforcement actions on banks with fintech partners as a means to glean wheat the Agencies expect and how the banks failed in meeting those expectations. Enforcement actions can be an important tool in the Agencies' arsenal when telegraphing what banks should be doing when managing their third-party risks.

However, while enforcement actions can be helpful in offering more concrete examples and providing a better understanding of how the regulations and guidance are applied to specific facts, the enforcement orders do not divulge specific information or fact patterns that might risk the confidential nature of bank examinations. As such, enforcement orders have limited utility in helping industry fully understand risks or examiner expectations. The narrative portions of the enforcement actions are vague, leaving uncertainty as to the specific circumstances that led to found deficiencies.

Instead of providing more facts, specificity, and detailed examples in the enforcement orders, ICBA recommends that the Agencies model a future effort on the CFPB's *Supervisory Highlights*. By being published periodically throughout the year, the *Supervisory Highlights* are not tied to any particular bank. There is certain degree of anonymity, which allows the Bureau the room to provide more detail on

[10] Santos Sanneh, Ebrima, "McKernan and Chopra want clearer bank-fintech guidance," Am Banker (Jul 10, 2024), https://www.americanbanker.com/news/mckernan-and-chopra-want-clearer-bank-fintech-guidance

particular facts and circumstances. The *Supervisory Highlights* also hit on themes, trends, and other issues that the Bureau feels is worth raising, often referencing existing law, regulation, or guidance.

While 'regulation through enforcement' is still a pervasive problem, ICBA believes that "Supervisory Highlights on Bank-Fintech Arrangements" will better inform and equip the marketplace to achieve a point where enforcement through regulation is not needed to communicate supervisory expectations.

3. <u>Explore the use of 'just in time' reviews and enhanced supervision of novel technologies</u>

To quickly and efficiently embrace new technology, community banks need to be able to collaborate with fintech firms. One obvious challenge with collaboration is the introduction of new risks requiring aggressive identification and mitigation. In order to both manage and minimize these risks, community banks need to work with partners who are in a strong position to assist in prudent risk management in real time. However, regulatory review should not be a barrier to allowing community banks to innovate at the speed necessary to remain competitive and operate on a level playing field. Instead, ICBA advocates that the Agencies respond to bank and fintech partner requests to provide feedback and assessments of proposed activity so that the industry may have more regulatory certainty when they undertake innovative endeavors.

To varying degrees in the past, each Agency has explored or initiated quasi-regulatory programs that were designed to mitigate the slow-moving realities of the traditional rulemaking process, such as pilot programs, sandboxes, and no-action letter ("NAL") policies. These programs attempt to allow for in-market testing of real world situations, which has the potential to offer valuable information for improving products and providing better value to consumers and other bank customers.

For example, the CFPB issued a NAL to Upstart Network, Inc. in 2020, giving the firm a 36-month period where the Bureau agreed to not bring a supervisory or enforcement action against upstart under ECOA or its Unfair, or Deceptive, or Abusive Acts and Practices Authority.[11] The NAL was conditioned on Upstart's adherence to a Model Risk Assessment Plan, which required the firm to provide the Bureau with model documentation on a periodic basis. Upstart would test their model and/or variables or groups of variables on a periodic basis for adverse impact and predictive accuracy by group, research less discriminatory alternatives ("LDA"), and conduct periodic access-to-credit testing to determine how Upstart's model compares to other credit models in enabling credit access, along with other requirements.

ICBA believes the NAL model, and other similar programs, has promise. Given the seriousness of fair lending violations, many banks remain uncomfortable using certain technology due to the perception that it could make them more at risk. Regulators can increase banks' willingness to use novel technologies by providing incentives to back-test the products and services to ensure there are no equally predictive LDA. Banks would feel more comfortable using technology from a third-party provider that has an NAL if there was a clear framework for how those models are to be tested and monitored.

Indeed, several consumer groups have independently supported programs that would recognize and adopt LDAs. The Consumer Federation of America and Consumer Reports wrote to the Bureau in June of

[11] CFPB, Upstart Network No Action Letter (Nov. 30, 2020), available at: https://files.consumerfinance.gov/f/documents/cfpb_upstart-network-inc_no-action-letter_2020-11.pdf.

this year, requesting that the CFPB issue guidance on how banks could search for LDAs.[12] Soon after, the National Community Reinvestment Coalition and several fintechs collectively wrote to the Bureau in September, also requesting for additional CFPB guidance on how banks could run methodologies that would find LDAs.[13]

Similar to the consumer groups' requests for guidance surrounding LDAs, NALs and other programs hold the promise of providing more certainty to the banks and fintechs that offer the product/service, while simultaneously delivering on a promise of fairer products that cause the least harm for consumers.

As expressed in response to several agencies' innovation initiatives, ICBA supports these regulatory frameworks that allow for the exploration of new technological developments that otherwise might be prohibited or curtailed by existing laws or regulations. These programs are nimbler alternatives to the formal rulemaking process, yet still have transparent components that are the hallmark of traditional rulemaking tools. This appropriately balances the need to rapidly adapt to advances in technology with the need to closely monitor these relationships.

4. <u>Utilize dormant authority provided under the Bank Service Company Act</u>

ICBA recommends that the Agencies explore greater use of their authority under Bank Service Company Act ("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."[14]

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.[15]

Currently, there seems to be a lack of transparency as to which third parties receive direct examination under BSCA and a confusion as to how or if banks are able to receive copies of the examination reports. Additionally, the current BSCA exams appear to be heavily focused on IT and operational risks, leaving room for the Agencies to staff the exam teams with other specialists. Finally, there may be appetite to supervise other third parties beyond significant service providers ("SSP").

Transparency on Significant Service Providers and their Exam Findings

As far as ICBA is aware, the Agencies only use their BSCA authority to directly examine legacy core service providers, as part of their SSP examination program. As part of the Federal Financial

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[12] Chien, Jennifer and Adam Rust, "Consumer groups call on CFPB to protect consumers from discriminatory algorithms used by banks and other financial institutions to make credit decisions," Consumer Reports, (Jun 26, 2024), https://advocacy.consumerreports.org/press_release/consumer-groups-call-on-cfpb-to-protect-consumers-from-discriminatory-algorithms-used-by-banks-and-other-financial-institutions-to-make-credit-decisions/#:~:text=The%20groups%27%20letter%20urges%20the,so%20companies%20follow%20best%20practices
[13] Press Release, "NCRC and Fintechs – Joint Letter on Fair Lending and the Executive Order on AI," NCRC (Sept 30, 2024), https://ncrc.org/ncrc-and-fintechs-joint-letter-on-fair-lending-and-the-executive-order-on-ai/
[14] 12 USC 1867(c)(1).
[15] FFIEC Supervision of Technology Service Providers, Handbook, https://ithandbook.ffiec.gov/it-booklets/supervision-of-technology-service-providers/supervisory-programs/mdps-program

Institutions Examination Council ("FFIEC"), the Agencies directly and jointly examine companies under the Multi-Regional Data Processing Servicers ("MDPS") Program, which includes companies that provide "mission-critical applications for a large number of financial institutions…posing a high degree of systemic risk,"[16] (sometimes referred to as SSPs). It is commonly understood that core service providers are designated as SSPs and receive direct examination from the Agencies. ICBA has learned from our banks that there is general inconsistency and confusion surrounding existing SSPs exams conducted under BSCA authority.

First, some banks are simply unaware that exam findings of their SSPs are even available to them. Other banks might be aware that the exam findings are available to them, but field examiners have said that banks must proactively request the reports. And finally, banks that receive the SSP exam findings report that the information is stale by the time they receive it, in some cases as old as 24 months.

This anecdotal evidence seems to be supported by a recent FDIC Office of the Inspector General ("OIG") report, which found that FDIC does not have any goals or metrics to define and measure the timeliness of the distribution of SSP exams. The report notes that FDIC "does not track or monitor how long it takes to distribute ROEs [report of examination] to financial institutions."[17]

Not only do banks have a general unawareness or confusion surrounding examinations of significant service providers, but so do the bank examiners. According to the OIG report, 52 percent of bank examiners responding to a survey indicated they were not aware of how to obtain or access all service provider information. The examiners' confusion apparently stems from the same underlying cause as the banks': "respondents expressed that it is difficult to identify whether an examination was performed on a relevant service provider due to the lack of a comprehensive list of service provider examinations."[18]

ICBA encourages the Agencies to address the OIG's findings, which would increase the transparency of SSP examinations, as well as increase the utility of the exam findings.

> **Comprehensive list.** First, there does not appear to be a list or database of which SSPs currently undergo examinations from the Agencies. ICBA recommends that the Agencies generate and publish this database, which would be useful for banks and their examiners. Without a knowledge of which SSPs are examined, how could a bank even be aware of an SSP report that is available to request?
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> **Direct distribution.** In the alternative, ICBA recommends that the Agencies should distribute the examination reports to the clients of the SSPs as soon as possible, after

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[16] FFIEC Supervision of Technology Service Providers, Handbook, https://ithandbook.ffiec.gov/it-booklets/supervision-of-technology-service-providers/supervisory-programs/mdps-program

[17] Gibson, Terry L., Memorandum to Doreen R. Eberley, Director, Division of Risk Management Supervision, RE FDIC's Regional Service Provider Examination Program, AEC Memorandum No. 24-01 (Dec 2023), FDIC Office of Inspector General, https://www.fdicoig.gov/sites/default/files/reports/2023-12/AEC%20Memorandum%20No.%2024-01.pdf

[18] Gibson, Terry L., Memorandum to Doreen R. Eberley, Director, Division of Risk Management Supervision, RE FDIC's Regional Service Provider Examination Program, AEC Memorandum No. 24-01 (Dec 2023), FDIC Office of Inspector General, https://www.fdicoig.gov/sites/default/files/reports/2023-12/AEC%20Memorandum%20No.%2024-01.pdf

the report has concluded, on an automatic basis. Although current policy allows clients of SSPs to request reports, it is not certain when the latest copy of the report is available and there might be significant delay between the SSP examination and delivery of those reports.

While it appears that the Agencies attempted to automatically provide bank clients with SSP exam findings through a 2019 pilot program, the effort was eventually scrapped due to erroneous client lists provided by the SSPs.[19] This could be solved by having both the SSP and the financial institution independently identify each other in a client-provider relationship.

ICBA applauds Governor Bowman for championing these suggestions, repeatedly calling for the Agencies to more proactively distribute examination findings of SSPs, as well as "being more transparent about who and what we [the Agencies] evaluate."[20] We hope the Agencies understand the value of these changes.

Develop the talent pool that conducts SSP examinations under BSCA beyond IT specialists

The Agencies have traditionally used BSCA authority to conduct SSP examinations that are focused on critical activities, being heavily focused in IT. The OIG report indicates that FDIC does not have a dedicated SSP examination team and relies on the pool of examiners used for risk management and IT examinations.[21]

ICBA recommends that the Agencies recognize the value of expanding the skillset of examination teams to include consumer protection, accounting, liquidity, and other types of specialists. As some third parties are so interconnected with the majority of banks, it is possible that consumer protection deficits at one third party could impact the ability of thousands of banks to comply with federal regulations. The recent challenges surrounding 'representment of checks' demonstrates the potential usefulness of this model, where there were discrepancies as to whether the core service providers could adequately identify represented checks.[22] Rather than focusing on the end-user banks, it would have been more efficient to identify and remediate this problem through a centralized third party.

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[19] Gibson, Terry L., Memorandum to Doreen R. Eberley, Director, Division of Risk Management Supervision, RE FDIC's Regional Service Provider Examination Program, AEC Memorandum No. 24-01 (Dec 2023), FDIC Office of Inspector General, https://www.fdicoig.gov/sites/default/files/reports/2023-12/AEC%20Memorandum%20No.%2024-01.pdf

[20] See Governor Michelle W. Bowman, "Direction of Supervision: Impact of Payment System Innovation on Community Banks," (Feb. 27, 2020), remarks made at, "Age of Advancement: The Intricacies of a Digital World" 2020 Banking Outlook Conference sponsored by the Federal Reserve Bank of Atlanta, Atlanta, Georgia, available at https://www.federalreserve.gov/newsevents/speech/bowman20200227a.htm

[21] Gibson, Terry L., Memorandum to Doreen R. Eberley, Director, Division of Risk Management Supervision, RE FDIC's Regional Service Provider Examination Program, AEC Memorandum No. 24-01 (Dec 2023), FDIC Office of Inspector General, https://www.fdicoig.gov/sites/default/files/reports/2023-12/AEC%20Memorandum%20No.%2024-01.pdf

[22] *See* ICBA Press Release, https://www.icba.org/newsroom/news-and-articles/2023/09/14/icba-meets-with-occ-on-re-presentment-concerns, where community bank representatives explained the lack of readiness of core service providers to accurately identify and stop fees from being assessed.

BSCA can provide for federal supervision without the need to establish a "federal payments license" or "fintech charter" or similar special charter

Recently, there appears to be an uptick in those calling for a federal payments licensing framework,[23] which seems to be the latest iteration of a concept first raised during the last administration – the special purpose national bank ("SPNB").[24] Similar to how some justified the creation of a SPNB as a means to directly oversee companies that are outside the banking perimeter, recent calls for a federal payment license use the same underlying rationale. The argument essentially amounts to, "*there is a gap in federal supervision of 'x' type of entity, therefore, we need a new law to give us authority to plug that gap*.'

Rather than seek new authority or create a new breed of charters, ICBA recommends that the BSCA already provides the Agencies with the authority to fill that gap and gain a direct line of sight into service providers that pose untenable risk. There is no need to seek legislative changes.

Here, too, Governor Bowman contemplated something similar, reflecting on the fact that the "regulatory burden of thid-party relationships falls heavily on bank." During remarks made at ICBA's Annual Conference in March 2023, Gov. Bowman positing, "it is worth considering whether […] additional parties—like fintechs and other technology companies—should be subject to closer scrutiny for the products and services they provide to banks. If third parties provide products and services to bank customers, it also may be appropriate for these providers to bear greater responsibility for their own products and services, including to ensure that they are provided in a safe and sound manner and in compliance with financial and consumer laws and regulations."[25]

ICBA supports Governor Bowman's sentiment and we would like to see consideration of additional third parties receiving direct examination from the Agencies. In the Agencies risk-mapping exercise (discussed below), it should be determined which category of third parties warrant a direct line of sight into their business practices, rather than use the circuitous route of examining the bank to better understand the third-party fintech.

5. Using economies of scale to more effectively map and monitor the complex or critical third-party relationships through the use of shared due diligence and standards-setting organizations

While using the BSCA authority more broadly would improve the health of the system, ICBA understands that the Agencies might not have the capacity to supervise *all* third parties. Instead, the Agencies would likely need to first map the fintech landscape, next conduct a risk assessment – categorizing and ranking

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[23] OCC's Hsu calls for federal payments licensing | Payments Dive; OCC's Hsu endorses federal standards for money transmission licenses | American Banker; Remarks before the Exchequer Club on the Size, Complexity, and Polarization in Banking, July 17, 2024; Remarks by Under Secretary for Domestic Finance Nellie Liang "Modernizing the Regulatory Framework for Domestic Payments" at the Chicago Payments Symposium, hosted by the Federal Reserve Bank of Chicago | U.S. Department of the Treasury

[24] OCC, "OCC Begins Accepting National Bank Charter Applications from Financial Technology Companies," press release, July 31, 2018, https://www.occ.gov/news-issuances/news-releases/2018/nr-occ-2018-74.html.

[25] Speech by Gov. Bowman, "The Innovation Imperative: Modernizing Traditional Banking," delivered at the Independent Community Bankers of America Live 2023 (Mar 14, 2023), https://www.federalreserve.gov/newsevents/speech/bowman20230314a.htm

the risks proposed, and then utilize certain economies of scale to gain a better view in determining which third parties warrant direct supervision under the BSCA.

Also worth noting, using the BSCA to supervise third parties beyond the SSPs could potentially counteract the oligopoly that has resulted from a few legacy service providers receiving direct supervision.

Use the third-party risk mapping exercise to determine which third parties could benefit from direct examination under BSCA

The Agencies currently have developed several workstreams to map the fintech landscape and to categorize certain fintechs into cohorts based on similar risk profiles and attributes.[26] While this risk mapping exercise should provide better insight into the existing number and type of fintechs currently in existence, ICBA recommends that the results of the mapping exercise be used to determine which fintechs should be directly supervised under BSCA. As discussed above, a compelling case could be made to extend direct supervision over third parties that pose unique risk or are so novel as to require a more direct line of sight into their activities.

Use shared due diligence to help categorize and rank third-party risk

Once the landscape of fintechs is identified, conducting shared due diligence on potential partners would gain economies of scale, allowing banks to pool their resources. This is supported by an idea espoused in a 2021 Federal Reserve Community Bank Advisory Council ("Council") meeting,[27] where due diligence and monitoring of third parties could be standardized and shared. As technology evolves and becomes increasingly complex, the Council explained collaboration among banks could help less mature community banks gain a better understanding of third-party relationships. As the Council rightfully noted, such an initiative would necessitate regulatory support and participation.[28]

Otherwise, the current model of subjecting each third-party to the same or similar due diligence and monitoring requirements is inefficient.[29] Banks are asking third parties a fairly common set of questions that have been asked and answered numerous times by third parties in response to multiple requests for proposals. It is frustrating for the fintechs, and certainly wasteful for the banks. Further, even if the Agencies were to use their BSCA authority to supervise more fintechs, there will never be enough resources to examine *all* fintechs. It will be necessary for the Agencies to leverage and utilize certain economies of scale.

Leveraging Standard Setting Organizations and Certifying Organizations

[26] Speech by Comptroller Hsu, "Safeguarding Trust in Banking: An Update," delivered at the TCH + BPI Annual Conference (Sept 7, 2022), https://www.occ.gov/news-issuances/speeches/2022/pub-speech-2022-106.pdf
[27] Minutes of the Community Depository Institutions Advisory Council and the Board of Governors, April 1, 2021, available at https://www.federalreserve.gov/aboutthefed/files/CDIAC-meeting-20210401.pdf.
[28] Minutes of the Community Depository Institutions Advisory Council and the Board of Governors, April 1, 2021, available at https://www.federalreserve.gov/aboutthefed/files/CDIAC-meeting-20210401.pdf.
[29] Speech by Gov. Bowman, "Innovation in the Financial System," delivered at the Salzburg Global Seminar on Financial Technology Innovation, Social Impact, and Regulation: Do We Need New Paradigms?," (Jun 17, 2024), https://www.federalreserve.gov/newsevents/speech/bowman20240617a.htm

A natural extension of shared diligence and monitoring would be the creation and utilization of a standards-setting organization ("SSO"), which is a concept first floated by the FDIC in 2020. The Agencies should already be familiar with SSOs and certifying organizations ("CO") by looking to other areas in banking that utilize SSOs. For example, every bank examiner is familiar with, and depends upon, the Federal Accounting Standards Board ("FASB"), which maintains and oversees the well-known Generally Accepted Accounting Principles ("GAAP") standards, which are explicitly referenced and required in many banking regulations. Recognizing the value of standards and SSOs, the federal banking agencies adopted GAAP as the reporting basis for the Call Report in March 1997. Additionally, the Securities and Exchange Commission has designated GAAP as the designated accounting standard for public companies.[30]

Closer to the fintech space, and just as well known and relied upon as GAAP standards, is reporting requirements associated with audits and/or certifications, such as a System and Organization Control ("SOC") type 1 and type 2 audits. Another more recently adopted standards framework is being developed through the CFPB's 1033 rule. As Director Chopra recently acknowledged when discussing how a SSO would be a part of the final rule:

> "We all probably recognize the importance of standard-setting. Electronics sold in the U.S. have a common set of plugs that fit into outlets installed in our homes and offices. Motor vehicles sold in the U.S. are designed to drive on the right side of the road. **Standards can help create a common understanding for engineers and designers to build products and offerings**. (emphasis added).[31]

Just as the creation of FASB, the adoption of GAAP standards, and SOC reports helped achieve uniformity, commonality, and an assurance that expectations have been met, the creation of a fintech SSO could greatly enhance and address the common inhibitors to bank-fintech partnerships.

The clear benefit of this model would be a shorter 'time-to-market' for fintechs. For example, a fintech that recently participated in ICBA's ThinkTECH Accelerator has explained that undergoing due diligence and initial vetting by potential bank partners is taking 10 months (and counting), whereas finalizing partnerships with non-banks has taken as little as 10 days. Once the initial due diligence requirements are met, though, fintechs have reported that the process is much easier to manage as an on-going process.

In an ideal world, certification of compliance with SSO standards would reduce the on-boarding by several months. So long as regulatory agencies uphold the validity of certificates and put weight in their assessments, SSOs and certifications would make it easier to get new technologies through a bank's internal approval process.

A critical factor with the certification would be the acceptance of the certification as a form of approval by regulators. If regulators do not accept the certificate, or if examiners add additional

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[30] About the FASB, available at https://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176154526495#:~:text=Established%20in%201973%2C%20the%20Financial,profit%20organizations%20that%20follow%20Generally

[31] Speech by Director Chopra, "Prepared Remarks of CFPB Director Rohit Chopra at the Financial Data Exchange Global Summit," (Mar 13, 2024) https://www.consumerfinance.gov/about-us/newsroom/prepared-remarks-of-cfpb-director-rohit-chopra-at-the-financial-data-exchange-global-summit/

due diligence measures because the third party is not certified, the creation of the SSO and certification program would be a step backward and increase burden without providing any benefit. For this program to work effectively, examiners must rely on the certification as evidence of compliance with agreed-upon standards.

A SSO model might also help better place the liability for missteps, bad practices, or simple negligence that result in consumer harm. For example, if a CO certifies a third party as meeting certain agreed upon standards, only for the bank to subsequently find that the certification review was flawed or negligent, then the CO should presumably share in the liability that stems from the underlying harm. There is more skin in the game in preventing harm, and in cases where there is, in making the aggrieved parties whole.

The standards-based approach could be very effective even in rapidly developing areas. If the SSO places responsibility upon the vendor to provide client banks with updates if material changes occur, then the community banks and regulators would be more informed and in better positions to develop responses to those changes. The SSO or CO could serve as a central clearinghouse that receives timely information from certified third parties and transmits that information to all interested parties, including the client banks and regulators.

For example, rather than passively waiting for an annual review or periodic assessment of a third-party's credit modeling, the third-party could actively update the SSO every time it changes its underwriting model or adopts new information upon which it makes decisions. The SSO would keep a log of these changes and notify the client bank or regulators based on the desired preference. Some banks might want to be notified every time a change to the model is made, whereas other banks might merely want to review the change log on a quarterly basis or only when a material change occurs. ICBA is aware of several groups that have initiated the exploration of SSOs and we encourage the Agencies to work be engaged in the process.[32]

Counterbalancing the bargaining power of third-party oligopolies

Apart from leveraging SSOs to map out the existing risk posed by third parties, they could also be used to recalibrate the asymmetries between community banks and certain fintech providers. For example, some community banks have claimed that some legacy third-party service providers are so large that community banks do not have sufficient bargaining power to receive answers or documents in response to basic due diligence questions and requests. If enough smaller community banks collaborate, shared diligence material, and utilize the services of an SSO, there likely would be enough bargaining power in the aggregate to access that information.

On the opposite end of the spectrum, SSOs can alleviate problems typically present with small or early stage fintechs. In contrast to large fintechs that have the requested information but simply will not share it, these early-stage fintechs would share the requested information but for the fact that they do not have it prepared. The shared diligence and SSO model could solve for this by acting as a shared platform on behalf of multiple banks, working with the early-stage fintech to develop the information sufficient for the SSO's certification. The banks benefit from the efficiencies of shared services, and the early-stage fintechs benefit from having the SSO's expert assistance in compiling the information.

[32] *See e.g.*, Coalition for Financial Ecosystem Standards (CFES), available at https://fsvector.com/cfes/, an industry-led organization to establish operating rules that would promote the safety and soundness for non-banks participating in financial services.

Conclusion

ICBA supports and encourages community banks as they innovate, both organically and through partnerships with other innovators, such as fintech companies. Partnering with fintech companies can offer valuable relationships that help community banks enhance the customer experience. ICBA has long advocated that through partnerships with fintechs, community banks can forge deeper relationships with their customers, while also reducing costs and increasing access for all small businesses and consumers

The ability for community banks to continually innovate and offer the latest products and services to consumers is essential to relationship banking. And in turn, it is essential for the Agencies to continually assess and improve their regulatory framework. ICBA sincerely appreciates the Agencies willingness to seek ideas and receive comment through this RFI. We are optimistic that the feedback provided will result in further dialogue and improvements to the community bank-fintech ecosystem. 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/

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