

Consumer Finance Monitor (Season 5, Episode 41): Use of the FDIC Name and Logo: Proceed With Caution

Speakers: Alan Kaplinsky, Mindy Harris, and Ron Vaske

Alan Kaplinsky:

Welcome to the award-winning Consumer Finance Monitor podcast where we explore important new developments in the world of consumer financial services and what they mean for your business, your customers, and the industry.

Our weekly podcast show is sponsored by the Consumer Financial Services Group at Ballard Spahr. I'm your host, Alan Kaplinsky. I'm the former Practice Group Leader for 25 years, and now Senior Counsel of the Consumer Financial Services Group at Ballard Spahr. And I'll be moderating today's program.

For those of you who want even more information, don't forget about our blog, also going by the name of Consumer Finance Monitor. We've hosted our blog since 2011, so there's a lot of relevant industry content there, including content about the topic that we are about to discuss today. We also regularly host webinars on subjects of interest to those in the industry. So if you want to subscribe to our blog or to get on the list to receive invites for our webinars, just visit us at ballardspahr.com. And if you like our podcast, let us know about it. Leave us a review on whatever platform you might be using today, whether it's Apple, Spotify, Google, or any other platform. Also, please let us know if you have any ideas for other topics that we should consider covering or any speakers that we should consider inviting as guests on our show.

So let me tell you about our show today and what we're going to focus on, and then I will introduce our guests and we will get going. So very recently, the FDIC issued a final rule to address regulatory concerns as to whether non-bank entities may be inappropriately representing that they are banks or that they have federal deposit insurance, insurance by the FDIC. The CFPB also has weighed in on this topic, including with an enforcement memorandum asserting that misrepresentations about FDIC insurance would be a material violation of the Consumer Financial Protection Act, which of course is part of Dodd-Frank.

Ensuing investigations and enforcement actions by the FDIC focused on companies that allegedly stated or suggested or implied that certain crypto-related products are FDIC insured. However, the FDIC rule and the CFPB advisories that have been issued include broad language covering misuse of the FDIC's name or logo and false or misleading representations about deposit insurance by any person or entity as to any product.

I also want to mention that we have been following this issue at the FDIC and at the CFPB for quite some time. And we did a podcast show last year which addressed itself to the proposed FDIC regulations. And now we have actually final regulation of the FDIC, which we're going to cover.

So let me introduce our guests today, and they are both lawyers that are with the Consumer Financial Services Group at Ballard Spahr. First of all, Mindy Harris. Mindy Harris is of counsel in our Denver office and advises clients on a myriad of federal and state banking and consumer financial regulations. Before joining Ballard Spahr in 2020, Mindy was in-house counsel for decades at FDIC-insured financial institutions, including a stint as general counsel at Nordstrom Bank, and in senior in-house positions at U.S. Bank and its predecessors.

In those roles, Mindy regularly advised the operations, marketing, strategic, and governance functions of her client organizations on legal compliance and risk management in connection with regulations of the FDIC, Federal Reserve Board, the Comptroller of the Currency and the CFPB, and interacted with regulators in the course of their supervisory activities. And Mindy, now that she is part of our Consumer Financial Services Group, has continued to advise our clients on the same subject.

So Mindy, a very warm welcome to you.

Mindy Harris:

Thank you, Alan. I'm looking forward to today's podcast.

Alan Kaplinsky:

Okay. And now let me introduce another guest on today's program. And that is Ron Vaske. Ron co-leads the firm's Fintech and Payments Industry Team. He has helped clients develop innovative products and services for more than 25 years, including payment and deposit products that promote and rely on pass-through FDIC insurance coverage. A substantial part of Ron's practice is related to bank fintech joint ventures that are designed to leverage the bank's authority and FDIC insurance through the fintech's technology. These relationships often involve cryptocurrency products provided by the fintech and fiat currency deposit and payment products provided by the bank. His clients include banks, fintech companies, payment facilitators, and companies that provide banking as a service.

So Ron, a very warm welcome to you as well.

Ron Vaske:

Thank you, Alan. Very pleased to be here.

Alan Kaplinsky:

Terrific. So I have a lot of questions for each of you. And so let's get into it. First of all, question for you, Mindy. What can you tell us about this FDIC final rule? It's entitled False Advertising, Misrepresentation of Insured Status, and Misuse of the FDIC's Name or Logo. It was issued on May 17th of this year and published in the Federal Register on June 2nd.

Mindy Harris:

That's right. Last May, the FDIC issued its final rule addressing false advertising, misrepresentation of insured status, and misuse of the FDIC name or logo. And as you said, it was published in the Federal Register June 2nd and was effective July 5, 2022.

There were very few differences between the final rule and the proposed rule that was issued in May of 2021. So I'm going to talk about the final rule in general. The rule expands the scope of the previously existing regulation on FDIC advertising and use of the FDIC logo to talk about not only advertisement of FDIC membership, but also to go into more detail about prohibitions against engaging in false advertising or making misrepresentations about deposit insurance. So the new rule starts out by changing the title of the reg, which for those who are taking notes is at 12 CFR Part 328, to advertisement of membership, false advertising, misrepresentation of insured status, and misuse of the name and logo.

Now, the previously existing official sign and advertising rules are preserved, but they're re-designated as Subpart A. And this is important as we'll see later. And they're now entitled, Subpart is entitled Advertisement of Membership. New Subpart B added by the new rule implements Section 18(a)(4) of the Federal Deposit Insurance Act. And the FDIC explained it didn't really have to issue a rule. But the policy objectives to be served by the proposed rule are these, and this is detailed in the supplementary information that went along with the rule, while the existing law, Federal Deposit Insurance Act, prohibits any person from engaging in false advertising by misusing the name or logo of the FDIC or making knowing misrepresentations about existence or extent of deposit insurance. And it's also a federal crime to misuse the FDIC name or make false representations about deposit insurance.

The FDIC previously had not exercised its rulemaking authority under the FDIA. However, the FDIC in both the proposed rule and the final rule stated it's recently observed an increasing number of instances where financial service providers or other entities or individuals have misused the FDIC's name or logo or made false or misleading representations that would suggest to the public that these products are FDIC insured. And the FDIC is concerned that the consumers of this information are not experts. And so it's very important that they not be misled into thinking there's insurance coverage.

So for that reason, the FDIC proposed and then adopted the new rule to clarify the procedures the FDIC will follow to identify, investigate, and take formal and informal action to address these violations.

Alan Kaplinsky:

Mindy, just to clarify things here. I mean, FDIC insurance has existed, it was part of the New Deal, I think, of FDR. I mean, we really go back a long way with it. And this regulation just got issued this year. But I am assuming that it's always been unlawful to use the logo or the name of the FDIC unless you are a banking institution that offers deposits that are insured by the FDIC. So there's no change in the sense that until this regulation was issued, you could use the FDIC name and logo willy-nilly.

Mindy Harris:

That's absolutely right. You couldn't just go ahead and use it. But the FDIC gave examples. I think first of all, I think they wanted to give a warning shot across the bow and draw attention to the issue. Second of all, they wanted to set out the procedures they're going to use. And third, as you will see as Ron and I will talk about, they added some definitions that really put a very fine point on what you can and can't do.

So for example, the new rule adds several new defined terms, and we'll talk about them in more detail later, but also states the prohibition in broad terms. No person may knowingly represent or imply that any "uninsured financial product," a new defined term that we'll talk about later, is insured or guaranteed by the FDIC by using FDIC-associated terms, another defined term, as part of a business name. And by the way, they're also alert to using FDIC-related terms on your website name or your URL. But they don't want you using those terms if in fact you're not a bank or the product that you're talking about is not insured. And then they also say explicitly, and this is what the statute says, no person may knowingly make false or misleading representations about deposit insurance.

So they tell you that they're borrowing from the FTC in a lot of what they've done in the proposed rule. And it's interesting, they are looking to the FTC standards governing deception under Section 5 of the FTC Act to inform what the FDIC thinks constitutes a misrepresentation. And interestingly, the FDIC added a definition of the term consumer to this reg to include not only individuals, but also all current or potential depositors, including not only natural persons but organizations, corporate entities, and governmental bodies. So anybody who's a depositor is a consumer. A little bit counterintuitive there for those of us who deal in consumer regulations, but that's a consumer for purposes of this new rule.

Alan Kaplinsky:

Yeah. So I understand, Mindy, that on the very same day that the FDIC issued its final rule, the CFPB, of course, never wanting to be left behind, they weighed in on this same issue that you've been talking about. Can you tell us what did the CFPB have to say? And are the CFPB and the FDIC in sync with respect to their thinking here?

Mindy Harris:

That's really an interesting point, Alan. You're right, the same day that the FDIC issued the final rule, the CFPB came out with a press release, a statement from Director Rohit Chopra supporting the FDIC rule and a Consumer Financial Protection circular establishing an enforcement position. And this circular stated the CFPB's enforcement position that covered persons or service providers likely violate the Consumer Financial Protection Act's prohibition on deception if they misuse the name or logo of the FDIC or engage in false advertising or make misrepresentations about deposit insurance regardless of whether such conduct is engaged in knowingly, including the misrepresentation of insured status.

So as evidenced by these statements, when it comes to consumers as defined by the CFPB, the Consumer Financial Protection Act, the CFPB is prepared to pursue misrepresentations about deposit insurance as UDAP violations under the CFPB, and as they have made crystal clear, regardless of whether or not the misrepresentation is done knowingly. In contrast to the FDIC's approach, at least as reflected in the FDIC rule, which aligns with the language of the FDIA that prohibits knowing misrepresentations.

Alan Kaplinsky:

Right. Right. So after issuing its final rule, and I want to address this question to you, Ron, the FDIC followed up quickly by issuing advisory guidance to FDIC-insured banks and by pursuing investigations and enforcement actions against a number of non-bank fintechs, in particular those involved in offering crypto-related products. What can you tell us about that, Ron?

Ron Vaske:

Yeah, Alan, I'm not sure if the FDIC had in mind in 2021 when it first proposed the rule if it was thinking about crypto in particular, but certainly events that occurred in 2022 over the summer in what some are calling the crypto winter probably raised the stakes and made it a bigger priority to get that rule finalized.

For example, it's reported that there's about \$2 trillion in market value lost in crypto assets during 2022. Crypto companies were under stress. Some were going into bankruptcy. Some were halting trading. Customers couldn't get their money out. Social media blew up with all kinds of talk about whether or not these deposits, whether or not their money is FDIC insured. A lot of things on social media were just not true. Allegedly, things that even the crypto companies were saying on social media were at least false or misleading, allegedly.

So it's probably not a surprise that the rule was finalized early this year. And it's not at all a surprise that it was followed up quickly by an advisory to banks that, well, all banks, but it was really targeted to banks that have any kind of relationship with crypto companies. It really told the banks the onus is on you. Take a look at all of your crypto relationships and do a deep dive. Make sure that everything that they're saying about FDIC insurance is true, that it's not misleading. Make sure that when they talk about when it applies, that it's true and not misleading.

For example, it applies when a bank fails. It doesn't have anything to do with when a crypto company fails. And then talk about what deposits it applies to. And that being bank deposits. It doesn't apply to crypto. It doesn't apply to any other assets. The rule here and the advisory, the advisory is targeted on crypto, but the rule really applies to far more than that and you can analogize it, the advisory to any kind of product that you might be in the market with.

And then talking about the enforcement you mentioned. There was first an enforcement action against Voyager. Voyager declared bankruptcy this summer, and shortly after that the FDIC issued a cease and desist order on August 5th ordering...

Alan Kaplinsky:

Could you tell us, Ron, what was Voyager's business?

Ron Vaske:

Voyager was a crypto exchange, so it was involved in exchanging crypto and lending...

Alan Kaplinsky:

Into dollars or dollars into crypto?

Ron Vaske:

Yeah. I mean, so different forms of crypto, Bitcoin, any other USDC in the forms of crypto, it was involved in the exchange, as well as then liquidating crypto into fiat currency, U.S. dollars so that customers could withdraw their funds. And so there were significant amounts of U.S. dollars, fiat currency that were held by Voyager in connection with their crypto accounts.

Voyager was the first to receive a cease and desist order from the FDIC. That was on August 5th. There were allegedly misleading statements made by Voyager about the extent of coverage that would apply, the pass-through coverage for FDIC insurance. And then it was followed up couple of weeks later with five others that were all issued on the same day. Similar facts, the FDIC alleges false and misleading statements made by these crypto companies, cryptonews.com, cryptosec.info, smartasset.com, FTXUS, and fdicrypto.com.

Alan Kaplinsky:

So in other words, just to put it in layman's terms, I take it what Voyager was doing was representing people who wanted to do business with it, that they need not worry about the safety of whatever they were exchanging because there was FDIC insurance, and so that the consumers, I guess some of them, maybe a lot of them thought they were dealing really with a bank or it was the equivalent of a bank.

Ron Vaske:

That's the allegation. I don't know that Voyager necessarily said anything quite like that. The allegation is that in context when we're looking at all of the statements surrounding the FDIC coverage, and they're certainly, most of these crypto exchanges, holding U.S. dollars on behalf of their customers, most of the time those are eligible for pass-through FDIC coverage. And so it is true that there's some FDIC insurance coverage in those cases.

I think what the FDIC has focused on was the extent of that coverage and does your representation give the net impression that that coverage goes beyond just the U.S. dollars that are held in the account and covers actually crypto assets and does it cover things like the failure of the crypto company. Voyager's bankruptcy really brought that to attention, that it didn't cover anything with respect to Voyager's bankruptcy. Only if the depository bank was insolvent would FDIC insurance come into play.

Alan Kaplinsky:

I got it. So the FDIC also issued a fact sheet on this topic. Am I right, Ron?

Ron Vaske:

Yeah, they did, about the same time that they issued the enforcement actions against the five crypto companies. Looking at all of the inaccuracies and things that were going on, especially in social media and out on the internet about the extent to which FDIC coverage applies, issued a fact sheet that's targeted to consumers to tell them this is when it applies and when it does not and trying to give consumers additional information about that.

So that was the FDIC's reaction. And obviously, it's an ongoing issue. And we'll probably see more action by the FDIC and probably the other agencies as well, in particular the CFPB.

Alan Kaplinsky:

Yeah. Sure. Let me just ask a technical question. So the FDIC issues a cease and desist order to these crypto exchanges or crypto-related companies and they don't fine them, they just tell them stop doing what you're doing and if you stop doing that, you're off the hook. Am I right? Do they have a bigger hammer that they can hold over them?

Ron Vaske:

They would. I don't think we've seen them exercise any authority beyond just telling them to stop at this point.

Alan Kaplinsky:

But they could. If they wanted to, they could get tougher. And of course, we know what the CFPB can do. Right? They got a full arsenal of all kinds of weapons that certainly no company would want to go to war with the CFPB over something like this.

So let's talk about some takeaways from what both you and Mindy have so well explained to our audience today. So I want to talk about the extent to which an FDIC-insured bank or a fintech that's in a partnership with a bank, the extent to which they can still use FDIC insured or the FDIC name or logo. And let me go back to you, Mindy, on that one.

Mindy Harris:

Yes, Alan. We think that before the new rule and after the issuance of the new rule, it's appropriate to refer to the bank, assuming it is in fact an FDIC-insured financial institution, as a Member FDIC. Now, of course, the fintech should not indicate that it is FDIC insured. But if you are, for example, take the most pure case, the bank has a credit card advertisement or the fintech is advertising a credit product and they say the credit card is issued by ABC Bank, Member FDIC, if that's true, that was permitted under the previous rule, and we think it's still permitted under the new rule.

Just a brief high-level explanation of that. When it restated and updated the definition of non-deposit product in the now re-designated Subpart A of the rule, the FDIC preserved the previously existing language that said, "For purposes of this definition, a credit product is not a non-deposit product, continuing the exception of credit products from the prohibition against using the FDIC official advertising statement in an advertisement relating solely to non-deposit products." There's some double negatives there. But we think this means this section of the regulation reasonably is read to continue to permit usage of the official advertising statement in credit product advertisements.

Now, Subpart B of the new rule, as I said, added a definition. First, it defines non-deposit product to have the same meaning set forth in Subpart A of the same rule that I just talked about. The new definition of uninsured financial product means any non-deposit product, hybrid product, investment security obligation, certificate share, or financial product other than an insured deposit. Since the specific definition of non-deposit product carves out credit products, we think this means credit products also are carved out that is not included in the definition of uninsured financial product.

Alan Kaplinsky:

Okay. So Ron, we did a blog on August 23rd on our consumerfinancemonitor.com. We said this was a report on what had happened with the FDIC going after about a half dozen or so crypto companies. We said that this time of volatility in the crypto market, we expect similar actions will be taken by the FDIC against other crypto companies that make similar representations to those that were the subject of the recent cease and desist letters.

So what is the main takeaway? I know you do a lot of work for fintech companies and some of them are involved in offering crypto. And so what are you advising your clients they should be doing right now, Ron?

Ron Vaske:

Well, I'm advising my clients, in particular to the bank clients that any relationship they have, a lot of the focus on this has been related to crypto companies, but it's not exclusive to crypto companies, any relationship that they might have that involves pass-through FDIC insurance, that's potentially a risky area for this because it's where things can get misunderstood.

Alan Kaplinsky:

Give our a listeners a definition of what you mean by pass-through insurance. If I go into a bank, I walk into Citibank or Chase and I want to open up a deposit account and I give them \$1,000 to put into a CD. It's insured, I think up to 250,000. That's not pass-through insurance. That's direct insurance. What would be pass through?

Ron Vaske:

That's right. So an example of pass-through insurance coverage is like a crypto company where the customer sends currency, fiat currency, U.S. dollars into the crypto company that's going to be invested then or used to purchase a crypto asset. Some other examples, similarly, a brokerage account where the same thing happens. The customer sends in fiat currency then to invest in securities, mutual funds and the like. And then when those are liquidated, just like when a crypto asset is liquidated, goes back into that account. That's not an account typically of the bank. It's an account of the crypto company, of the investment company, whatever.

And so it qualifies, assuming that certain conditions are met, it qualifies for pass-through FDIC insurance coverage. So if that company is holding those funds at an insured bank, it maintains the records of whose money, who the beneficial owners are and how much they are entitled to, their share of that pooled deposit account and some other technicalities on how it's set up, that then those deposits pass through, the insurance passes through up to \$250,000 in each bank for those.

Alan Kaplinsky:

For each customer in the pooled account. It's one account, but the crypto company may have 5,000 customers. And it's all pooled together. So there's a lot more than 250,000 in that account. But if meticulous records are maintained so that you know how much each of the customers has deposited, then you have the full insurance for each one.

Ron Vaske:

That's right. And so oftentimes that account will be titled in the name of the custodian, the crypto company, for example. And so if it were just an account of the crypto company, it would be entitled to FDIC coverage in the amount of \$250,000, whereas with the pass-through each of the beneficial owners gets the benefit of that coverage.

Alan Kaplinsky:

So you were saying before I interrupted you, to make sure we got this, I want to make sure our listeners understood what you meant by pass-through insurance. But I guess what you were about to say is that it's really important if you're a bank that you take a close look at the pass-through relationships that you have.

Ron Vaske:

Yeah. And that would be, like I said, anything, a title company customer, for example, maybe promoting the fact that their funds that are held in an escrow are subject to pass-through coverage. All of those kinds of relationships you need to think about and do a deep-dive analysis on them and look at what are they saying about the coverage, about FDIC coverage.

One thing also that you can slip up on I think is that the coverage, the pass-through coverage only applies to deposits. So that means the money has to actually be in the bank. If, for example, the brokerage, the crypto company, the escrow company, whomever, doesn't put the money there, they're engaged in fraud, they take the money, they use it for other purposes, there's no pass-through coverage for that. So it has to actually be a deposit. And so be very focused on what they're saying and how they're saying it to make sure that customers wouldn't misunderstand that.

Alan Kaplinsky:

And what does this tell us about risk management and governance considerations?

Ron Vaske:

You need to have controls in place. I think you need to be watching social media even to look for things that might be inaccurate, misleading that are being said on social media. Watch all of your customers, if you're the bank, all of your customers, anything that they're promoting regarding the deposit, regarding FDIC insurance coverage, that you're on top of that. So you've got to be constantly monitoring what's going on, what's being communicated. And then have controls in place that your agreement with those customers allows you to take action if there is some sort of false or misleading representation, that you would have some authority to deal with that.

Alan Kaplinsky:

Okay. What about some other action items? I mean, I assume if you're a bank or a fintech, regardless you have to stay on top of regulatory developments such as what happened at the FDIC and the CFPB. You got to take a close look at various planned uses of technology, I guess, right? What would that cover?

Ron Vaske:

Well, I think what it would cover is looking at different kinds of things that develop, as technology develops and where could there be an application that would be relevant to FDIC coverage or depository fiat currency, any kind of application where FDIC insurance would come into play.

Alan Kaplinsky:

And I guess you have to look thoroughly at all the advertisements that are being used and the promotional material and red flag anytime you see FDIC-insured bank and take a close look at that to make sure that it's accurate, right?

Mindy Harris:

Yeah. That's right, Alan. The consumer's perspective has to always be kept front and center. A lot of times both banks and their partners that are very used to operating in this space believe that minimal statements are just fine. And you can't overemphasize, you want to make sure that you're absolutely crystal clear who's the Member FDIC. If you have to make it more prominent, if you have to make it more proximate to the reference of the name, take into consideration that the consumer's not an expert and you have to be absolutely clear. It might be perceived as overkill by those who like streamlined marketing pieces. But in this instance and in this environment, we're going to advise to err on the side of caution.

Alan Kaplinsky:

Yeah. And I guess you got to take a look at all your policies and procedures and make sure that they accurately reflect this FDIC regulation. Right? You certainly would want to do that. And you got to, as part of your review, you've got to take, well, you called it a deep dive, Ron, but you got to look at everything, websites, marketing material, customer agreements, any and all documents, et cetera.

Ron Vaske:

And I would say then make sure when you do that, you also document that you've done it so that when you're examined by the CFPB bank examiners or whomever, that you can demonstrate that you are on top of this.

Alan Kaplinsky:

Okay. Well, we're drawing to the end of our program today, but before we say our goodbyes, I'm wondering if either of you have anything more to add that we haven't already addressed.

Mindy Harris:

Well, I would like to add that Ron wrote a great blog on the topic that you just asked about. It's on our Consumer Finance Monitor blog called FDIC Issues Advisory on Deposit Insurance and Crypto Assets. And it was issued August 4th. So if anybody needs a recap, a little more detail in writing, that's where it is. And that's the information that Ron provided. I thought it was great.

Alan Kaplinsky:

Okay. Ron, how about you? Do you want to have the last word?

Ron Vaske:

I guess the only thing that I'd like to leave everyone with is in looking at this stuff, look at the net impression that it makes. Don't look at individual specific statements, but think about it holistically.

Alan Kaplinsky:

Well, and I guess don't look at it so much as a lawyer, but look at it as a consumer, a lay person who's looking at the reference to FDIC insured or Member FDIC because that's how the regulators will look at it. Right?

Ron Vaske:

Absolutely. And whether it fits the technical definition of deceptive under UDAP principles or not, if it seems deceptive or if it seems confusing, you're going to have to justify that.

Alan Kaplinsky:

Well, we have drawn to the end of our program today. And first, I want to thank you, Ron, and you, Mindy, for participating in today's program and enlightening our audience about this important topic.

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