

SPECIAL ALERT: OCC TAKES THE NEXT STEP TOWARD A FINTECH NATIONAL BANK CHARTER

On December 2, 2016, the Office of the Comptroller of the Currency (“OCC”) [announced](#) its plans to move forward with developing a special purpose national bank charter for financial technology (“fintech”) companies. Accompanying the Comptroller of the Currency, Thomas J. Curry’s announcement, the OCC published a [white paper](#) that describes the OCC’s authority to grant national bank charters to fintech companies and outlines minimum supervisory standards for successful fintech bank applicants.¹ These standards include capital and liquidity standards, risk management requirements, enhanced disclosure requirements, and resolution plans.

Over the past several months, the OCC has taken a series of carefully calculated steps to position itself as a leading regulator of fintech companies and this proposal from the OCC reflects the culmination of those efforts. The fintech industry interest in some form of federal charter has increased as state regulatory agencies have taken increasingly aggressive approaches on the need for licensing for fintech companies that participate in bank outsource relationships to originate loans.

In August 2015, Comptroller Curry announced the OCC’s intent to assemble a team of policy experts, examiners, attorneys and other agency staff that would research innovative developments in the financial services industry. In March 2016, the OCC released a [white paper](#) summarizing its initial research and detailing its plans for guiding the development of responsible financial innovation. Months later, in September 2016, the OCC issued a [notice of proposed rulemaking](#) clarifying the framework and process for receiverships of national banks without deposits insured by the Federal Deposit Insurance Corporation (“FDIC”). That proposal would apply to all nondepository national banks, including those with special purpose national bank charters. In the OCC’s more recent white paper, it detailed its plans to implement a responsible innovation framework and announced its plan to establish an Office of Innovation, a dedicated, central point of contact for fintech companies as well as requests and information related to innovation.²

Taken together, these initiatives set the stage for the OCC’s plans to provide the ability for fintech companies to operate under a single national bank charter, as opposed to a patchwork of state licenses to conduct their activities.

¹ Office of the Comptroller of the Currency, [Exploring Special Purpose National Bank Charters for Fintech Companies](https://www.occ.gov/topics/bank-operations/innovation/special-purpose-national-bank-charters-for-fintech.pdf) (Dec. 2016), <https://www.occ.gov/topics/bank-operations/innovation/special-purpose-national-bank-charters-for-fintech.pdf> [“December White Paper”].

² Office of the Comptroller of the Currency, Recommendations and Decisions for Implementing a Responsible Innovation Framework (Oct. 2016), <https://www.occ.gov/topics/bank-operations/innovation/recommendations-decisions-for-implementing-a-responsible-innovation-framework.pdf>.

The OCC's newest white paper provides important insights about the agency's chartering process and supervisory expectations for fintech companies. However, the proposal is far from final, as it prompts nearly as many questions as it answers. The OCC is attempting to help fintech companies simplify their operations through comprehensive federal supervision and preemption from state usury caps. However, fintech companies and their investors will need to closely evaluate whether these benefits are offset by becoming subject to the additional regulatory regimes, restrictions on activities, not permissible under the National Bank Act and other applicable law, and heightened supervisory expectations that may be tied to the OCC's bank charter.

Comments on the OCC's white paper, which includes 13 discrete questions for consideration, are due January 15, 2017.

OCC'S CHARTERING AUTHORITY

The OCC asserts that it may rely on the same authority under the National Bank Act that it has historically relied on to charter trust banks and credit card banks.³ Under this authority, the OCC may grant a "special purpose national bank charter" to an entity that engages in fiduciary activities or at least one of the following three core banking functions: receiving deposits, paying checks, or lending money.

Scope

The OCC will take an expansive, case-by-case view when determining whether a fintech company engages in a core banking function in an effort to include technology-based innovations in financial services. While it is apparent that this definition would encompass marketplace lenders, it is unclear how the OCC will classify fintech companies under the "paying checks" or "receiving deposits" categories. The industry will need clarity on whether fintech companies engaging in various forms of payment processing, prepaid payments, remittances, virtual currencies, blockchain and other forms of ledger technology could also apply to become a bank. For instance, as written, the proposal seems to exclude "online lending exchanges" which connect borrowers to lenders, but do not themselves originate any loans.

The OCC states that fintech companies operating under its bank charter "may engage only in activities that are permissible for national banks." Historically, the OCC has interpreted the powers of national banks expansively by broadening the meaning of what constitutes the "business of banking" or what is considered incidental to the business of banking.

The OCC has been proactive in messaging its recognition that the regulatory regime should expand to the fintech arena. However, given the ambiguities in the recent proposal, it is currently unclear which fintech companies will be eligible to—and which will choose to—apply to become a national bank. However, based on the nature of the OCC's baseline supervisory expectations (including minimum capital and liquidity requirements), it appears that the ability to obtain a fintech bank charter—at least in the near term—would be reserved for mature fintech companies with more established business models and

³ The OCC also has used this authority to charter bankers' banks, community development banks, and cash management banks.

compliance management programs relative to less-developed start-ups and emerging entrants in this space.

PROPOSED REGULATORY LANDSCAPE

On December 2, the Comptroller stated that it is in the public interest to allow companies that offer banking products and services the choice to become a national bank if they choose to do so. "It would be much better for the health of the federal banking system and everyone who relies on those institutions, if these companies enter the system through a clearly marked front gate rather than through some back door."

Several fintech companies have praised the OCC's proposal as a positive development and expressed openness to seeking a national bank charter. However, many state regulators and consumer advocates have expressed concerns that a special purpose national bank charter would provide a lawful means for fintech companies to circumvent state consumer protection obligations. For example, the Superintendent of the New York Department of Financial Services opposes the OCC's proposal, arguing that "[a]ny reliance on a federal fintech regulatory framework, such as the proposal contemplated by the OCC, would be irresponsible if it were to ignore the states' historical role and longstanding expertise in this arena."⁴ The Conference of State Bank Supervisors has also condemned the charter, claiming that the charter would "distort the marketplace for financial services" and "undermine state laws and regulations" governing such issues.⁵ Additionally, 49 consumer and small business advocacy groups swiftly issued a joint letter to Comptroller Curry opposing the charter.⁶

This new special purpose national bank charter would allow chartered fintech companies to export interest rates permitted by the laws of the bank's home state and eliminate the need to obtain multiple state licenses to engage in core banking functions. The charter, however, could subject these same companies to supervision by other regulators and additional regulatory regimes and restrictions that could be detrimental to their current business model and activities. It will be important to watch whether the proposed regulatory framework under a fintech charter would have a chilling effect on the number of fintech companies that would ultimately apply.

When announcing the proposal, the Comptroller expressed the OCC's concerted effort to foster collaboration with other regulators, noting his firm belief that all financial regulators must collaborate.

- **Consumer Financial Protection Bureau (CFPB).** The OCC acknowledges that, even with a special national bank charter for fintech companies, the OCC would continue to have

⁴ New York Department of Financial Services, Statement by DFS Superintendent Maria T. Vullo Regarding the OCC Special Purpose National Bank Charters for Fintech Companies (Dec. 2, 2016), <http://www.dfs.ny.gov/about/press/pr1612021.htm>.

⁵ Conference of State Bank Supervisors, Receiverships for Uninsured National Banks, Proposed Rule; Docket ID OCC-2016-0017 (Nov. 14, 2016), <https://www.csbs.org/regulatory/policy/Documents/2016/CSBS%20Comment%20Letter%20on%20OCC%20Receiverships%20for%20Uninsured%20National%20Banks%20NPRM.pdf>.

⁶ <http://ourfinancialsecurity.org/wp-content/uploads/2016/12/OCC-fintech-charter-49-groups-FILED-12-1-2016.pdf> (Dec. 2, 2016).

considerable overlap with the CFPB's supervisory and enforcement jurisdiction. The OCC would have exclusive supervisory and primary enforcement authority over special purpose national banks that are insured depository institutions and have assets of \$10 billion or less.⁷ Special purpose national banks that are insured depository institutions with an excess of \$10 billion in assets would be subject to the CFPB's exclusive supervisory jurisdiction and primary enforcement authority.⁸ Special purpose national banks that do not accept deposits would be subject to CFPB supervision if they engage in mortgage lending or servicing, private education lending, or payday lending or are otherwise deemed a "larger participant" by the CFPB.⁹ And, as long as a special purpose national bank offers any "consumer financial product or service," it is subject to CFPB enforcement jurisdiction.

- **Federal Reserve.** On the same day the OCC released its proposal, Federal Reserve Governor Lael Brainard confirmed that the Fed has formed a [Fintech working group](#) and is coordinating with the other banking regulators on the best approaches to supervising innovative financial services."¹⁰
 - *Applicability of the Federal Reserve Act.* The Federal Reserve Act requires national banks – including special purpose national banks – to become members of the Federal Reserve System.¹¹ Under current law, fintech companies that become national banks would then become subject to statutes and regulations that apply to all Federal Reserve member banks. The Federal Reserve's Regulation W imposes restrictions on how banks can engage in transactions with their affiliates. Those restrictions could deter fintech companies from seeking a national bank charter to the extent that it has shared investors or relationships with affiliates that could run afoul of the prescribed limitations.
 - *Applicability of the Bank Holding Company Act (BHCA).* The OCC has stated that fintech companies that become special purpose national banks may be subject to the BHCA and the Federal Reserve's implementing regulations if the fintech company is owned or deemed to be controlled by a holding company and the fintech company is considered a "bank" for purposes of the BHCA. Importantly, the BHCA, by definition, applies only to

⁷ 12 U.S.C. § 5516(d).

⁸ 12 U.S.C. § 5515(a).

⁹ 12 U.S.C. § 5514. Under the Dodd-Frank Wall Street and Consumer Protection Act, the CFPB may supervise non-bank "larger participant[s] of a market for other consumer financial products or services," as the Bureau defines by rule. 12 U.S.C. § 5514(a)(1)(B). To date, the CFPB has used this authority to supervise certain consumer reporting agencies, debt collectors, student loan servicers, and international money transmitters.

¹⁰ Remarks of Governor Lael Brainard at the Conference on Financial Innovation at the Board of Governors of the Federal Reserve System (Dec. 2, 2016), <https://www.federalreserve.gov/newsevents/speech/brainard20161202a.htm> (noting that the Fed is "in ongoing communication with other regulators to promote, to the greatest extent possible, consistency in approaches and alignment of supervisory requirements").

¹¹ National banks in territories or insular possessions of the United States are exempt from this requirement.

FDIC-insured institutions or entities that both accept demand deposits and make commercial loans.¹²

- **Federal Deposit Insurance Corporation (FDIC).** The FDIC's involvement in a fintech company that becomes a special purpose national bank turns on whether that company proposes to accept deposits. If a nationally chartered fintech company decides to accept deposits, it must obtain the FDIC's approval to do so and would also be subject to the laws that apply to insured depository institutions.

Whether other banking laws and regulations would apply to fintech bank charters would depend on the fintech's activities. However, even where a law would not directly apply, the OCC emphasized that it would use its discretionary powers to ensure that a fintech company achieves the goals of a particular statute or regulation – including those that currently apply exclusively to insured depository institutions through the OCC's authority to impose conditions on its approval of a charter. Current guidance is insufficient to determine how these rules would apply. As a result, there remains uncertainty in the regulatory regimes and supervisory expectations that a fintech company should expect if it were to become a national bank.

- **Community Reinvestment Act (CRA).** Though nondepository institutions are not subject to the CRA, the OCC stated that as part of the chartering process it would require fintech companies seeking a bank charter to demonstrate their commitment to financial inclusion, including how they support fair access to financial services and the fair treatment of their customers. In its white paper, the OCC signaled its intent to impose "CRA-like" standards on fintech companies that would depend on the entity's business model and product offerings.

BASELINE SUPERVISORY EXPECTATIONS

The white paper outlines a set of baseline supervisory expectations for fintech firms seeking a bank charter. Among these requirements are minimum and ongoing capital and liquidity levels based on a fintech company's business model and risk profile. The OCC signaled its intent to impose higher capital standards on fintech companies with off-balance sheet activities that must be maintained at all times. Clarity on capital and liquidity requirements will be vital for fintech companies to begin the cost/benefit analysis of becoming a national bank.

Aside from these capital and liquidity requirements, the OCC's baseline supervisory expectations include: (1) a robust, well-developed business plan that spans a three-year period; (2) a governance structure with the expertise and risk management framework to promote safety and soundness; (3) a well-developed compliance management system; (4) initiatives designed to promote financial inclusion; and (5) recovery and exit strategies documenting the fintech company's plans to unwind the institution in an organized manner in the event of specified financial or risk triggers.

Impact on Existing Bank-Fintech Partnerships

¹² 12 U.S.C. § 1841.

The impact the proposal will have on marketplace lenders who operate under a bank partnership model will be closely monitored by multiple industry and market participants. While a number of banks will praise the OCC's effort to "level the playing field" for banks and fintech companies that are not directly subject to many of the same regulatory requirements, introduction of a bank charter for fintech companies could place significant strain on banks that have significantly altered their business models to cater to the needs – and provide a source of funding – to fintech entrants. For this reason, the amount of time it will take for the OCC to review and approve fintech bank charter applications may be an important factor. The length of the approval process will also be a significant consideration for fintech companies that have gained notoriety for their ability to move quickly when compared with traditional banks.

CONCLUSION

A national bank charter for fintech companies would provide an important option for firms seeking to engage in lending or money transmitting activities without the need for a bank partnership or state licensing. The ultimate practical effect of the OCC's proposal, however, is unclear as too many open questions remain. In the meantime, fintech companies should consider submitting comments and requests for clarifications as the OCC acknowledged that its formal policy for assessing whether a company should receive a national bank charter will be informed by the comments it receives.

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Questions regarding the matters discussed in this Alert may be directed to any of our lawyers listed below, or to any other BuckleySandler attorney with whom you have consulted in the past.

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