

On March 15, 2017, the Office of the Comptroller of the Currency (OCC) released a draft supplement to the Comptroller's Licensing Manual on "Evaluating Charter Applications from Financial Technology Companies" (Licensing Supplement).¹ While the OCC does not normally release drafts of the Licensing Manual for public comment, according to the OCC, it is doing so in this instance to be "consistent with its guiding principles of transparency and fostering open dialogue with stakeholders."² **Comments are due April 14, 2017.** In connection, the OCC also released the "OCC Summary of Comments and Explanatory Statement: Special Purpose National Bank Charters for Financial Technology Companies" (Summary Paper).³

In the first part of this alert, we summarize the OCC's releases and in the second part, we explore a few of the public policy implications.

OCC Draft FinTech Licensing Supplement Overview and Purpose

The Licensing Supplement closely mirrors the OCC's December 2016 paper titled "Exploring Special Purpose National Bank Charters for FinTech Companies" (SPNB Paper), while providing a few key clarifying statements on: (1) the purpose and scope of the charter; and (2) the OCC's expectations for companies applying for a charter.

In the Summary Paper, the OCC noted that the agency received over 100 comment letters on the SPNB Paper. Based on the comments received, the OCC stated that it would be guided by three threshold principles that inform the Licensing Supplement:

1. The OCC will not allow the inappropriate commingling of banking and commerce.
2. The OCC will not allow products with predatory features, nor will it allow unfair or deceptive acts or practices.
3. There will be no "light-touch" supervision of companies that have an SPNB charter. Any FinTech companies granted such charters will be held to the same high standards that all federally chartered banks must meet.

According to the OCC, SPNB charters would be in the public interest by providing uniform standards and robust supervision, which would help ensure that these companies operate in a safe and sound manner and fairly serve the needs of consumers, businesses and communities. Further, the OCC believes that this charter: (1) supports a robust dual banking system while giving companies the option of a federal charter; (2) strengthens the financial system by promoting growth, modernization and competition; and (3) potentially broadens access to financial services.

Activities of FinTechs

The Licensing Supplement applies only to applications from FinTech companies to engage in either lending money or paying checks (or a modern equivalent). These procedures do not apply to a FinTech company that plans to take deposits and thus must be insured by the Federal Deposit Insurance Corporation (FDIC). The OCC notes that lending money and paying checks involve many types of activities. "For example, discounting notes, purchasing bank-permissible debt securities, engaging in lease-financing transactions, and making loans are forms of lending money. Similarly, issuing debit cards or engaging in other means of facilitating payments electronically may be considered the modern equivalent of paying checks."⁴ If a company is interested in engaging in an activity that has not previously been determined to be part of or incidental to the business of banking, a proposal to do so may be included as part of the application process.

Application Procedure

Interested parties (applicants) should make an initial inquiry with the OCC's Office of Innovation, which will set up an exploratory meeting with the organizer and staff from the OCC Licensing Division. That meeting will include a discussion of the company's business model, the Licensing Supplement and the OCC's expectations. An OCC Licensing contact will be assigned to the company and will involve other OCC staff as appropriate for informal discussions with the applicants to discuss the process or any aspects of the application that may present novel or complex issues. This pre-filing stage may include one or more formal pre-filing meetings with the OCC Licensing Division; before that meeting, the applicants should provide the OCC with an overview of the charter proposal, the business plan, qualifications of applicants, proposed senior management, the relevant market, any novel policy or legal issues and any unique aspects of the proposal. Once the application is filed, the applicant must publish a notice of its charter and provide a 30-day period for public comments.

¹ <https://www.occ.treas.gov/publications-by-type/licensing-manuals/file-pub-lm-fintech-licensing-manual-supplement.pdf>. (Note: The Licensing Supplement is not a comprehensive guide to all procedures and requirements for filing an application for SPBN charter and those interested in doing so are directed to review other OCC manuals, regulations and guidance materials.)

² <https://www.occ.treas.gov/news-issuances/news-releases/2017/nr-occ-2017-31.html>.

³ <https://www.occ.treas.gov/topics/bank-operations/innovation/summary-explanatory-statement-fintech-charters.pdf>

⁴ Licensing Supplement, 5

Standards and Policy Considerations

The OCC is guided by certain principles in evaluating an application to establish a national bank, including an SPNB: (1) maintaining a safe and sound banking system; (2) encouraging a national bank to provide fair access to financial services by helping to meet the credit needs of its entire community; (3) ensuring compliance with laws and regulations; and (4) promoting fair treatment of customers, including efficiency and better service. The OCC will not approve proposals contrary to OCC policy or other established public policy, such as proposals that coningle banking and commerce or proposals that include products or services that have predatory, unfair, or deceptive features or that pose undue risk to consumer protection, compliance, or safety and soundness.

Evaluating an Application

In evaluating any application for a national bank charter, the OCC considers, among other factors, whether the applicant bank: (1) has organizers and management with appropriate skills and experience;⁵ (2) has adequate capital to support the projected volume and type of business and proposed risk profile; (3) has a business plan that articulates a clear path and a timeline to profitability; and (4) includes in its business plan, if applicable, a financial inclusion plan (FIP) that has an appropriate description of the proposed goals, approach, activities and milestones for serving the relevant market and community. The OCC will coordinate with other regulators that would have jurisdiction over the proposed SPNB as appropriate. A pending investigation or enforcement action by another regulator may be grounds for denial of a charter application.

Business Plan

The Licensing Supplement includes detailed guidance on the business plan an applicant must submit to the OCC, supplemental to the interagency Business Plan Guidelines.⁶ The Licensing Supplement focuses on six key elements of the business plan:

- 1. Risk Assessment:** The business plan should include a risk assessment that identifies and discusses the particular risks the applicants expect the proposed bank to face given its business model (e.g., concentration risk, compliance risk, reputation risk, strategic risk and operational risk, including cybersecurity risk) and how the bank would effectively manage the identified risks.
- 2. Records, Systems, and Controls:** This section describes the bank's system for customer record keeping and transaction processing and internal controls that will enable the bank to protect customer data and process transactions in an accurate and efficient manner, as well as the bank's compliance management programs.
- 3. Financial Management:** An SPNB will be subject to the minimum leverage and risk-based capital requirements applicable to all national banks.⁷ However, these requirements may not be sufficient for measuring capital adequacy of some SPNBs, especially those with limited on-balance-sheet assets or nontraditional strategies.

This section should propose both minimum capital levels the bank will adhere to initially and minimum capital levels the bank will adhere to after profitability. This section should also discuss how the proposed bank would address adverse market conditions. Finally, this section should address liquidity and funds management.

- 4. Monitoring and Revising the Plan:** This section should include how the board of directors will monitor adherence to the business plan and adjust or amend the plan as appropriate to accommodate significant or material changes. Significant deviations to the business plan may require OCC supervisory non-objection.
- 5. Alternative Business Strategy; Contingency Plans; Recovery and Exit Strategies:** The OCC may require an applicant to include an alternative business strategy detailing how the SPNB will manage potential scenarios when expectations differ significantly from the original plan. In any event, the plan should discuss realistic contingency plans based on critical assumptions, recovery planning and exit strategies.
- 6. Financial Inclusion Plan (FIP):** Applicants engaged in lending or providing financial services to consumers or small businesses must demonstrate a commitment to financial inclusion. The FIP must describe the proposed goals, approach, activities and milestones for serving the relevant market and community. The FIP should describe the products and services the SPNB intends to offer, including any that will foster financial inclusion and the relevant market and community, identify the financial services needs of the relevant market and community, identify milestones for the accomplishment of the financial inclusion objectives, and identify the terms and conditions under which the SPNB will provide lending or financial products and services to consumers or small businesses. The FIP also should address how the SPNB will communicate and receive public input regarding its progress in executing on its FIP and updating or modifying its FIP in appropriate circumstances.

Chartering Decision

A preliminary conditional approval provides the OCC's permission to proceed with the organization of the bank, as it is an indication that the application has passed the first phase of OCC review. A national bank must generally open for business within 18 months of the preliminary conditional approval. The OCC may impose standard requirements (e.g., establishing appropriate policies and procedures) or special requirements (e.g., requiring the bank to raise a higher amount of capital than proposed in the business plan). The OCC also may impose standard conditions (e.g., no deviating from the business model without prior OCC non-objection or adhering to the FIP) or special conditions (e.g., requiring the bank to have a resolution plan, conditions similar to those in law that apply to insured banks, or assessments). The OCC then will issue final approval, being the bank can begin to conduct banking business. The OCC will supervise the SPNB under scheduled supervisory exams. Any conditions imposed will remain in place until removed or modified by the OCC and will be reviewed for compliance as part of the examination process.

⁵ The OCC's regulations and licensing policy include guidance regarding qualifications of organizers, management and directors. The OCC may tailor certain criteria as appropriate. The OCC expects organizers, managers and directors to be well qualified, with diverse experience in relevant areas.

⁶ <https://www.occ.gov/static/licensing/form-business-plan-v2.pdf>.

⁷ 12 CFR 3.

Public Policy Implications

Turning to Capitol Hill, despite the Comptroller Thomas J. Curry's pushing ahead, the OCC's proposal to offer FinTech charters has received considerable pushback from both sides of the aisle. House Republicans and Senate Democrats have separately sent letters to Comptroller Curry urging him not to rush the OCC's plans to regulate FinTech companies, as his term is set to expire on April 1, 2017. Despite the pushback from Congress, he has defended the OCC's authority to make the charters available to FinTech companies, arguing that the agency is merely expanding a longstanding practice of issuing special purpose bank charters. That said, lawmakers are in a position to push back on – or seek to undo – any such moves.

Current Congressional Efforts

On March 10, 2017, all 34 Republican members of the House Financial Services Committee signed a letter⁸ asking Comptroller Curry to avoid rushing the OCC's efforts to establish a SPNB charter for FinTech companies to allow the industry more time to better understand the proposal. Specifically, in their letter, lawmakers argue that the OCC should provide "a full and fair opportunity for stakeholders to see the details of the special charter, solicit feedback, and allow the incoming Comptroller the opportunity to assess the special purpose charter."

Notably, the letter also threatens legislative action if the OCC "proceeds in haste" to establish an SPNB FinTech charter. In particular, House Republicans make clear that if the OCC creates a new policy without providing the opportunity for additional comments or rushes "to finalize the charter prior to the confirmation of a new Comptroller," then they will work to ensure that Congress examines and possibly overturns any such actions.

The pushback is not limited to Republicans alone. Two months prior to the House Republican letter, on January 9, 2017, Senators Sherrod Brown (D-OH) and Jeff Merkley (D-OR) warned in their own letter⁹ to Comptroller Curry that OCC SPNB FinTech charters could undermine financial stability and jeopardize consumer protections. Specifically, the Senators questioned whether the agency has the legal authority to issue such a charter, suggesting that Congress, not the OCC, should determine who has the proper authority to oversee such companies. They also expressed concern that the OCC's proposal could allow predatory practices to spread more quickly. As such, the Senators urged the OCC to "refrain from offering any alternative or special purpose charters" and warned that the OCC's "plan to offer alternative charters to nonbank and FinTech firms as explained could upset the current financial regulatory structure."

This is not the only action on the Hill regarding FinTechs. In September 2016, Representative Patrick McHenry (R-NC) introduced the Financial Services Innovation Act of 2016, which attempts to create a regulatory "sandbox" approach for FinTech firms. The sandbox approach, which loosely mirrors a similar program in the UK, lets companies work alongside a regulator when testing a FinTech product or service. The bill intends to give these firms the ability to test a new product or service with a limited launch without going through the full regulatory process. Representative McHenry's bill also requires 12 financial federal regulators to develop an internal "Financial Services Innovation Office" where companies can seek help in testing a product or service. While the bill has not been re-introduced in this Congress at the time of publication, we anticipate that a reintroduced "2.0" version of the legislation could serve as the starting point for congressional action on FinTech legislation. That said, it is unclear whether both sides will be able to agree on enough issues to garner widespread support.

Next Steps

Comptroller Curry's term expired on April 1, just two weeks before the public comment period closes. What happens next is still difficult to determine. Comptroller Curry could, in theory, continue to serve as Comptroller until a new one is confirmed by the Senate. That said, the confirmation process could take several months and afford Comptroller Curry ample time to shepherd the release of the new FinTech policy, despite congressional resistance. Alternatively, President Trump could ask for Comptroller Curry's resignation – or he could resign on his own. In either case, an Acting Comptroller would be appointed and would serve until the new Comptroller is nominated and confirmed by the Senate. Under the governing law, the Treasury Secretary effectively has the authority to designate whomever he chooses to serve as Acting Comptroller, with no restriction on that person being a current employee of the OCC. It is rumored that Secretary Mnuchin is actively looking for a new Comptroller.

At this point, it is difficult to determine what will happen to the Licensing Supplement and the OCC's proposed FinTech regulatory scheme. What is certain, however, is that the OCC's FinTech policy will be in the spotlight over the coming weeks.

⁸ <http://paybefore.com/wp-content/uploads/2017/03/OCC-Congress-letter-March-2017.pdf>.

⁹ <https://morningconsult.com/wp-content/uploads/2017/01/2017-01-09-OCC-Fintech-letter.pdf>.

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