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OCC to Issue Special Purpose National Bank Charters to Fintech Companies

Posted by Michael Nonaka, Covington & Burling LLP, on Sunday, December 11, 2016

Editor's note: Michael Nonaka is a partner in the financial institutions group at Covington & Burling LLP. This post is based on a Covington publication by Mr. Nonaka, John Dugan, and Luis Urbina.

On December 2, 2016, Comptroller of the Currency Thomas J. Curry announced that the Office of the Comptroller of the Currency ("OCC") would move forward with issuing special purpose national bank charters to financial technology ("fintech") companies. The OCC released a whitepaper[1] outlining its authority to issue charters to fintech companies, its approach to supervising fintech companies, and its process for evaluating charter applications. The OCC is requesting public comment on the whitepaper by January 15, 2017.

Special Purpose Chartering Authority

The National Bank Act authorizes the OCC to grant charters for national banks, and the agency has long interpreted this authorization as allowing it to grant charters for special purpose national banks.[2] Special purpose national banks include trust banks and credit card banks.

To obtain a charter, special purpose national banks must engage in fiduciary activities or provide at least one of the following banking services:

- Receiving deposits;
- Paying checks; or
- Lending money.[3]

The OCC takes the position in the whitepaper that, in at least certain cases, the innovative services offered by fintech companies are tantamount to one of these traditional activities, therefore allowing such companies to obtain special purpose charters. For example, the whitepaper notes that issuing debit cards or engaging in other means of facilitating electronic payments are the "modern equivalent" of paying checks. Ultimately, the OCC will determine whether an applicant's services render it eligible for a special purpose charter on a case-by-case basis.

[1] Office of the Comptroller of the Currency, Exploring Special Purpose National Bank Charters for Fintech Companies 2 (2016) [Hereinafter OCC Whitepaper], https://occ.gov/topics/bank-operations/innovation/special-purpose-national-bank-charters-for-fintech.pdf.
[2] *See* 12 C.F.R. § 5.20(e)(1) (citing 12 U.S.C. §§ 1 *et seq.*).
[3] *Id.*

Because all national banks, including special purpose national banks, are chartered and governed by the National Bank Act, a fintech company with a special purpose charter would be subject to the provisions of the act that prescribe the bank's corporate organization and structure (e.g., classes of shares, voting rights, number of directors, and term of office) and circumscribe the activities that the bank is permitted to conduct.

Rules and Standards Applicable to a Special Purpose National Bank

Special purpose national banks are subject to the same laws, regulations, examination, reporting requirements, and ongoing supervision as other national banks. For example, special purpose national banks are subject to federal statutes and regulations on lending limits; limits on real estate holdings; anti-money laundering and economic sanctions; and prohibitions on unfair, deceptive, or abusive acts or practices. Depending on the bank's activities, other laws may apply. A special purpose bank that is engaged in mortgage lending, for example, would be subject to the Truth in Lending Act, Real Estate Settlement Procedures Act, and other statutes.

Some statutes apply only to a national bank that offers deposits insured by the Federal Deposit Insurance Corporation ("FDIC"). For example, the Community Reinvestment Act ("CRA") establishes a supervisory regime for publicly evaluating a bank's efforts to meet the credit needs of all community members, including low-and moderate-income neighborhoods. The CRA applies only to FDIC-insured banks. Another example is the receivership section in the Federal Deposit Insurance Act ("FDIA") that establishes a framework for the FDIC to act as a conservator or receiver to resolve an insured bank. To address these gaps, the OCC could impose CRA-like requirements on an uninsured special purpose national bank as a condition to approval of the charter application or resolve an uninsured national bank under the National Bank Act, respectively. The OCC recently issued a proposed rule that would provide a framework for the OCC to resolve an uninsured national bank pursuant to the National Bank Act (and not the FDIA).

State law will apply to a special purpose fintech bank "in the same way and to the same extent" that it does to full-service national banks.[4] In particular, the whitepaper notes that a special purpose national bank would look to the National Bank Act (as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act), OCC regulations, and federal judicial precedent to determine if or how state laws apply. Under these statutes, regulations, and precedent, state laws that require the bank to obtain a license to engage in an activity would not apply. However, state law requirements regarding anti-discrimination, fair lending, debt collection, taxation, zoning, criminal laws, torts, and unfair or deceptive treatment of customers would apply.

Coordination among Regulators and Related Banking Laws

Although the OCC would be the primary prudential regulator of a fintech company with a special purpose national bank charter, other regulators will play important roles:

- **Federal Reserve**—All national banks, with few exceptions, are required to be members of the Federal Reserve System by subscribing for stock in the appropriate Federal Reserve Bank. A special purpose national bank would be subject to the laws and regulations applicable to Federal Reserve member banks. In addition, the Bank Holding

[4] OCC Whitepaper, *supra* note 1, at 5.

Company Act ("BHCA") could apply to a company if it controls a special purpose national bank that is a "bank" for purposes of the BHCA—that is, the bank is FDIC-insured or accepts demand deposits and makes commercial loans, and the bank does not qualify for any of the exceptions in the BHCA.

- **FDIC**—A fintech company that proposes to accept deposits other than trust funds is required to apply to and receive approval from the FDIC.
- **Consumer Financial Protection Bureau**—A fintech company that engages in an activity subject to a federal consumer financial law administered by the Consumer Financial Protection Bureau ("CFPB") may be subject to the CFPB's oversight. The CFPB would have primary supervisory and enforcement authority for these laws with respect to an FDIC-insured special purpose national bank with over \$10 billion in assets. The CFPB also will have authority over certain activities conducted by an uninsured special purpose national bank.

Supervisory Expectations

The OCC whitepaper emphasizes that a fintech company with a special purpose national bank charter, like all national banks, would be required to meet high supervisory standards relating to safety and soundness, fair access, and fair treatment of customers, tailored to the company's size, complexity, and risks.[5]

The OCC has identified the following baseline supervisory expectations for a fintech company seeking a national charter: well-supported business plan; governance structure; capital; liquidity; compliance risk management; financial inclusion; and recovery and resolution planning.

Business Plan

A fintech company applying for a special purpose national bank charter will need to submit a comprehensive and detailed business plan. The plan should describe in detail the reasons why the company is applying for a charter and the company's activities. Further, the plan should cover a minimum of three years and include analyses of the markets to be served by the company, management's assessment of relevant risks, descriptions of management's expertise and experience, plans for initial and future capital contributions, information on how the company will maintain and monitor appropriate capital levels as well as any available external sources of capital, comprehensive alternative business strategies, and plans for serving the community, if applicable.

The plan should demonstrate that the company has a reasonable chance for success, will operate in a safe and sound manner, and will have adequate capital to support its risk profile. A company may be required to obtain the prior approval of the OCC in order to materially depart from its business plan.

[5] OCC Whitepaper, *supra* note 1, at 2.

Governance Structure

As it does with all national banks, the OCC will assess a fintech company's proposed governance structure on the basis of whether it is "commensurate with the risk and complexity of its proposed products, services, and activities."[6] The OCC expects national banks to have the expertise, financial acumen, and risk management framework to promote safety and soundness oversight. The Board of Directors must play a prominent role in governance, and directors are required to actively oversee management, provide credible challenge, and exercise independent judgment.

Capital

The OCC will evaluate a fintech company from a capital perspective to determine whether minimum and ongoing capital levels are commensurate with the risk and complexity of the proposed activities, including on- and off-balance sheet activities. A fintech company applying for a special purpose national bank charter will be analyzed by the OCC from a capital adequacy perspective based on the risks and complexities of the company's products, services, and operating characteristics, taking into account quantitative factors (e.g., total assets, assets measured by risk weighting) and qualitative factors (e.g., quality of management, ownership, asset quality, earnings, risk diversification).

A fintech company that has off-balance sheet activities would be expected to propose a minimum level of capital to the extent that the OCC's minimum regulatory capital requirements do not adequately take into account the risks from its off-balance sheet activities. The OCC will consider adapting capital requirements as necessary to adequately reflect the company's risks and to the extent consistent with law.

Liquidity

Similarly, the OCC expects to require liquidity commensurate with a fintech company's risk and complexity as informed by the company's access to funds and its cost of funding. Relevant factors considered by the OCC include expected funding sources, needs, and costs; net cash flow and liquid asset positions; projected borrowing capacity; highly liquid asset and collateral positions; requirements for unfunded commitments; and the adequacy of a company's contingency funding plans.

Compliance Risk Management

A fintech company seeking a special purpose national bank charter is expected to demonstrate a culture of compliance that includes a top-down, enterprise-wide commitment to understanding and adhering to applicable laws and regulations and operating in accordance with OCC supervisory guidance. The company should have a compliance management system that is commensurate with its risks and that includes an anti-money laundering ("AML") and economic sanctions compliance program and a consumer compliance program to ensure fair treatment of customers, fair access to financial services, and compliance with prohibitions on unfair,

[6] *Id.* at 9.

deceptive, or abusive acts or practices. The OCC will consider whether and how innovative elements of a business model may affect the proposed bank's compliance risk profile.

Financial Inclusion

The National Bank Act charges the OCC with ensuring that national banks treat their customers fairly and provide fair access to financial services. The OCC will be guided by these principles in evaluating an application for a special purpose national bank charter.

The OCC expects a fintech company seeking a special purpose national bank charter that engages in lending activities to demonstrate a commitment to financial inclusion that supports fair access to financial services and fair treatment of customers. The nature of the commitment will depend on the company's business model and types of loan products or services. In addition, a fintech company engaged in lending will be required to explain its commitment to financial inclusion in its business plan, with appropriate consideration of the following elements:

- An identification and method to defining the relevant market, customer base, or community;
- A description of the products and services the company intends to offer, marketing and outreach plans, and the intended delivery mechanisms;
- An explanation of how the company's products and services, marketing plans, and delivery mechanisms promote financial inclusion (e.g., provide access to underserved consumers or small businesses); and
- Full information on how the company's policies, procedures, and practices are designed to ensure its products and services are offered on a fair and non-discriminatory basis.

Recovery and Exit Strategies; Resolution Plan and Authority

The fintech company's business plan is required to include alternative business and recovery strategies to address best-case and worst-case scenarios. The plan should be integrated into the company's overall risk governance framework, aligned with the company's other risk management plans, and coordinated with any applicable parent or affiliate risk management planning. The plan should include triggers alerting the company to the risk or presence of severe stress, a wide range of credible options that could be taken to restore its strength and viability, and escalation and notification procedures. While the objective of these measures is to remain a viable entity, the OCC may require the company to have a clear exit strategy.

Charter Application Process

The whitepaper states that fintech companies interested in a special purpose national bank charter can expect the OCC to follow its standard policies and procedures for reviewing and making determinations on charter applications. Applicants should review the OCC's chartering regulation, 12 C.F.R. § 5.20, and the "Charters" booklet of the *Comptroller's Licensing Manual.*

The licensing process generally consists of four stages:

- **Prefiling Stage**—potential applicants engage with the OCC, including the Licensing Department and Office of Innovation, in formal and informal meetings to discuss their proposal, chartering process, and application requirements, and prepare a complete application, including business plan.
- **Filing Stage**—applicants submit the application and publish notice of the application in a newspaper as soon as possible before or after the date of the filing.
- **Review and Evaluation Stage**—the OCC conducts background and field examinations, and reviews and analyzes the application to determine whether the fintech company has a reasonable chance of success, will be operated in a safe and sound manner, will provide fair access to financial services, will ensure compliance with laws and regulations, will promote fair treatment of customers, and will foster healthy competition.
- **Decision Stage**—the OCC decides whether to grant preliminary conditional approval (preliminary conditional approval phase); the company raises capital, prepares for opening, and is subject to a preopening examination from the OCC (organization phase); and the OCC decides whether the company has satisfied the requirements for opening (final approval phase).

The OCC will impose a number of standard conditions when it grants preliminary conditional approval, such as the establishment of appropriate policies and procedures and the adoption of an internal audit system appropriate to the size, nature, and scope of the company's activities. The OCC also may impose additional conditions, including the following:

- Prior OCC approval in order for the company to change its business model
- Higher capital and liquidity requirements
- Resolution plan to sell itself or wind down if necessary
- CRA-like conditions

The fintech company may be required to enter into an "Operating Agreement" with the OCC containing these substantive conditions.

At the same time, the OCC recognizes that it may need to tailor some requirements that apply to a full-service national bank to address the fintech company's business model. The capital requirements for fintech companies with substantial off-balance sheet activities illustrate the need for appropriate tailoring of certain requirements.

Request for Comment

The OCC is requesting comment on all aspects of the whitepaper and in response to the following questions:

1. What are the public policy benefits of approving fintech companies to operate under a national bank charter? What are the risks?
2. What elements should the OCC consider in establishing the capital and liquidity requirements for an uninsured special purpose national bank that limits the type of assets it holds?
3. What information should a special purpose national bank provide to the OCC to demonstrate its commitment to financial inclusion to individuals, businesses and communities? For instance, what new or alternative means (e.g., products, services)

might a special purpose national bank establish in furtherance of its support for financial inclusion? How could an uninsured special purpose bank that uses innovative methods to develop or deliver financial products or services in a virtual or physical community demonstrate its commitment to financial inclusion?

4. Should the OCC seek a financial inclusion commitment from an uninsured special purpose national bank that would not engage in lending, and if so, how could such a bank demonstrate a commitment to financial inclusion?
5. How could a special purpose national bank that is not engaged in providing banking services to the public support financial inclusion?
6. Should the OCC use its chartering authority as an opportunity to address the gaps in protections afforded to individuals versus small business borrowers, and if so, how?
7. What are potential challenges in executing or adapting a fintech business model to meet regulatory expectations, and what specific conditions governing the activities of special purpose national banks should the OCC consider?
8. What actions should the OCC take to ensure special purpose national banks operate in a safe and sound manner and in the public interest?
9. Would a fintech special purpose national bank have any competitive advantages over full-service banks the OCC should address? Are there risks to full-service banks from fintech companies that do not have bank charters?
10. Are there particular products or services offered by fintech companies, such as digital currencies, that may require different approaches to supervision to mitigate risk for both the institution and the broader financial system?
11. How can the OCC enhance its coordination and communication with other regulators that have jurisdiction over a proposed special purpose national bank, its parent company, or its activities?
12. Certain risks may be increased in a special purpose national bank because of its concentration in a limited number of business activities. How can the OCC ensure that a special purpose national bank sufficiently mitigates these risks?
13. What additional information, materials, and technical assistance from the OCC would a prospective fintech applicant find useful in the application process?