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Dueling Fintech Regulatory Initiatives May Work Best Together

By **Philip Rosenstein**

Law360 (November 20, 2019, 8:00 PM EST) -- Federal and state banking regulators have locked horns over the legality of the Office of the Comptroller of the Currency's fintech charter, but insiders say a state-backed initiative to standardize payment laws could work in concert with the charter to the benefit of the industry.

The OCC's controversial charter for nondepository financial institutions, known as the fintech charter, and the Conference of State Bank Supervisors' model payments law address related pain points stemming from a complex U.S. financial regulatory landscape, and attorneys and industry players tell Law360 the two may provide their own unique benefits to the space and ultimately complement each other.

"Both the OCC fintech charter and CSBS model payments law reflect the growing realization from policymakers that 20th-century regulations might not be best suited for 21st-century financial technology companies," Nick Catino, head of policy and campaigns at global payments company TransferWise, told Law360.

"TransferWise supports both initiatives, which could simplify and harmonize regulatory compliance for modern payments companies," he said. "Fintech companies, the financial marketplace and consumers will be well served if both proposals are successfully implemented."

As innovation in financial services increasingly provides the opportunity for payments companies of all stripes to thrive, the rigidity and complexity of the U.S. financial regulatory system has been seen as a barrier to seamless growth.

The OCC first outlined its special-purpose national charter in a white paper at the tail end of 2016, and the CSBS has likewise geared up to address financial innovation through its Vision 2020 initiative announced in May 2017.

Both the CSBS and the New York Department of Financial Services have sued the OCC challenging its authority to offer a national bank charter to nondepository institutions, throwing cold water on the initiative, at least for now.

The New York case is expected to ascend to the Second Circuit after the U.S. Southern District of New York ruled in the state's favor last month. The CSBS case was brought in D.C. federal court and was dismissed in early September.

As state banking regulators seek to retain regulatory authority over the burgeoning fintech space crowded with payments, lending and blockchain companies, the CSBS has been exploring its own initiatives to simplify the matrix of regulations that vary state by state with a model payments law.

The CSBS is composed of financial regulators from all 50 U.S. states and Washington, D.C., Guam, Puerto Rico, American Samoa and the U.S. Virgin Islands.

Experts say TransferWise's appreciation for both initiatives is a testament to a widespread desire in the financial services sector for more standardization and simplicity in the regulatory framework, particularly from firms that don't have the luxury of a bank charter.

Both the OCC and CSBS have taken the concerns of industry to heart, and each initiative, while potentially overlapping in their goals of reducing regulatory burdens, may very well work well together, according to Michael Nonaka, co-chair of Covington & Burling LLP's financial services group.

"I think that the two frameworks are complementary and not necessarily at odds," Nonaka told Law360. "Whether a company will be most interested in the model payments law or a special purpose fintech charter is primarily going to come down to what financial products and services they're offering and the scale of the products and services and the different geographic regions in which they want to offer them."

The fintech charter would provide companies with a limited version of a national bank charter that would allow these firms to engage in banklike activities, such as paying checks and making loans across the country in exchange for strict federal oversight, freeing them from some of the burdens faced in complying with multiple state chartering and licensing requirements.

Senior vice president and deputy general counsel at CSBS Margaret Liu explained that the OCC made clear that its fintech charter is focused on a subset of well-established financial services companies aiming to do business on a national scale. The model payments law, on the other hand, is geared toward any company, of any size, looking to engage in the payments space.

"The two circles in the Venn diagram don't really overlap in the sense that we're focused on the nuts and bolts of what state regulators do," Liu said. "What the [model payments law] looks at are licensing definitions, financial safety, and soundness and consumer protection. And our members are focused on improving what's within their purview, which is the licensing the consumer protection and data supervision."

From the start, the OCC has been clear that it's looking to established companies with proven business models to apply for the charter, whereas the model payments law is really geared toward a whole gamut of payments companies, Liu said.

"State licensing is for small companies [and] it's for big companies," Liu said. "There are some very large national or multinational companies that for their payments business activities will need a state license. But state licensing is also there for small companies. It's for brick-and-mortar, it's for online companies. So there are a lot of different business models."

The model payments law may also serve as a stepping stone for companies that want to eventually work on a national scale.

Some payments companies "may in the future want to make loans, or they may in the future want to engage more directly with the payment services," Nonaka outlined. "And so at that point, the business model could be more conducive to having a special purpose national bank charter for fintech companies."

But there is still the chance that in the event a fintech charter is allowed to move forward after a favorable court decision, companies that may have benefited from the model payments law would rather focus their energy on applying for a federal charter.

Stephen Aschettino, chair of payments technology at Loeb & Loeb LLP, suggested that a larger company looking to do business on a national scale would likely aim directly at the fintech charter.

"Under a hypothetical where an existing company wants to come into the U.S. and provide services on a national basis, I would advocate that they apply for the fintech charter" in a scenario where both the model payments law and the fintech charter are available options, Aschettino said.

In the meantime, however, for a pure fintech payments company, a model payments law would provide outsized benefits.

"The [CSBS] model state law would harmonize licensing, examination and supervision rules across the country for national payments companies," Catino said. "As TransferWise is already licensed in nearly every state, the main benefits of the CSBS proposal could come from increased examination coordination and more consistent prudential supervision. Despite the lengthy licensing process, we've generally had a positive experience with our state regulators."

Aschettino added that he expects a model payments law would have a more immediate effect in the short term, and there is already a significant amount of coordination between state regulators that can help quell some of the burdens stemming from variation between states.

While the fintech charter is held up in court, the timeline for implementing a model payments law is also unclear, leaving fintech companies hoping for consistency across state financial regulations in the meantime.

The OCC declined to comment on this matter.

--Additional reporting by Jon Hill. Editing by Philip Shea and Jay Jackson Jr.