

OCC Forges Ahead With Fintech Charter, Releasing Draft Licensing Manual Supplement

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The OCC's fintech charter proposal is generating a lot of political and media sound and fury. Comptroller Curry's [speech](#) in strong defense of the fintech charter was followed by a [letter](#) from the House Financial Services Committee warning the Comptroller against finalizing the new policy – i.e. beginning to accept applications – in light of the change in Administration and his short time left in office. The OCC nonetheless forged ahead with its fintech charter framework by publishing a [supplement](#) to its licensing manual last week which, in a possible nod to the HFSC majority, was in draft form.

Despite all of this sound and fury, however, there is an element of disappointment in the OCC's latest release, for what might have been a viable method to broaden access to financial services appears likely to be inaccessible to all but the most established and well-capitalized fintech companies. The repeated emphasis on “no inappropriate commingling of banking and commerce,” on “no light touch” with respect to regulation and on the full panoply of laws and regulations being applicable do not bode well for the nimble fintech company accustomed to moving rapidly to meet changing customer preferences backed by equally nimble and demanding venture capitalists, equity funds or deep-pocket corporate investors.

The most important revelations in the supplement and the accompanying [explanatory statement](#) are:

- The overwhelming focus in these new materials on “fintech” business models, coupled with the statement that the OCC will “not allow the inappropriate commingling of banking and commerce,” significantly narrows the types of businesses that are likely to be granted a charter. For example, retailers who seek to obtain a charter in order to offer card products and reduce their interchange fees would face significant headwinds. Money transmitters, some payment service providers and established marketplace lenders, however, could benefit.
- The OCC expects charter applicants will likely conduct one of the core banking activities of lending money or paying checks (interpreted broadly) but not the core banking activity of accepting deposits. Although the materials do not preclude an applicant that expects to accept deposits, as we predicted in our previous [memo](#) and [webcast](#) on the OCC's December 2016 [proposal](#), we think the combined impact of the FDIC's reticence to grant deposit insurance to monoline banks, the significant downsides of being treated as a Bank Holding Company Act bank and the OCC's posture in the materials, all make it unlikely that a deposit-taking institution will be able to successfully obtain a special purpose national bank charter.
- Payday lenders and similar companies are out of luck. The OCC has stated that it “will not allow products with predatory features nor will it allow unfair or deceptive acts or practices.”

Over 100 [comments](#) were submitted to the OCC's December 2016 proposal. Many non-bank lenders, payment service firms and their trade associations strongly support the proposal and encouraged the OCC to provide further flexibility for charter applicants. Many community and regional banks, as well as state regulators and attorneys general, however, expressed concern that the special purpose charter would hold chartered firms to less stringent consumer protection requirements and banking safety and soundness standards, and thus encourage regulatory arbitrage.

In response to the comments received, the OCC said in the [explanatory statement](#) released concurrently with the licensing supplement that it would be guided by certain threshold principles:

- The OCC will not allow the inappropriate commingling of banking and commerce.
- The OCC will not allow products with predatory features nor will it allow unfair or deceptive acts or practices.
- There will be no “light-touch” supervision of companies that have a special purpose national bank charter. Any fintech companies granted such charters will be held to the same high standards that all federally chartered banks must meet.

Chartering Process

The licensing supplement sets out the requirements for applicants seeking the special purpose national bank charter as well as the general process for submission, OCC review and approval. The chartering process, which will look familiar to anyone who has been through the usual process for chartering a national bank, consists of four main phases:

- **Pre-filing phase**, including an initial meeting with OCC staff to discuss preliminary questions and more formal pre-filing meetings to discuss the applicant’s proposed business plan, qualifications of the organizers and senior management and any novel policy or legal issues.
- **Filing of charter application by applicant**, including the business plan and publication for public notice and comment of its application in the community in which the applicant is located.
- **OCC review and evaluation of an application**, at which point the OCC will consider, among other factors, whether the applicant:
 - has organizers and management with appropriate skills and expertise;
 - has adequate capital to support the business model;
 - has a business plan that provides a clear path and timeline to profitability; and
 - includes in its business plan an appropriate financial inclusion plan.
- **OCC approval**, consisting of a preliminary conditional approval step, indicating that the applicant may proceed with its organization as a bank according to the proposed business plan, and final approval, at which point the OCC formally issues the special purpose charter.

Business Plan

As noted above, an applicant must submit a detailed business plan as part of its charter application. The business plan must include a discussion of the applicant’s:

- risk profile and how the applicant would effectively manage the identified risks;
- system for customer record keeping and transaction processing, internal controls ensuring transaction and data integrity and enterprise-wide compliance management program;
- financial management plan, including proposed minimum capital levels and how the applicant would address adverse market conditions;
- processes for the board of directors to monitor adherence to the proposed business plan and make adjustments as necessary;
- contingency plans, recovery and exit strategies, as well as an alternative business strategy in certain cases; and
- financial inclusion plan, including the proposed goals, approach, activities and milestones for serving its market and community if the applicant is engaged in lending or providing financial services to consumers or small businesses.

No Light Touch

Consistent with the OCC’s assurance that companies receiving a special purpose national bank charter will not be afforded “light touch” supervision, the supplement emphasizes that chartered firms will be subject to the same laws, regulations and federal supervision that apply to all national banks. For instance, chartered firms would be subject to the same leverage and risk-based capital guidelines applicable to all national banks under the OCC’s regulations. In addition, the supplement notes that the OCC may impose special conditions on a firm as a condition of its charter approval, such as higher capital and liquidity levels and the development of a resolution plan, depending on the specific risks presented by a firm’s business model. While the Community Reinvestment Act technically does not apply to non-deposit-taking institutions, OCC approval will be conditioned on a demonstrated commitment to financial inclusion if an applicant’s business plan includes lending or providing financial services to consumers or small businesses. For some fintechs, the practical utility of the charter, namely the benefit of federal preemption of costly state licensing requirements and usury laws, will have to be balanced by the capital, liquidity and supervisory standards accompanying a bank charter.

The OCC's release also did not provide further information on coordination with other banking regulators, except to note that the OCC will "coordinate with other regulators as appropriate" with other regulators that may have jurisdiction over the proposed special purpose bank.

OCC Comptroller Curry, who has been a driving force for the fintech charter, is ending his five year term at the OCC in April, and [statements](#) by Treasury Secretary Steven Mnuchin indicate that the Trump administration is planning to replace him with another Comptroller. The new Comptroller would have significant power to shape or stall the fintech charter program.

The OCC will accept comments on the supplement until April 14, 2017.

Law Clerk Madison J. Roberts contributed to this post.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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