

**MORE SENSE THAN MONEY: NATIONAL CHARTER OPTION FOR  
FINTECH FIRMS IS THE RIGHT CHOICE**

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*The financial technology field is a rapidly growing sector that threatens to disrupt established financial institutions and their accompanying regulatory structure. New types of financial services and products do not fit neatly into the current regulatory landscape, which has hampered growth and competition with traditional financial institutions. This article advances the idea that the Office of the Comptroller of the Currency's recently proposed special purpose national bank charter provides an appropriate solution that protects consumers, encourages innovation and competition, and moves the industry forward. First, this article briefly describes the financial technology sector and the scheme of national bank regulation. Second, the proposed charter is put in context, examining the state and national regulatory schemes currently monitoring the financial technology industry. Lastly, this article evaluates the potential impact of a special purpose national bank charter on consumers, regulatory bodies, and financial technology companies themselves.*

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## I. INTRODUCTION

When attempting to explain the explosive growth of the financial technology sector (“fintech”), it is an understatement to say that the industry has hit record highs in the past six months, year, or even three years. Rather, fintech growth has been astronomical and has consistently set and broken growth records, despite a slowdown in billion-dollar mega-deals for 2016.<sup>1</sup> In

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2014, investment in the industry tripled over the previous year to a stunning \$12 billion.<sup>2</sup> Another evaluation showed that industry investment grew from \$17.8 billion to more than \$38 billion between 2014 and 2015.<sup>3</sup> While it may be impossible to count the exact number of fintech firms, Forbes notes that different estimates put the number between 5,000 and 6,000 firms.<sup>4</sup> Another reason it can be so hard to quantify fintech's explosive growth is due to the diversity of industries encompassed by fintech.<sup>5</sup> Cryptocurrencies,<sup>6</sup> blockchain,<sup>7</sup> security, banking and payments, and

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<sup>1</sup> Julia Verhage, *Trouble Brewing for Private Companies?*, BLOOMBERG MARKETS (Nov. 16, 2016), <https://www.bloomberg.com/news/articles/2016-11-16/private-funding-for-fintech-firms-has-taken-a-tumble>.

<sup>2</sup> Call Levels, *The State of Fintech Industry as We Know It Infographic*, FINTECH FINANCE (Feb. 3, 2016), <http://www.fintech.finance/01-news/the-state-of-fintech-industry-as-we-know-it-infographic/>.

<sup>3</sup> Jean Baptiste Su, *The Global Fintech Landscape Reaches over 1000 Companies, \$105B In Funding, \$867B In Value: Report*, FORBES (Sept. 28, 2016), <http://www.forbes.com/sites/jeanbaptiste/2016/09/28/the-global-fintech-landscape-reaches-over-1000-companies-105b-in-funding-867b-in-value-report/#41f7b52a4e86>.

<sup>4</sup> Falguin Desai, *Fintech Startups Face Difficult Market Ahead*, FORBES (Jan. 4, 2016), <http://www.forbes.com/sites/falgunidesai/2016/01/04/fintech-startups-face-difficult-market-ahead/#48d614e13145>.

<sup>5</sup> Larry D. Wall, *Avoiding Regulation: FinTech versus the Sharing Economy*, FED. RES. BANK ATLANTA (Sept. 2016), <https://frbatlanta.org/cenfis/publications/notesfromthevault/09-avoiding-regulation-fintech-versus-the-sharing-economy-2016-09-29>. “Financial technology companies are generally startups founded with the purpose of disrupting incumbent financial systems and corporations that rely less on software.” (citing *Fintech Definition*, FINTECH WEEKLY, <https://www.fintechweekly.com/fintech-definition> (last visited Apr. 4, 2017)).

<sup>6</sup> Crypto-currency can be defined as “a currency underpinned by technological surety as opposed to a central bank.” Robert Churcher & Louise Perfect, *A Beginner's Guide to FinTech: Navigating the Jargon*, PWC (May 11, 2016), [http://pwc.blogs.com/megatrend\\_matters/2016/05/a-beginners-guide-to-fintech-navigating-the-jargon.html](http://pwc.blogs.com/megatrend_matters/2016/05/a-beginners-guide-to-fintech-navigating-the-jargon.html).

<sup>7</sup> “Blockchain, generally speaking, is used to create public ledgers of transactions and distribute them in a decentralized manner to several computers, making it just about impossible to hack and change all the recorded versions of the data.” Natalie Rodriguez, *An Inside Look At A Law Firm Diving Into Bitcoin*

insurance are just a few<sup>8</sup> of the categories that make up the fintech landscape.<sup>9</sup> Several popular companies, such as Square, LendingClub, and Social Finance, Inc. (“SoFi”) are all valued above \$6 billion.<sup>10</sup> By some measures, Paypal (which owns the popular peer-to-peer payment<sup>11</sup> company Venmo) holds more customer deposits than all but twenty U.S. banks.<sup>12</sup>

The growth of this industry, combined with the large amount of consumer funds that some fintech companies hold, has raised

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*Tech*, LAW360 (March 10, 2016), <https://www.law360.com/articles/769691/an-inside-look-at-a-law-firm-diving-into-bitcoin-tech>. Blockchain is the underlying technology for crypto-currencies, as well as smart contracts “that can automatically execute payments upon validating ownership information or recognizing a trigger event using online information.” *Id.* For a more detailed explanation of bitcoin and blockchain technology, see Marco Santori et al., *How Blockchain Will Revolutionize Commercial Transactions*, LAW360 (May, 12, 2016), <https://www.law360.com/articles/794611/how-blockchain-will-revolutionize-commercial-transactions>.

<sup>8</sup> For a broader view of the different sub-sectors that make up FinTech, as well as an overview of the disruptive impact of FinTech on the financial services industry as a whole, see generally *Blurred Lines: How FinTech is Shaping Financial Services*, PWC (Mar. 2016), <http://www.pwc.com/gx/en/advisory-services/FinTech/pwc-fintech-global-report.pdf>.

<sup>9</sup> Su, *supra* note 3.

<sup>10</sup> Call Levels, *supra* note 2. SoFi has recently partnered with the ABA to market directly to law students who may have an interest in refinancing their loans, touting their loan volume of \$13B+ for over 200,000 borrowers. See *SoFi Student Loan Refinancing*, AMERICAN BAR ASSOCIATION, [http://www.abainsurance.com/personal-programs/student-loan-refinancing/?utm\\_source=Listrak&utm\\_medium=Email&utm\\_term=http%3A%2F%2Fwww.abainsurance.com%2Fpersonal-programs%2Fstudent-loan-refinancing%2F&utm\\_campaign=Student+Loans+%26+the+Benefits+of+Refinancing](http://www.abainsurance.com/personal-programs/student-loan-refinancing/?utm_source=Listrak&utm_medium=Email&utm_term=http%3A%2F%2Fwww.abainsurance.com%2Fpersonal-programs%2Fstudent-loan-refinancing%2F&utm_campaign=Student+Loans+%26+the+Benefits+of+Refinancing) (last visited Mar. 17, 2017).

<sup>11</sup> Peer to peer payment services allow individuals to send each other money “from their mobile devices through a linked debit card” or bank account. Those funds are then stored in an account that can disperse funds to other individuals or banks. See generally Amber Murkakami-Fester, *Venmo, PayPal, Square Cash and More: What Are Peer-to-Peer Payments?*, NERDWALLET (Oct. 21, 2016), <https://www.nerdwallet.com/blog/banking/p2p-payment-systems/>.

<sup>12</sup> Telis Demos, *PayPal Isn’t a Bank, But It May Be the New Face of Banking*, WALL STREET J. (June 1, 2016), <http://www.wsj.com/articles/as-banking-evolves-fintech-emerges-from-the-branch-1464806411>.

concerns. Particularly, money held by many of these firms is not protected or backstopped<sup>13</sup> by the federal government's deposit insurance, as only banks can hold deposits.<sup>14</sup> This potential risk to consumers, combined with an increase in the number of bank-like activities, has led various governmental agencies in the U.S. to address concerns about instability in the financial system and the insecurity of consumer funds. Recently, the White House under President Obama published a white paper entitled "A Framework for Fintech,"<sup>15</sup> outlining "widely-shared values and practical expectations for the financial services sector . . . ."<sup>16</sup> The ten enumerated principles focused on consumers, maximizing transparency, promoting financial inclusion and health, and protecting financial stability.<sup>17</sup> Similarly, the federal banking regulator of nationally chartered banks, the Office of the Comptroller of the Currency ("OCC"), announced it would consider issuing formal bank charters to online lenders, payment

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<sup>13</sup> "The FDIC was created by the Banking Act of 1933, commonly referred to as the Glass-Steagall Act, to maintain public confidence in the banking system by, among other things, insuring bank deposits within a specified limit." Paul T. Clark, *Just Passing Through: A History and Critical Analysis of FDIC Insurance of Deposits Held by Brokers and Other Custodians*, 32 REV. BANKING & FIN. L. 99, 100 (2012–2013). "Deposit insurance is intended to instill confidence in depositors by assuring them that their deposits are safe regardless of the financial condition of their bank." *Id.* at 168.

<sup>14</sup> See generally Demos, *supra* note 12.

<sup>15</sup> NATIONAL ECONOMIC COUNCIL, A FRAMEWORK FOR FINTECH, WHITE HOUSE (2017), [https://obamawhitehouse.archives.gov/sites/obamawhitehouse.archives.gov/files/documents/A%20Framework%20for%20FinTech%20\\_FINAL.pdf](https://obamawhitehouse.archives.gov/sites/obamawhitehouse.archives.gov/files/documents/A%20Framework%20for%20FinTech%20_FINAL.pdf). While President Obama's directives in this area may have signaled one approach, President Trump's new administration will be able to pick the next Comptroller of Currency, and may decide to take a wholly different approach to fintech companies. See *Trump's Chance to Redefine the Regulators*, WALL STREET J. (Jan. 18, 2017), <http://graphics.wsj.com/Who-are-the-financial-regulators/?mod=e2tw>.

<sup>16</sup> *Id.*

<sup>17</sup> *Id.* While these principles are subject to change with a new incoming President, the white paper provides an outline of the potential considerations the federal government faces when attempting to deal with the growing and disruptive industry.

companies, and other fintech firms.<sup>18</sup> This special purpose national bank charter (previously used to authorize credit card banks)<sup>19</sup> would require any firms who elected to seek a charter to conform to a formal system of federal regulation, instead of having to comply with a patchwork of state regulation by partnering with chartered financial institutions.<sup>20</sup>

While some commenters argue that government regulation will only create uncertainty in a growing industry,<sup>21</sup> fintech companies, like Circle Internet Financial,<sup>22</sup> have requested increased regulation and security in order to increase the ease of doing business nationally due to uniformity of laws and regulations.<sup>23</sup> Fintech companies will continue to reduce costs associated with borrowing, improve the quality of financial services, harness the

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<sup>18</sup> James Rufus Koren, ‘*Fintech*’ Firms Notch Win as Regulator Allows Them to Seek Federal Bank Charters, L.A. TIMES (Dec. 2, 2016), <http://www.latimes.com/business/la-fi-fintech-charters-20161202-story.html>.

<sup>19</sup> Credit card banks are national banks limited to the issuance of credit cards to customers. See OFFICE OF THE COMPTROLLER OF THE CURRENCY, EXPLORING SPECIAL PURPOSE NATIONAL BANK CHARTERS FOR FINTECH COMPANIES (Dec. 2016), <https://www.occ.treas.gov/topics/bank-operations/innovation/comments/special-purpose-national-bank-charters-for-fintech.pdf> [hereinafter *Exploring Special Purpose National Bank Charters for Fintech Companies*].

<sup>20</sup> Rachel Witkowski & Telis Demos, *Fintech Startup Craves More Regulation*, WALL STREET J. (June 9, 2016), <http://www.wsj.com/articles/fintech-startup-craves-more-regulation-1465517775>. Currently, many companies are forced to rely on relationships with currently chartered banks or engage in state-by-state compliance in order to issue loans. *Id.*

<sup>21</sup> Rohit Arora, *Government Should Think Before Imposing Regulation on Fintech*, TECHCRUNCH (Aug. 2, 2015), <https://techcrunch.com/2015/08/02/government-should-think-before-imposing-heavy-regulation-on-fintech/> (arguing regulators should create clarity, not more regulation, in order to lower the cost of administering critical credit for underserved markets and increase transparency).

<sup>22</sup> Circle Internet Financial, or simply “Circle,” is a payments processing company that uses open Internet standards and protocols (including blockchain) to make “online payments easier to use, safer and more convenient than ever.” *About*, CIRCLE INTERNET FINANCIAL LIMITED, <https://www.circle.com/en/about> (last visited Apr. 4, 2017).

<sup>23</sup> Witkowski & Demos, *supra* note 20.

power of data-driven analytics for assessing risk, and create a more diverse and stable credit landscape.<sup>24</sup> Additionally, the OCC believes that fintech companies will continue to drive changes in financial services to “reach unbanked and underserved populations, [and] make products and services safer and more efficient . . . .”<sup>25</sup> These improvements will likely continue regardless of a charter offering for fintech firms, and consumers and small business owners across the country stand to benefit from a new age in banking that is more accessible and inclusive than ever.

This Recent Development argues that a special purpose bank charter would benefit both consumers and the financial services industry by subjecting larger fintech companies to increased scrutiny and regulation. A more cohesive scheme of regulations would create improved transparency, competition, and consumer protection, while reducing the limiting effect of the current state-by-state regulatory scheme on fintech companies. Part II of this recent development provides a brief overview of the scheme of national bank regulation, including the role of the OCC, the value of special purpose bank charters, and the OCC’s statutory authority for creating new bank charters. Part III examines the costs and benefits of current regulation of the fintech industry, focusing on institutions that specialize in lending or other activities that often attract increased regulatory scrutiny. Lastly, Part IV evaluates the potential of a specified bank charter for fintech firms, including the benefits and risks that would accompany it. Despite concerns leveled by state banks and other institutions that would be adversely impacted by a charter for fintech firms, such a charter would provide better management of the unique risks present in the industry, increase transparency, and better protect consumers while

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<sup>24</sup> *The Fintech Revolution: A Wave of Startups is Changing Finance for the Better*, THE ECONOMIST (May 9, 2015), <http://www.economist.com/news/leaders/21650546-wave-startups-changing-financefor-better-fintech-revolution>.

<sup>25</sup> Thomas J. Curry, Comptroller, Office of the Comptroller of the Currency, Remarks Regarding Special Purpose National Bank Charters for Fintech Companies, at 2 (Dec. 2, 2016), <https://www.occ.treas.gov/news-issuances/speeches/2016/pub-speech-2016-152.pdf>.

also providing enhanced services for consumers and small business owners.

## II. EXPLANATION OF THE FEDERAL BANK REGULATORY SYSTEM AND THE OCC

The federal government provides regulatory oversight for the banking and securities markets of the United States in order to protect borrowers and investors that participate in those markets.<sup>26</sup> Financial regulation is designed to mitigate financial instability through the promulgation of rules for specific types of institutions and behaviors.<sup>27</sup> The responsibility of overseeing major financial institutions like banks is divided amongst several federal agencies whose duties sometimes overlap with state level regulatory authority. The parallel federal and state banking systems that co-exist in the United States give potential banks the option of chartering under federal law and regulation, or state law and regulation.<sup>28</sup> Both banking systems provide “different, positive contributions to the overall strength of the U.S. banking system.”<sup>29</sup> This section will provide a brief overview of the federal regulatory scheme, the structure of special purpose banks, and how financial technology companies would fit into the federal regulatory scheme under a special purpose charter.

### A. *Outline of the Federal Bank Regulatory System*

The OCC currently serves as the primary federal regulator for national banks, federal savings associations, and federal branches

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<sup>26</sup> EDWARD V. MURPHY, CONG. RESEARCH SERV., R43087, WHO REGULATES WHOM AND HOW? AN OVERVIEW OF U.S. FINANCIAL REGULATORY POLICY FOR BANKING AND SECURITIES MARKETS (2015), <https://fas.org/sgp/crs/misc/R43087.pdf>.

<sup>27</sup> *Id.*

<sup>28</sup> *See generally* OFFICE OF THE COMPTROLLER OF THE CURRENCY, NATIONAL BANKS AND THE DUAL BANKING SYSTEM, (Sept. 2003), <https://www.occ.treas.gov/publications/publications-by-type/other-publications-reports/national-banks-and-the-dual-banking-system.pdf> [hereinafter *National Banks and the Dual Banking System*].

<sup>29</sup> *Id.*



of foreign banks<sup>30</sup> and has the power to grant charters for those companies under the National Bank Act<sup>31</sup> and Home Owners' Loan Act.<sup>32</sup> Banks that elect state charters are regulated by their state-level regulator and also by a federal regulator: either the Federal Reserve Board ("FRB") for state banks that are members of the Federal Reserve System, or Federal Deposit Insurance Corporation ("FDIC") for state non-member banks.<sup>33</sup> The OCC conducts examinations by analyzing loan and investment portfolios, capital, assets, funds management, earnings, liquidity, and sensitivity to market risk.<sup>34</sup> Additionally, the OCC can take supervisory enforcement action against any bank it supervises that does not comply with the law or regulations issued by the OCC in the form of monetary penalties or required remedial actions.<sup>35</sup>

The OCC has the power to grant charters for national banks under the National Bank Act,<sup>36</sup> and will approve charter proposals that "will provide fair access to financial services; will ensure compliance with laws and regulations; will promote fair treatment

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<sup>30</sup> *About the OCC*, OFFICE OF THE COMPTROLLER OF THE CURRENCY, <https://www.occ.gov/about/what-we-do/mission/index-about.html> (last visited Mar. 4, 2017) [hereinafter *About the OCC*].

<sup>31</sup> See 12 U.S.C. § 38 (2012).

<sup>32</sup> See 12 U.S.C. §§ 1, 1461 (2012). The OCC also has authority, under the International Banking Act, 12 U.S.C. § 3102, to license a foreign bank to operate a federal branch or agency in the United States. See *Exploring Special Purpose National Bank Charters for Fintech Companies*, *supra* note 19.

<sup>33</sup> See generally *Who Regulates My Bank?*, OFFICE OF THE COMPTROLLER OF THE CURRENCY, <https://www.helpwithmybank.gov/national-banks/national-banks.html>, (last visited Mar. 4, 2017) [hereinafter *Who Regulates My Bank?*].

<sup>34</sup> *About the OCC*, *supra* note 30.

<sup>35</sup> *Enforcement Actions*, OFFICE OF THE COMPTROLLER OF THE CURRENCY, <https://www.occ.gov/topics/laws-regulations/enforcement-actions/index-enforcement-actions.html> (last visited Mar. 4, 2017) [hereinafter *Enforcement Actions*]; see also 12 U.S.C. §§ 1818 (2012) (Cease and Desist Orders), 1818(i)(2) (Civil Money Penalty Orders), 1831o (2012) (Prompt Corrective Action Directives).

<sup>36</sup> OFFICE OF THE COMPTROLLER OF THE CURRENCY, COMPTROLLER'S LICENSING MANUAL: CHARTERS 50 (2016), <https://www.occ.gov/publications/publications-by-type/licensing-manuals/charters.pdf> [hereinafter *Comptroller's Licensing Manual: Charters*].

of customers; and will foster healthy competition.”<sup>37</sup> The OCC considers whether the proposed bank has competent management, sufficient capital, will be operated in a safe and sound manner, poses acceptable risk to the Federal Deposit Insurance Fund, and demonstrates that its corporate powers are consistent with the purposes of federal savings associations,<sup>38</sup> federal savings banks,<sup>39</sup> or national banks.<sup>40</sup> The OCC has stated that “the business of banking develops over time as the economy and business methods evolve,”<sup>41</sup> and also has the authority to determine what activities are permissible for national banks.<sup>42</sup> Specifically, the OCC believes that it “has the legal authority to construe these activities to include bank-permissible, technology-based innovations in financial services.”<sup>43</sup>

In the aftermath of the 2008 financial crisis, Congress passed the Dodd–Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”) “[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system. . . .”<sup>44</sup> The Act implemented changes affecting the oversight and supervision of financial institutions, created the

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<sup>37</sup> *Id.*

<sup>38</sup> *See generally* 12 U.S.C. § 1464 (2012).

<sup>39</sup> *Id.*

<sup>40</sup> *See* 12 C.F.R. § 5.20(e), (f) (2017) (outlining factors the OCC considers when reviewing a charter application).

<sup>41</sup> *Exploring Special Purpose National Bank Charters for Fintech Companies*, *supra* note 19.

<sup>42</sup> *See generally* *NationsBank of N.C., v. Variable Annuity Life Ins. Co.*, 513 U.S. 251 (1995); *M&M Leasing Corp. v. Seattle First Nat’l Bank*, 563 F.2d 1377 (9th Cir. 1977), *cert. denied*, 436 U.S. 987 (1978); OFFICE OF THE COMPTROLLER OF THE CURRENCY, OCC CONDITIONAL APPROVAL NO. 267 (January 12, 1998), <https://www.occ.gov/static/bit/ca267.pdf> (certification authority and repository and key escrow are part of the business of banking); OFFICE OF THE COMPTROLLER OF THE CURRENCY, OCC INTERPRETIVE LETTER NO. 494 (Dec. 20, 1989) (allowing national banks to purchase and sell financial futures for their own account).

<sup>43</sup> *Id.*

<sup>44</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376, 1376 (2010).

Consumer Financial Protection Bureau (“CFPB”),<sup>45</sup> provided for a new resolution procedure for large financial companies, and reformed the regulation of credit rating agencies.<sup>46</sup> While many of the changes made by Dodd-Frank did not directly affect special purpose charters or financial technology companies, the Act signaled a renewed focus on protecting the stability of the financial system and ensured that large institutions or new products could not have a destabilizing effect on the economy.<sup>47</sup> Increased concerns about stability may cause some regulators in the financial services industry to see new, untested products or financial entities as a risk to that stability, especially if they could affect the financial industry on a national level.<sup>48</sup> This perspective could generate opposition to the potential entry of fintech companies into the federal banking system. However, the former chief counsel of the OCC believed that current institutions will recognize the value of competition, and “balance their support for technical innovation” with “safety-and-soundness-based caution.”<sup>49</sup>

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<sup>45</sup> The CFPB is a federal agency responsible for implementing and enforcing compliance with consumer finance laws. See *The Bureau*, CONSUMER FINANCE PROTECTION BUREAU, <https://www.consumerfinance.gov/about-us/the-bureau/> (last visited Mar. 28, 2017).

<sup>46</sup> *The Dodd-Frank Act: A Cheat Sheet*, MORRISON & FOERSTER (2010), <http://media.mofo.com/files/uploads/Images/SummaryDoddFrankAct.pdf>.

<sup>47</sup> Federal Reserve Board Chair Janet Yellen recently remarked, “Dodd-Frank placed considerable emphasis on financial stability . . .” and also affirmed that the recent financial crisis has led to a higher priority on safeguards and supervisions that result in a “. . . safer and sounder financial system.” Amanda Schiavo, *Fed Chair Yellen Why Banks Need Dodd-Frank*, THE STREET (Nov. 17, 2016), <https://www.thestreet.com/story/13898085/1/fed-chair-janet-yellen-i-think-dodd-frank-was-very-important.html>.

<sup>48</sup> See, e.g., Szu Ping Chan, *Fintech ‘Boom’ Risks Fresh ‘Bust’ If Left Unchecked, Warns Carney*, THE TELEGRAPH (Jan. 25, 2017), <http://www.telegraph.co.uk/business/2017/01/25/fintech-boom-risks-fresh-bust-left-unchecked-warns-carney/> (arguing global regulators should monitor developments in fintech closely to avoid boom and bust cycles).

<sup>49</sup> Gregory Roberts, *Ex-OCC Counsel Predicts Caution From Regulators on Fintech*, BLOOMBERG BNA (June 9, 2016), <https://www.bna.com/exocc-counsel-predicts-n57982073852/>. Julie Williams served as chief counsel for the OCC for nineteen years before leaving in 2012, and later joined Promontory Financial Group in Washington, DC. *Id.*

### B. *Special Purpose National Banks*

The OCC also offers a separate special purpose bank charter. Special purpose banks “must engage in fiduciary activities or provide at least one of following banking services: receiving deposits; paying checks; or lending money.”<sup>50</sup> On March 15, 2017, the OCC issued a document entitled “A Draft Licensing Manual Supplement for Evaluating Charter Applications from Financial Technology Companies.”<sup>51</sup> In an explanation of the document, the OCC stated that it anticipates that special purpose national banks will “elect to demonstrate that they are engaged in paying checks or lending money.”<sup>52</sup> Additionally, the OCC noted, “issuing debit cards or engaging in other means of facilitating payments electronically may be considered the modern equivalent of paying checks.”<sup>53</sup>

Traditionally the special purpose bank, while bound by many of the same restrictions on standard national bank charters, “may offer only a small number of products, target a limited customer base, incorporate nontraditional elements, or have narrowly targeted business plans.”<sup>54</sup> Whereas national banks are generally authorized by their articles of associations or charters to exercise all express or implied powers of their respective charter, the OCC may require a business seeking a special purpose charter to specify

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<sup>50</sup> Michael Nonaka, *OCC to Issue Special Purpose National Bank Charters to Fintech Companies*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REGULATION (Dec. 11, 2016), <https://corpgov.law.harvard.edu/2016/12/11/occ-to-issue-special-purpose-national-bank-charters-to-fintech-companies/>. See also 12 C.F.R. § 5.20(e)(1) (2014).

<sup>51</sup> OFFICE OF THE COMPTROLLER OF THE CURRENCY, EVALUATING CHARTER APPLICATIONS FROM FINANCIAL TECHNOLOGY COMPANIES (Mar. 2017), <https://www.occ.treas.gov/publications/publications-by-type/licensing-manuals/file-pub-lm-fintech-licensing-manual-supplement.pdf> [hereinafter *Evaluating Charter Applications from Financial Technology Companies*].

<sup>52</sup> OFFICE OF THE COMPTROLLER OF THE CURRENCY, OCC SUMMARY OF COMMENTS AND EXPLANATORY STATEMENT: SPECIAL PURPOSE NATIONAL BANK CHARTERS FOR FINANCIAL TECHNOLOGY COMPANIES (Mar. 2017), <https://www.occ.treas.gov/topics/responsible-innovation/summary-explanatory-statement-fintech-charters.pdf>.

<sup>53</sup> *Id.*

<sup>54</sup> *Comptroller’s Licensing Manual: Charters*, *supra* note 36.

in more detail the activities in which it plans to be engaged.<sup>55</sup> Businesses that are granted special purpose charters are not permitted to deviate from those activities without prior OCC approval.<sup>56</sup>

Fintech firms may be subject to other federal laws including the Bank Secrecy Act,<sup>57</sup> Electronic Funds Transfer Act,<sup>58</sup> Home Mortgage Disclosure Act,<sup>59</sup> Equal Credit Opportunity Act,<sup>60</sup> Fair Housing Act,<sup>61</sup> Fair Credit Reporting Act,<sup>62</sup> Truth in Lending Act,<sup>63</sup> and any economic sanctions levied by the Office of Foreign Assets Control.<sup>64</sup> Fintech firms that obtain a special purpose national bank charter from the OCC would be subject to laws regarding legal lending limits, restrictions on transactions with affiliates, and insider-lending requirements.<sup>65</sup> Although the OCC Whitepaper<sup>66</sup> doesn't touch upon it, special purpose national banks are "subject to the Change in Bank Control Act, which would require that any

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<sup>55</sup> David F. Freeman, Jr. et al., *OCC Unveils Its Plan to Charter FinTech Companies as Special Purpose National Banks*, ARNOLD & PORTER KAYE SCHOLER LLP (Dec. 6, 2016), <http://www.apks.com/en/perspectives/publications/2016/12/occ-unveils-its-plan-to-charter-fintech>.

<sup>56</sup> *Exploring Special Purpose National Bank Charters for Fintech Companies*, *supra* note 19.

<sup>57</sup> 31 U.S.C. §§ 5311–5330 (2012); 12 U.S.C. §§ 1818(s), 1829(b), 1951–1959; 31 C.F.R. §103 (2014); 31 C.F.R. Chapter X (2014).

<sup>58</sup> 15 U.S.C. § 1693b (2012); 12 C.F.R. § 205 (2014).

<sup>59</sup> 12 U.S.C. § 2801 (2012); 12 C.F.R. § 1003 (2014).

<sup>60</sup> 15 U.S.C. § 1691 (2012); 12 C.F.R. § 1002 (2014).

<sup>61</sup> 42 U.S.C. §§ 3601–3619 (2012); 24 C.F.R. § 100 (2014).

<sup>62</sup> 15 U.S.C. § 1681 (2012); 12 C.F.R. § 222 (2014).

<sup>63</sup> 15 U.S.C. § 1601 (2012); 12 C.F.R. § 1026 (2014).

<sup>64</sup> 31 C.F.R. Chapter V (2014).

<sup>65</sup> Lawrence D. Kaplan et al., *The OCC's Proposed Fintech Charter: If It Walks Like a Bank and Quacks Like a Bank, It's a Bank*, PAUL HASTINGS (Dec. 13, 2016), [https://www.paulhastings.com/publications-items/details/?id=2b1eeb69-2334-6428-811c-ff00004cbded#\\_edn13](https://www.paulhastings.com/publications-items/details/?id=2b1eeb69-2334-6428-811c-ff00004cbded#_edn13) (citing 12 U.S.C. § 84 (2014) and 12 C.F.R. § 32 (2012); 12 U.S.C. §§ 371c, 371c-1(2012) and 12 C.F.R. § 223 (2014); and 12 U.S.C. §§ 375a(a)–(b) (2012) and 12 C.F.R. § 215 (2014)).

<sup>66</sup> See *Exploring Special Purpose National Bank Charters for Fintech Companies*, *supra* note 19.

person acquiring control of a Fintech Bank obtain prior OCC approval after at least a 60-day public notice and comment period.”<sup>67</sup>

The most common example of an institution that is chartered under a special purpose charter is a credit card bank, which is primarily concerned with issuing credit cards and generating credit card receivables.<sup>68</sup> Credit card banks traditionally engage only in a limited amount of activities, and “offer a small number of products, target a limited customer case, incorporate nontraditional elements, or have narrowly targeted business plans.”<sup>69</sup> The Federal Reserve Board usually subjects companies that own credit card banks to additional supervision and oversight, but there are exceptions under the Competitive Equality Banking Act of 1987 (“CEBA”).<sup>70</sup> Not only must such credit card banks meet requirements for creation under the CEBA amendment<sup>71</sup> to the Bank Holding Company Act (“BHCA”),<sup>72</sup> they must also become insured depository institutions<sup>73</sup> and apply for membership in the Federal Reserve System.<sup>74</sup> Furthermore, since credit card banks are highly specialized and may pose risks that do not typically occur in consumer and commercial banking operations, the OCC may impose a number of additional requirements.<sup>75</sup> The OCC may also

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<sup>67</sup> Kaplan et al., *supra* note 65 (citing 12 U.S.C. § 1817(j) (2012); 12 C.F.R. § 5.50 (2014)).

<sup>68</sup> *Comptroller’s Licensing Manual: Charters*, *supra* note 36 at 51.

<sup>69</sup> *Id.*

<sup>70</sup> *Id.*; *see also* 12 C.F.R. 225.145 (2017).

<sup>71</sup> Competitive Equality Banking Act of 1987, PL100-86, Sect. 101, August 10, 1987, 101 Stat 552.

<sup>72</sup> *See* 12 U.S.C. § 1841(c)(2)(F) (2012).

<sup>73</sup> 12 U.S.C. § 1813(c)(2) (defining insured depository institutions as “any bank or savings association the deposits of which are insured by the Corporation pursuant to this chapter”).

<sup>74</sup> *Comptroller’s Licensing Manual: Charters*, *supra* note 36; *see* 12 C.F.R. § 225.145 (2017).

<sup>75</sup> Those requirements can include maintaining a specific minimum capital floor, a certain percentage of tier 1 capital (leverage ratio), and developing a business contingency plan in case the bank does not achieve original business plan results. *See Comptroller’s Licensing Manual: Charters*, *supra* note 36; 12

require an operating agreement between the special purpose bank and the OCC establishing minimum requirements regarding capital, liquidity, corporate governance, risk-management, and other items.<sup>76</sup>

### *C. Special Purpose Bank Charters for Fintech Companies*

In light of the substantial historical background of special purpose banks, the OCC “views the National Bank Act as sufficiently adaptable to permit national banks—full-service or special purpose—to engage in new activities as part of the business of banking or to engage in traditional activities in new ways.”<sup>77</sup> In its recent white paper on potential charters for fintech businesses, the OCC notes that special purpose banks are subject to the same laws, regulations, examination, reporting requirements, and ongoing supervision as national banks.<sup>78</sup> Additionally, state law applies to special purpose banks to the same extent as to national banks, and including limits on state visitorial authority.<sup>79</sup> While the OCC is the primary federal regulator, all national banks are required to be members of the Federal Reserve System.<sup>80</sup> If fintech companies were to become chartered national banks, statutes and regulations enforced by the Federal Reserve Board on member banks would also apply to fintech firms.<sup>81</sup> The Bank Holding Company Act (“BHCA”) could also apply to a fintech company in

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U.S.C. § 1818 (2012) (termination of status as insured depository institution); 12 C.F.R. § 225.145 (2017).

<sup>76</sup> See *Comptroller’s Licensing Manual: Charters*, *supra* note 36 at 54; see 12 C.F.R. § 225.145 (2017).

<sup>77</sup> *Comptroller’s Licensing Manual: Charters*, *supra* note 36. See, e.g., 12 CFR § 7.5002 (OCC regulation authorizing national banks to use electronic means to conduct activities they are otherwise authorized to conduct, subject to appropriate safety and soundness and compliance standards and conditions).

<sup>78</sup> *Comptroller’s Licensing Manual: Charters*, *supra* note 36.

<sup>79</sup> *Id.* However, this second statement about state visitorial power may be less likely in light of *Cuomo v. Clearing House Ass’n, L.L.C.*, 557 U.S. 519, 523, 129 S. Ct. 2710, 2714 (2009).

<sup>80</sup> See 12 U.S.C. § 222 (2012).

<sup>81</sup> For example, the Federal Reserve Act imposes quantitative and qualitative restrictions on a member bank’s transactions with its affiliates. See 12 U.S.C. §§ 371c–371c-1 (2012).

the business of offering consumer financial products that has a corporate structure that includes parents and subsidiaries.<sup>82</sup> Accordingly, the BCHA would apply “if [the parent company] 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.”<sup>83</sup> However, similar to credit card banks that were exempted from the BHC, fintech firms under a special purpose national bank charter could similarly be exempted.<sup>84</sup> The OCC notes that other regulators such as the FDIC and CFPB may supervise national banks, which would work in tandem to regulate the special purpose bank.<sup>85</sup>

Some industry bodies have voiced opposition to the OCC’s potential move to grant charters to fintech companies, with most complaints coming from the Conference of State Bank Supervisors (“CSBS”), an organization of state bank regulators.<sup>86</sup> The CSBS argues to the OCC that Section 5.20(e)(1)(i) of the OCC’s chartering regulations “exceeds the statutory limits of the OCC’s chartering authority by authorizing the OCC to charter an

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<sup>82</sup> See Lawrence D. Kaplan et al., *The OCC’s Proposed Fintech Charter: If It Walks Like a Bank and Quacks Like a Bank, It’s a Bank*, PAUL HASTINGS (Dec. 13, 2016), <https://www.paulhastings.com/publications-items/details/?id=2b1eeb69-2334-6428-811c-ff00004cbded>.

<sup>83</sup> Michael Nonaka, *OCC to Issue Special Purpose National Bank Charters to Fintech Companies*, HARV. L. SCH. FORUM ON CORP. GOVERNANCE & FIN. REGULATION (Dec. 11, 2016), <https://corpgov.law.harvard.edu/2016/12/11/occ-to-issue-special-purpose-national-bank-charters-to-fintech-companies/>.

<sup>84</sup> See Competitive Equality Banking Act of 1987, PL100-86, Sect. 101, August 10, 1987, 101 Stat 552 (exempting credit card banks from BHCA coverage); For a more in-depth discussion of the BHCA treatment of fintech firms chartered under a special purpose national bank charter, see Fannie Chen, *Beyond FinTech: The OCC’s Special Purpose National Bank Charter*, DAVIS POLK & WARDWELL LLP (Dec. 9, 2016), [https://www.davispolk.com/sites/default/files/2016-12-9\\_occ\\_special\\_purpose\\_national\\_bank\\_charter.pdf](https://www.davispolk.com/sites/default/files/2016-12-9_occ_special_purpose_national_bank_charter.pdf).

<sup>85</sup> *Comptroller’s Licensing Manual: Charters*, *supra* note 36, at 6–8.

<sup>86</sup> Jim Kurtze, *Statement by the Conference of State Bank Supervisors on Comptroller’s Announcement of New Federal Charters*, CONFERENCE OF STATE BANK SUPERVISORS (Dec. 12, 2016), <https://www.csbs.org/news/press-releases/pr2016/Pages/120216.aspx>.



institution that engages exclusively in non-depository core banking functions—whether lending money and/or paying checks.”<sup>87</sup> Additionally, the CSBS maintains that “the creation of a new charter type for an institution engaged exclusively in lending money or paying checks would massively preempt otherwise applicable State licensing and consumer protection laws,”<sup>88</sup> which is a key benefit from the perspective of fintech firms. These arguments<sup>89</sup> could signal the possibility of a legal challenge to any OCC attempt to grant charters to fintech companies, which could considerably delay any possibility of a charter being awarded to any interested fintech company. Any legal challenge could tie up the OCC in months or years of litigation, which would forestall or prevent the OCC’s rollout of an OCC charter and would leave fintech firms in an uncertain position while attempting to navigate a fragmented regulatory scheme. Additionally, the Trump administration will appoint a new Comptroller of the Currency in April 2017, and that individual may be more persuaded by the states’ rights argument.<sup>90</sup>

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<sup>87</sup> John W. Ryan, *Receiverships for Uninsured National Banks, Proposed Rule; Docket ID OCC-2016-0017*, CONFERENCE OF STATE BANK SUPERVISORS (Nov. 14, 2016), <https://www.csbs.org/regulatory/policy/Documents/2016/CSBS%20Comment%20Letter%20on%20OCC%20Receiverships%20for%20Uninsured%20National%20Banks%20NPRM.pdf>. At least one court has taken a similar position. See *Independent Bankers Ass’n of America v. Conover*, 1985 U.S. Dist. LEXIS 22529, at \*34 -36 (M.D. Fla. Feb. 15, 1985) (*IBAA v. Conover*) (holding that an institution which does not engage in both accepting deposits and making loans cannot be chartered as a national bank because it would not be engaged in the “business of banking” within the meaning of the National Bank Act).

<sup>88</sup> Ryan, *supra* note 87.

<sup>89</sup> See, e.g., Joel Stashenko, *NY Regulator Slams Plan for Federal Fintech Bank Charter*, N.Y. L. J. (Jan. 18, 2017), [www.newyorklawjournal.com/home/id=1202777069796/NY-Regulator-Slams-Plan-for-Federal-Fintech-Bank-Charter?mcode=1202617075062&curindex=0&slreturn=20170018213441](http://www.newyorklawjournal.com/home/id=1202777069796/NY-Regulator-Slams-Plan-for-Federal-Fintech-Bank-Charter?mcode=1202617075062&curindex=0&slreturn=20170018213441).

<sup>90</sup> See Liz Hoffman et al., *Steven Mnuchin’s OneWest Lieutenant Is Considered for Comptroller Job*, WALL STREET J. (Feb. 16, 2017), <https://www.wsj.com/articles/steven-mnuchins-onewest-lieutenant-is-considered-for-comptroller-job-1487208755>.

### III. THE CURRENT REGULATORY LANDSCAPE FOR FINTECH FIRMS

Without the option to apply for a national charter, fintech firms that want to operate in different states across the country (to say nothing of international markets) are required to sort through both federal and state regulatory schemes.<sup>91</sup> While the dual-charter system usually allows for financial institutions to benefit from a coherent regulatory framework at one level or the other, fintech companies are forced to deal with regulations and laws at both levels.<sup>92</sup> This complexity makes it difficult for fintech companies to create coherent policies and practices in short periods of time, especially given the limited budget or small size of many young fintech firms and the cost and complexity of creating those policies.<sup>93</sup> Additionally, many of the applicable regulations were created before today's Internet dependent world, which poses another obstacle for companies attempting to grow and scale products. Fintech firms have attempted to navigate this complex landscape through a variety of approaches, including bank partnerships, hiring senior ex-regulators, and utilizing new regulation technology tools.<sup>94</sup> This section will provide an overview of the ways fintech firms currently attempt to deal with

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<sup>91</sup> SEC Commissioner Michael Piowar recently observed that innovation in the U.S. is often hindered by a fragmented “alphabet soup” regulatory structure. Tom Zanki, *SEC Chair Says Investors Need Info For Fintech To Flourish*, LAW 360 (Nov. 14, 2016), <https://www.law360.com/articles/862229/sec-chair-says-investors-need-info-for-fintech-to-flourish> Piowar also said that, “The great potential of fintech should not be hindered by our current regulatory structure.” *Id.*

<sup>92</sup> See Brian Knight, *Why State-by-State Fintech Oversight Doesn't Work*, MERCATUS CTR., GEORGE MASON U. (Sept. 6, 2016), [https://www.mercatus.org/expert\\_commentary/why-state-state-fintech-oversight-doesnt-work](https://www.mercatus.org/expert_commentary/why-state-state-fintech-oversight-doesnt-work) [hereinafter Knight, *Why State-by-State Fintech Oversight Doesn't Work*].

<sup>93</sup> See *id.* (complying with state by state regulation is expensive and time consuming, and “a massive disadvantage to young companies trying to compete with incumbents”).

<sup>94</sup> See generally Peter Rudegeair, *Online Lender Avant Names Sheila Bair to Board*, WALL STREET J., Apr. 1, 2016, <https://www.wsj.com/articles/online-lender-avant-names-sheila-bair-to-board-1459503001>.

regulatory issues, a more detailed analysis of the issues facing fintech firms and the financial industry as a whole, and conclude with an analysis of the benefits and drawbacks of the current regulatory landscape.

*A. Overview of Current Approaches to Regulatory Challenges*

Most fintech firms are startup companies funded by venture capital firms or other private funding options.<sup>95</sup> Their goal is to innovate in a segment of the financial sector like peer-to-peer payments or lending.<sup>96</sup> However, this means that the teams attempting to create a regulatory compliance model for their companies are often small compared to the vast resources available to more traditional financial institutions.<sup>97</sup> The current regulatory system requires varied approaches for the different industries in which the fintech companies exist. While financial technology includes everything from insurance to crowd funding, the majority of current regulatory concern seems focused on lending.<sup>98</sup> Consumer advocates, in addition to federal and state regulators, are especially concerned about the potential for unfair, deceptive, or abusive lending practices that have been present in other industries.<sup>99</sup> In the aftermath of Dodd-Frank, significant regulatory

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<sup>95</sup> See Vitas Argimon, *The New Wave of Partnership Models Between Banks and Fintech Startups*, CTR. FOR FIN. INCLUSION (Sept. 8, 2016), <https://cfi-blog.org/2016/09/08/the-new-wave-of-partnership-models-between-banks-and-fintech-startups/>.

<sup>96</sup> *Regulatory Guidance Regarding FinTech Products and Services*, SULLIVAN & CROMWELL, LLP (Apr. 5, 2016), [https://www.sullcrom.com/siteFiles/Publications/SC\\_Publication\\_Regulatory\\_Guidance\\_Regarding\\_FinTech\\_Products\\_and\\_Services.pdf](https://www.sullcrom.com/siteFiles/Publications/SC_Publication_Regulatory_Guidance_Regarding_FinTech_Products_and_Services.pdf).

<sup>97</sup> Nicholas Elliott, *Where Fin-Tech is Struggling with Regulation*, WALL STREET J.: RISK & COMPLIANCE J. (Nov. 24, 2015), <http://blogs.wsj.com/riskandcompliance/2015/11/24/where-fin-tech-is-struggling-with-regulation/>.

<sup>98</sup> *Id.*

<sup>99</sup> James Rufus Koren, *Online Lenders Drawing More Scrutiny by Regulators*, L.A. TIMES, Mar. 9, 2016, <http://www.latimes.com/business/la-fi-online-lending-regulations-20160309-story.html>. See James Rufus Koren, *Toyota Will Compensate Black and Asian Borrowers to Settle Bias Investigation*, L.A. TIMES, Feb. 2, 2016, <http://www.latimes.com/business/la-fi-toyota-settlement->

loopholes were closed, but the legislation also significantly increased the compliance costs of financial institutions.<sup>100</sup> This increased regulatory scrutiny, combined with an already complex regulatory scheme has led fintech companies to seek a variety of solutions in order to maintain growth and remain competitive.<sup>101</sup>

The most popular approach utilized by fintech firms involves joining forces with other banks and creating a cooperative agreement, sometimes referred to as a bank partnership.<sup>102</sup> For example, Circle Internet Financial, a digital payment company, has been forced to team up with institutions like Barclays to provide accounts for its mobile app.<sup>103</sup> While relationships like these may be less than ideal due to reliance on outside partners for business plan viability, “the bank partnership model has two big advantages if structured properly: (1) no lender licenses for the platform company and (2) interest may be charged uniformly nationwide at rates that may not be permitted for direct lenders.”<sup>104</sup> OCC regulations allow national banks “located in any state charge

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20160202-story.html (reporting that Toyota paid as much as \$21.9 million to black and Asian borrowers who paid more for auto loans than whites).

<sup>100</sup> See Bart van Liebergen, et al., *Regtech in Financial Services: Solutions for Compliance and Reporting*, INST. INT’L FIN. (Mar. 22, 2016), <https://www.iif.com/publication/research-note/regtech-financial-services-solutions-compliance-and-reporting>.

<sup>101</sup> See, e.g., Mike Whalen, *Bank Partnership or Go It Alone?*, GOODWIN PROCTER, LLP (Aug. 23, 2016), [http://www.goodwinlaw.com/viewpoints/2016/08/08\\_23\\_16-bank-partnership-or-go-it-alone](http://www.goodwinlaw.com/viewpoints/2016/08/08_23_16-bank-partnership-or-go-it-alone) (exploring bank partnerships as a potential solution for the risk posed by fintech companies acting as direct lenders).

<sup>102</sup> Alessio Botta et al., *New Partnership Models in Transaction Banking*, 8 MCKINSEY PAYMENTS 11 (May 2015), <http://www.mckinsey.com/industries/financial-services/our-insights/new-partnership-models-in-transaction-banking>. “Without national banking licenses, startups are forced either to team up with banks or scale back their ambitions.” Telis Demos and Rachel Witkowski, *States to Feds: Back Off on New Fintech Bank Plan*, WALL STREET J. (Jan. 11, 2017), <http://www.wsj.com/articles/states-to-feds-back-off-on-new-fintech-bank-plan-1484132401>.

<sup>103</sup> Witkowski & Demos, *supra* note 20.

<sup>104</sup> Whalen, *supra* note 101.  
[http://www.goodwinlaw.com/viewpoints/2016/08/08\\_23\\_16-bank-partnership-or-go-it-alone](http://www.goodwinlaw.com/viewpoints/2016/08/08_23_16-bank-partnership-or-go-it-alone).

interest at the maximum rate permitted to any state-chartered or licensed lending institution by the law of that state,” which is commonly known as interest rate exportation.<sup>105</sup> Several different kinds of cooperative approaches exist, namely outsourcing partnerships in addition to investment and acquisition agreements.<sup>106</sup> Partnerships occur when banks outsource operations, either in part (also known as white-labeling) or in full, to a fintech startup that bears the regulatory risk.<sup>107</sup> The opposite can also occur, like in the case of Circle Internet Financial, when the fintech firm takes advantage of the regulatory position of a bank. Sometimes banks use venture capital funds to encourage the development of financial technology, and invest or acquire fintech companies (or simply specific technologies or personnel).<sup>108</sup> Lastly, some banks will innovate internally, by funding and building solutions that are integrated with their other operations.<sup>109</sup>

While financial technology companies or banks may use these partnerships to gain access to new markets or continue expansion, the partnership agreements can also be established in order to protect existing relationships and customer bases.<sup>110</sup> These agreements allow banks to harmonize customer experiences and integrate platforms and processes, while dealing with the struggles that come with multiple regulatory regimes and the digitization of the financial services industry.<sup>111</sup> While bank partnerships may seem less than optimal for fintech companies, the agreements create positive benefits for both sides of the transaction.<sup>112</sup> Fintech

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<sup>105</sup> 12 C.F.R. § 7.4001(b) (2014) (authorized by 12 U.S.C. § 85 (2012)); *see also* 12 U.S.C. § 25b(f) (2012).

<sup>106</sup> Argimon, *supra* note 95 (explaining specific kinds of cooperative partnership agreements).

<sup>107</sup> *See* Botta et al., *supra* note 102.

<sup>108</sup> Argimon, *supra* note 95.

<sup>109</sup> *Id.*

<sup>110</sup> Botta et al., *supra* note 102.

<sup>111</sup> *Id.*

<sup>112</sup> *See* Rob Nichols, *Bank or No Bank, Fintech Must be Regulated*, AMERICAN BANKER (Feb. 18, 2016), <https://www.americanbanker.com/opinion/bank-or-no-bank-fintech-must-be->

operations give banks fast and iterative approaches to innovation, without the need to expend large amount of capital.<sup>113</sup> On the other side of the relationship, banks deliver fintech firms access to large customer bases, important real-world infrastructure, and big data.<sup>114</sup> Both parties benefit from improved customer experiences and trust, while cutting costs and increasing revenue in many cases.<sup>115</sup>

While bank partnerships have worked for some fintech firms, larger entities like Square, Inc. and Lending Club who may try to navigate the regulatory scheme themselves have argued “having to navigate multiple federal and state laws makes it hard for them to expand nationally.”<sup>116</sup> Others accuse fintech firms and other sharing economy companies like AirBnB and Uber of skirting long-standing regulations,<sup>117</sup> despite accommodations given by some governmental entities to allow such companies to continue operation outside historical regulatory frameworks.<sup>118</sup> Larger fintech companies have responded to increased regulatory scrutiny by hiring ex-regulators to serve in senior advisory positions,<sup>119</sup> which may provide valuable expertise as well as insight into

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regulated (“Both [banks and fintech firms] are looking for regulatory certainty and healthy cooperation — all to the good of our customers.”).

<sup>113</sup> René Lacerte, *Is 2017 The Year Bank-Fintech Partnerships Hit Product/Market Fit?*, FORBES (Feb. 13, 2017), <http://www.forbes.com/sites/forbesfinancecouncil/2017/02/13/is-2017-the-year-bank-fintech-partnerships-hit-productmarket-fit/#7fc9832a379f>.

<sup>114</sup> *Id.*

<sup>115</sup> A study by Mayer Brown surveyed seventy UK financial services providers (including banks, insurers, and asset managers), and found that 87% of respondents were able to cut costs by working with fintech providers. 54% said that partnerships had boosted revenue, while 83% said that collaborations allowed respondents to refresh their branding. *54% of Incumbents Say Fintech Partnerships Have Boosted Revenue*, BUS. INSIDER: BI INTELLIGENCE (Nov. 28, 2016), <http://www.businessinsider.com/54-of-incumbents-say-fintech-partnerships-have-boosted-revenue-2016-11>.

<sup>116</sup> Stashenko, *supra* note 89.

<sup>117</sup> Wall, *supra* note 5.

<sup>118</sup> Brittany Wallman, *Uber is Back in Broward County*, SUN SENTINEL, Oct. 15, 2015, <http://www.sun-sentinel.com/local/broward/fl-uber-final-vote-20151013-story.html>.

<sup>119</sup> See Rudegeair, *supra* note 94.

strategies to better navigate the regulatory landscape. For example, online lender SoFi brought on former Securities and Exchange Commission chairman Arthur Levitt.<sup>120</sup> Former FDIC chair Sheila Bair joined the board of directors for another lending fintech firm, Avant.<sup>121</sup> While bringing on ex-regulators may be viable for some larger fintech firms, other firms will need to look for other solutions to regulatory compliance.

### *B. Regtech as a Potential Solution for Regulatory Compliance*

While larger companies may have the structure and funding to attract senior ex-regulators,<sup>122</sup> smaller and medium size firms may find solutions in another sector of startup companies: regulation technology or “regtech.”<sup>123</sup> According to the Institute for International Finance, a research-oriented trade association in Washington, regtech is “the use of new technologies to solve regulatory and compliance requirements more effectively and efficiently.”<sup>124</sup> Kari Larsen, a former regulator at the Commodity Futures Trading Commission, described regtech as “technological

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<sup>120</sup> *SoFi Surpasses \$4 Billion in Funded Loans and Adds Arthur Levitt, Former SEC Chairman, as Advisor*, SOC. FIN., INC. (Sept. 10, 2015), <https://www.sofi.com/press/sofi-surpasses-4-billion-in-funded-loans-and-adds-arthur-levitt-former-sec-chairman-as-advisor/>. SoFi noted that “Levitt will provide strategic counsel to SoFi’s executive management team as the firm moves closer to its goal of becoming the primary financial services partner for members.” *Id.*

<sup>121</sup> Rudegeair, *supra* note 94. Ms. Bair also remarked “[i]nnovation got a bad name because of some of the harmful innovations we saw during the sub-prime mortgage craze.” *Id.* While serving as the FDIC chair in 2010, the agency said that loans that Avant originated through WebBank, an FDIC-supervised bank in Salt Lake City, mislead consumers about the credit cards it had issued on behalf of another financial company. *Id.* WebBank eventually paid a \$300,000 penalty and changed its business practices, but did not admit any wrongdoing. *Id.*

<sup>122</sup> “Former U.S. Treasury Secretary Lawrence Summers is a director at LendingClub Corp., and Raj Date, who used to be the deputy director of the Consumer Financial Protection Bureau, sits on the board of Prosper Marketplace Inc.” Rudegeair, *supra* note 94.

<sup>123</sup> See Gregory Roberts, *Fintech Spawns Regtech to Automate Compliance With Regulations*, BLOOMBERG BNA (June 22, 2016), <https://www.bna.com/fintech-spawns-regtech-n57982074535/>.

<sup>124</sup> van Liebergen, *supra* note 100.

advancement that assists those focused on compliance and regulatory-related activities in their professions.”<sup>125</sup> Regtech includes technologies like machine learning and artificial intelligence to help aggregate big-data, update compliance manuals, and even model risk for bank stress testing.<sup>126</sup> The industry would not be regulated like fintech firms that directly deal with finance, but regulators could assist “in the creation of common integrated standards.”<sup>127</sup> Regtech tools can also be used to improve anti-money laundering and know-your-customer programs, as well as helping to prevent fraud and in-house violations.<sup>128</sup> Utilizing regtech and other partnerships could “becom[e] an essential element of any fintech start-up’s strategy,” thereby improving both the profitability and efficiency of those financial institutions.<sup>129</sup>

While regtech shows promise as an industry, the barriers to implementation of regtech solutions are similar to those faced by fintech firms. Restrictions on the use of data set out by data privacy laws can curb the use or sharing of certain data or create unstandardized data that cannot be aggregated and analyzed automatically.<sup>130</sup> Protecting the security and confidentiality of clients’ data is crucial for any financial institution, especially those who are seeking to establish or improve customer trust. Similar to the fintech industry, regtech firms face duplicative and overlapping regulatory schemes making it difficult to effectively partner with

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<sup>125</sup> Roberts, *supra* note 49. Ms. Larson also noted that these technologies enable “easier, swifter, more complete, more efficient [monitoring of] compliance and regulatory obligations,” and that “[i]n her experience . . . regulators are receptive to regtech innovations.” *Id.*

<sup>126</sup> *Id.*

<sup>127</sup> Imran Gulamhuseinwala et al., *Innovating with RegTech: Turning Regulatory Compliance Into a Competitive Advantage*, ERNST & YOUNG GLOBAL LIMITED 7 (2016), [http://www.ey.com/Publication/vwLUAssets/EY-Innovating-with-RegTech/\\$FILE/EY-Innovating-with-RegTech.pdf](http://www.ey.com/Publication/vwLUAssets/EY-Innovating-with-RegTech/$FILE/EY-Innovating-with-RegTech.pdf).

<sup>128</sup> Roberts, *supra* note 49.

<sup>129</sup> Marika Vilen, *Fintech Partnerships Vital for Start-up Success*, THOMSON REUTERS (Jan. 5, 2017), <https://blogs.thomsonreuters.com/financial-risk/fintech-innovation/fintech-partnerships-vital-start-success/>.

<sup>130</sup> van Liebergen, *supra* note 100, at 15.



banks.<sup>131</sup> However, a more streamlined regulatory scheme, with consistent interpretation of requirements for data protection and privacy, would make it easier for regtech firms to operate and for financial institutions to benefit from potential partnerships.<sup>132</sup>

Despite potential challenges, regtech solutions could help fintech companies—especially smaller firms—with the burden of complex regulatory compliance. Regtech will allow smaller disruptive fintech companies to assess regulatory overlaps and minimize differing interpretations of rules and regulations.<sup>133</sup> Additionally, partnerships between regtech and fintech allow for more real-time regulation management enabling companies to adopt preemptive and proactive strategies for regulatory compliance.<sup>134</sup> Not only would regtech solutions help fintech firms navigate the current regulatory landscape but they could also continue to assist fintech companies that seek a national charter, especially in regards to compliance and reporting obligations.<sup>135</sup> Regardless of the outcome of the OCC's inquiry into national charters for fintech firms, both fintech firms and other financial institutions will benefit from the clarity and control regtech provides in dealing with the cumbersome and time-consuming nature of regulation compliance.<sup>136</sup>

### *C. Challenges Created by the Current Landscape*

The current regulatory landscape requires fintech firms to navigate a fluctuating and overlapping mix of federal and state regulations.<sup>137</sup> Without the benefit of preemption provided by a national charter,<sup>138</sup> fintech companies currently have to comply

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<sup>131</sup> *Id.* at 22.

<sup>132</sup> *Id.* at 24.

<sup>133</sup> Gulamhuseinwala et al., *supra* note 127.

<sup>134</sup> *Id.*

<sup>135</sup> See Sean Smith, *RegTech is the New FinTech*, DELOITTE (2016), <https://www2.deloitte.com/ie/en/pages/financial-services/articles/RegTech-is-the-new-FinTech.html>.

<sup>136</sup> *See id.*

<sup>137</sup> *See supra* Part III, Section A.

<sup>138</sup> For an explanation of federal and state charter preemption issues in the context of regional and community banks utilizing fintech online delivery

with different regulations in every state in which they want to operate.<sup>139</sup> Attempting to maintain growth and compliance across multiple states poses multiple challenges due to expense, dependence on other financial institutions, and constantly fluctuating regulations.<sup>140</sup> While some solutions exist to mitigate these challenges,<sup>141</sup> they still pose a major threat to the viability and success of the financial technology sector.

The complicated regulatory landscape is unfriendly to fintech firms primarily because compliance is difficult and a burden on company time and resources.<sup>142</sup> Receiving lender licenses from all the states can cost up to \$500,000 and take over a year,<sup>143</sup> which may be too high for many smaller startups to effectively afford. Many young companies may be unable to reach a point of viability or attract interest from outside investors before the costs of regulatory compliance doom the enterprise.<sup>144</sup> These startups may instead be forced to expand launch windows and “internal compliance reviews while lawyers try to apply regulatory guidance from traditional financial services to new and disruptive technologies.”<sup>145</sup> Even within a single regulatory agency, there may

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systems, see generally Greg Omer, *Fintech: Internet Banking Across State Borders Triggers Compliance Challenges for State Banks*, THOMPSON COBURN LLP (Jan. 20, 2017), <http://www.thompsoncoburn.com/insights/blogs/bank-check/post/2017-01-20/fintech-internet-banking-across-state-borders-triggers-compliance-challenges-for-state-banks>.

<sup>139</sup> See Knight, *Why State-by-State Fintech Oversight Doesn't Work*, *supra* note 92.

<sup>140</sup> See *id.* (noting that differences in state law can in some cases cause lenders seeking state-by-state compliance to not lend in states with interest and fee limitations).

<sup>141</sup> See *supra* Part III, Section A.

<sup>142</sup> Knight, *Why State-by-State Fintech Oversight Doesn't Work*, *supra* note 92.

<sup>143</sup> Whalen, *supra* note 96.

<sup>144</sup> See Knight, *Why State-by-State Fintech Oversight Doesn't Work*, *supra* note 92. (“Rather than dealing with the hassle and expense, some firms just give up. Consumers end up paying more or missing out on products and services altogether.”).

<sup>145</sup> Samuel G. Kramer, *Emerging Regulatory Framework of FinTech in the U.S.*, BAKER MCKENZIE (May 27, 2016),

be inconsistent guidance between regulations, rules, operating circulars, and policies, and as a result, fintech firms may have difficulty determining what guidance is controlling.<sup>146</sup> Those same inconsistencies make it increasingly burdensome for fintech companies simply to track changes in all fifty states and the federal government and, moreover, to adapt their products and services to fit those new requirements.<sup>147</sup>

Aside from the regulatory mire, excitement about innovation has chilled in the aftermath of the financial crisis.<sup>148</sup> Financial innovation was once viewed positively, as “new techniques and products made America’s financial system more resilient.”<sup>149</sup> However, the more recent prevailing view is that innovations like securitization<sup>150</sup> exacerbated the financial crisis by “making instruments too complex to value” through concentration of value while spreading uncertainty over where toxic assets were located.<sup>151</sup> This cautionary view has persisted and has even been

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<http://www.lexology.com/library/detail.aspx?g=dd2b13d4-7cea-4ae1-8036-4dcbb6364a43>.

<sup>146</sup> Nicholas Elliot, *Where Fin-Tech is Struggling with Regulation*, WALL STREET J. (Nov. 24, 2015, 1:28 PM), <http://blogs.wsj.com/riskandcompliance/2015/11/24/where-fin-tech-is-struggling-with-regulation/>.

<sup>147</sup> See Knight, *Why State-by-State Fintech Oversight Doesn’t Work*, *supra* note 92.

<sup>148</sup> See Felix Salmon, *How Financial Innovation Causes Crisis*, REUTERS NEWS AGENCY (Apr. 11, 2010), <http://blogs.reuters.com/felix-salmon/2010/04/11/how-financial-innovation-causes-crises/>.

<sup>149</sup> *Such Seething Brains, Such Shaping Fantasies*, ECONOMIST, Feb. 25–Mar. 2, 2012, <http://www.economist.com/node/21548232> (“True, financial creativity is often put to unproductive ends—gaming capital regulations, for example—but it is also needed to solve genuinely big problems.”) [hereinafter *Such Seething Brains, Such Shaping Fantasies*].

<sup>150</sup> Securitization is the bundling of mortgages into securities that were sold to investors. This bundling of underlying assets diversified and dispersed risks, but may have also weakened lenders’ incentives to screen out bad borrowers and to renegotiate bad loans. Edward L. Glaeser, *Debating the Securitization of Mortgages*, N.Y. TIMES: ECONOMIX (July 27, 2010, 6:00 AM), [https://economix.blogs.nytimes.com/2010/07/27/debating-the-securitization-of-mortgages/?\\_r=0](https://economix.blogs.nytimes.com/2010/07/27/debating-the-securitization-of-mortgages/?_r=0).

<sup>151</sup> *Such Seething Brains, Such Shaping Fantasies*, *supra* note 149.

applied to innovations coming from financial technology companies.<sup>152</sup> The introduction of new financial instruments and services poses a challenge for regulators and financial institutions alike. A lack of market history makes it difficult for the market and regulators to set benchmarks for the risk associated with new products or services.<sup>153</sup> While some senior regulators and politicians have expressed willingness to foster innovation and growth,<sup>154</sup> the current climate is not welcoming to expanding fintech services.

The difficulties that the crypto-currency industry encounters serve as a perfect example of the dysfunction of the current state-by-state compliance requirements. Companies that transmit virtual currency “typically have to first register as money transmitters in each jurisdiction they want to operate in and second create a single business model that complies with varying standards for factors like net worth, bonding, and investor due diligence.”<sup>155</sup> In order to have the knowledge and resource to comply with the varied state requirements, fintech companies are forced to partner with

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<sup>152</sup> See, e.g., Szu Ping Chan, *Fintech “Boom” Risks Fresh “Bust” if Left Unchecked, Warns Carney*, TELEGRAPH (Jan. 25, 2017, 5:50 PM), <http://www.telegraph.co.uk/business/2017/01/25/fintech-boom-risks-fresh-bust-left-unchecked-warns-carney/> (“Global regulators must monitor developments in fintech closely in order to avoid the ‘boom’ and ‘bust’ cycles that have characterized previous advances in financial innovation.”).

<sup>153</sup> *Financial Innovation & Crises: An Executive Summary of Conference Papers*, FEDERAL RESERVE BANK OF ATLANTA (May 2009), <https://frbatlanta.org/-/media/documents/news/conferences/2009/financial-markets-conference/conference-summary.pdf>.

<sup>154</sup> See Aaron Klein & Nicholas Montalbano, *FinTech: How Can Government Promote the Good and Protect Against the Bad?*, BROOKINGS INSTITUTE (Feb. 14, 2017), <https://www.brookings.edu/blog/up-front/2017/02/14/fintech-how-can-government-promote-the-good-and-protect-against-the-bad> (summarizing a Brookings Institute moderated panel of government officials and financial industry representative that proposed actions to boost innovation and growth include enacting real-time payments, increasing access to IRS data, and even allowing the OCC fintech charter).

<sup>155</sup> Lalitla Clozel, *When Will Fintech Grow Up*, AM. BANKER (Oct. 5, 2016, 6:00 AM), <https://www.americanbanker.com/news/when-will-fintech-regulation-grow-up>.

traditional banks, which threatens to stifle fintech companies by forcing them to rely too heavily on traditional banking institutions.<sup>156</sup> According to Circle Chief Executive Jeremy Allaire, many fintech firms would welcome a federal banking charter, as it would take “a lot of the cost and complexity of working with many third parties out of the equation.”<sup>157</sup> Federal regulators have grown increasingly concerned about these third-party relationships, and the inability to understand certain technical innovations only made it more difficult to police those relationships.<sup>158</sup>

The inconsistencies and differences that exist among the states fracture the national market,<sup>159</sup> which is extremely frustrating for companies whose ability to offer low margin products relies in part on their services being accessible to anyone with an internet connection.<sup>160</sup> The need to simultaneously fulfill requirements in so many jurisdictions hampers fintech companies’ ability to innovate and grow.<sup>161</sup> In addition, consumers who are pushed away from the mainstream financial system often seek less regulated, “alternative financial products that charge exorbitant fees.”<sup>162</sup> This situation creates negative effects for both consumers and regulatory agencies concerned with money-laundering and other types of fraud.<sup>163</sup>

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<sup>156</sup> *Id.*

<sup>157</sup> Witkowski & Demos, *supra* note 20.

<sup>158</sup> Roberts, *supra* note 49.

<sup>159</sup> Knight, *Why State-by-State Fintech Oversight Doesn’t Work*, *supra* note 92.

<sup>160</sup> See Miklos Dietz et al., *Cutting Through the Noise Around Financial Technology*, MCKINSEY & COMPANY (Feb. 2016), <http://www.mckinsey.com/industries/financial-services/our-insights/cutting-through-the-noise-around-financial-technology>.

<sup>161</sup> See Knight, *Why State-by-State Fintech Oversight Doesn’t Work*, *supra* note 92.

<sup>162</sup> Patricia Hart, *Banks Are Right To Be Afraid of the FinTech Boom*, TIME (Dec. 12, 2016), <http://time.com/3949469/financial-technology-boom/>.

<sup>163</sup> See Jim Sivon, *FinTech and the Existing Legal Framework for Anti-Money Laundering and Counter-Terrorism Financing*, BARNETT SIVON & NATTER (June 2015), [http://www.bsnlawfirm.com/newsletter/OP1506\\_Sivon.pdf](http://www.bsnlawfirm.com/newsletter/OP1506_Sivon.pdf).

Lastly, state-by-state regulation means that firms forced to comply with the laws of one state “may not offer a particular product anywhere in response to one state’s ban, even if other states would welcome the product.”<sup>164</sup> As a result, lucrative markets like New York or California could “set the regulatory tone” for the rest of the country, assuming that a particular product was already approved in other states. This could deprive citizens of the ability to hold policymakers accountable for poor regulatory choices if they do not happen to live in a lucrative market.<sup>165</sup> If lucrative markets are allowed to functionally dictate stringent requirements across the country, the overregulation could reduce the financial products available in small states.<sup>166</sup> This outcome would reduce competition in those markets as well as ensure that unbanked consumers remain unbanked.

#### *D. Pros and Cons of the Current Regulatory Scheme*

The current system of regulatory schemes for fintech firms errs on the side of caution instead of promoting growth and fostering innovation. The system does allow for both companies and states to experiment and tinker with different regulations and supervisory schemes in order to find a good fit that matches consumer needs and safety requirements.<sup>167</sup> This system also provides more accountability for lawmakers who will have more direct accountability to the citizens of their own states.<sup>168</sup> State agencies are, traditionally, geographically closer to the entities they regulate, but the lower number of institutions that they oversee means that more time and attention could be spent on ensuring that fintech firms receive the guidance and advice necessary to help

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<sup>164</sup> Knight, *Why State-by-State Fintech Oversight Doesn’t Work*, *supra* note 92.

<sup>165</sup> *Id.*

<sup>166</sup> *Id.*

<sup>167</sup> “As State regulators continue to work to foster a regulatory and supervisory environment which promotes innovative practices in the delivery of financial services . . . .” Ryan, *supra* note 87.

<sup>168</sup> *But see* Knight, *Why State-by-State Fintech Oversight Doesn’t Work*, *supra* note 92.

them thrive.<sup>169</sup> However, since most fintech firms only have a physical presence in one or two locations, this benefit would only exist if firms established liaisons in each state. Traditionally, states also have higher standards for consumer protection, and state regulators have voiced concerns that a national charter could preempt state-level consumer protection laws.<sup>170</sup> At the federal level, the CFPB currently adopts regulations regarding consumer finance and enforces federal consumer financial laws through legal action.<sup>171</sup> As noted before, the current legislative approach is fractured but places a high emphasis on financial stability and consumer protection and allows a more tailored approach.<sup>172</sup>

Despite the numerous positive characteristics of the current scheme of regulation for fintech firms, there are a multitude of negative factors that create an environment that is ultimately hostile to emerging companies. The primary obstacle is the splintered nature of the current landscape, as companies are unable to find a clear set of rules by which to operate, and instead are forced to navigate fifty states-worth of regulations.<sup>173</sup> The energy and time required to deal with the multitude of schemes pulls resources away from research and development. Those efforts could instead be devoted to creating new financial products and improving current ones, which would amplify the already positive impact of fintech firms. Some experts allege that some fintech firms have even decided that a lack of meaningful federal oversight means that it is more advantageous to ignore the rules and focus on growth instead.<sup>174</sup>

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<sup>169</sup> See Ryan, *supra* note 87 (citing concerns about the risks of a larger, more risky, federal scheme).

<sup>170</sup> *Statement by the Conference of State Bank Supervisors on Comptroller's Announcement of New Federal Charters*, CSBS (Dec. 2, 2016), <https://www.csbs.org/news/press-releases/pr2016/Pages/120216.aspx>.

<sup>171</sup> CFPB, CONSUMER FINANCIAL PROTECTION BUREAU, STRATEGIC PLAN FY 2013–FY 2017 (Apr. 2013), <http://files.consumerfinance.gov/f/strategic-plan.pdf>.

<sup>172</sup> Zanki, *supra* note 91.

<sup>173</sup> Clozel *supra* note 155.

<sup>174</sup> *Id.* “‘Everybody on the road is speeding, but the question is who’s going to get pulled over and be given a ticket,’ said Carol Van Cleef, a partner at Manatt,

Access to internet-based financial solutions is also an important means of increasing financial inclusion, or allowing underserved communities to access lending and payment options that are not often offered by traditional banking services due to margins and risk.<sup>175</sup> According to the World Bank's Findex Database, which measures financial inclusion around the world, in 2014, two billion adults worldwide did not have a bank account.<sup>176</sup> Growth of account holders in developing countries, especially in Sub-Saharan Africa, has been credited to financial technology services like mobile-based peer-to-peer payment systems.<sup>177</sup> According to a study conducted by the Gates Foundation, the Better than Cash Alliance, and the World Bank, "broader access to and participation in the financial system can reduce income inequality, boost job creation, accelerate consumption, increase investments in human capital, and directly help poor people manage risk and absorb financial shocks."<sup>178</sup> The current restriction of access to internet-based financial solutions is a large weakness of the current regulatory structure, and it limits the opportunity for the financial services to help under-developed regions of the United States.

Lastly, the ability of single states in lucrative markets to "set the regulatory tone" for the rest of the country and to dominate the landscape with restrictive regulation is a major negative of the current regulatory scheme.<sup>179</sup> Since it is impossible for fintech

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Phelps & Phillips. "We really need to rethink whether we should have those laws in place if we're not going to enforce them." *Id.*

<sup>175</sup> Knight, *Why State-by-State Fintech Oversight Doesn't Work*, *supra* note 92.

<sup>176</sup> Asli Demirguc-Kunt et al., *The Global Findex Database 2014*, WORLD BANK GRP. (Apr. 2015), <http://documents.worldbank.org/curated/en/187761468179367706/pdf/WPS7255.pdf#page=3>. 2014 is the most recent year for which data was published by the World Bank Group's Development Research Group.

<sup>177</sup> *Id.*

<sup>178</sup> Leora Klapper & Dorothe Singer, *The Opportunities of Digitizing Pay*, WORLD BANK GRP. (Aug. 24, 2014), [http://www.gatesfoundation.org/~media/GFO/Documents/What%20We%20Do/G20%20Report\\_Final.pdf](http://www.gatesfoundation.org/~media/GFO/Documents/What%20We%20Do/G20%20Report_Final.pdf).

<sup>179</sup> Knight, *Why State-by-State Fintech Oversight Doesn't Work*, *supra* note 92.



companies to avoid these markets if they want to remain profitable, they are forced to tailor their products to those markets and deprive citizens in other states of the political autonomy to affect the policies and laws that affect their lives.<sup>180</sup> Consequently, if two states' regulations or policies are in conflict, financial technology companies may well be forced to choose a state to operate in if the cost of compliance in both is impossible. This challenge is enhanced by the mobile nature of many fintech tools, where products or services are not confined by a brick-and-mortar location, and instead move freely across state lines.

In the past, some solutions have been proposed to combat the issue of the inconsistent nature of state-by-state regulation. One such example is section 203 of the Uniform Money Services Act,<sup>181</sup> which permits companies that have obtained a money transmission license under the act in one state to operate in other states that have enacted the same or similar legislation. Unfortunately, only five states have passed the legislation, which severely limits (and almost completely reduces) the effectiveness of the scheme.<sup>182</sup> Another potential solution proffered more recently is the “passporting”<sup>183</sup> of state licenses.<sup>184</sup> This policy is already available

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<sup>180</sup> *Id.*

<sup>181</sup> *Amendments to Uniform Money Services Act*, NAT'L. CONFERENCE OF COMM'RS. ON UNIFORM STATE LAWS (Aug. 6, 2004), [http://www.uniformlaws.org/shared/docs/money%20services/umsa\\_am04%20final\\_not%20styled.pdf](http://www.uniformlaws.org/shared/docs/money%20services/umsa_am04%20final_not%20styled.pdf).

<sup>182</sup> Judith Rinearson, *Payments Innovation Wars, Part II: U.S. Strikes Back*, AM. BANKER (Jan. 6, 2017), <https://www.americanbanker.com/opinion/payments-innovation-wars-part-ii-us-strikes-back-AB1093187>.

<sup>183</sup> “Passporting” allows business licenses to be recognized across state lines, much like driver's licenses. States engaged in passporting accept one state's license in their own state. See Jennifer Teshler & Jeanna Hogarth, *Comments on Exploring Special Purpose National Bank Charters for Fintech Companies*, CTR. FOR FIN. SERVS. INNOVATION (Jan. 17, 2017), <https://www.occ.gov/topics/bank-operations/innovation/comments/comment-cfsi.pdf>.

<sup>184</sup> Aaron Klein & Nicholas Montalbano, *FinTech: How Can Government Promote the Good and Protect Against the Bad?*, BROOKINGS INST. (Feb. 14, 2017), <https://www.brookings.edu/blog/up-front/2017/02/14/fintech-how-can->

in the EU, but a U.K. fintech firm will likely need two licenses in order to passport after the completion of Brexit.<sup>185</sup> While these solutions are proposals that would help alleviate many negative aspects of the current regulatory system, they would also remove the ability for states to implement protections that other states may decline to establish. Similar to the current system, single states with lucrative markets might dominate the landscape, which would not eliminate the political autonomy issue.

On balance, the negative consequences of the current regulatory system combined with the unstoppable growth of the financial technology sector means that new solutions are needed to better serve and protect consumers, as well as encourage these emerging companies to continue their growth and job creation. The current regulatory landscape may have been a better fit for pre-2007, when regulators already had a relationship with most financial institutions and could trust that they would handle innovation responsibly.<sup>186</sup> However, the current iteration of the industry is comprised of both established players such as bankers, older fintech companies, and emerging players.<sup>187</sup> As emerging players continue to expand rapidly in size, the current regulatory strategy of focusing on “too-big-to-fail” actors in order to prevent systematic threats to the industry needs to be adjusted. Regulators will have to work hard to identify non-traditional institutions that can go from “too-small-to-care” to “too-big-to-fail” in a matter of years,<sup>188</sup> if not months.<sup>189</sup> While all fintech companies are unlikely

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government-promote-the-good-and-protect-against-the-bad/. This solution was only backed by one of the panel’s six participants, while the rest did not express a positive or negative opinion. *Id.*

<sup>185</sup> Rinearson, *supra* note 182.

<sup>186</sup> Douglas Arner et al., *The Evolution of Fintech: A New Post-Crisis Paradigm*, UNIV. NEW SOUTH WALES (Oct. 20, 2015, last revised Sept. 7, 2016), [https://papers.ssrn.com/sol3/papers2.cfm?abstract\\_id=2676553](https://papers.ssrn.com/sol3/papers2.cfm?abstract_id=2676553).

<sup>187</sup> *Id.*

<sup>188</sup> For an example of how explosive fintech growth can be, Alibaba’s money fund Yu-E Bao (“Leftover Treasure”), grew from 0 to 578 billion yuan (around \$78 billion at today’s exchange rate) in less than two years. Madison Marriage, *Huge Growth in China’s Money Funds Poses Risk*, FIN. TIMES (June 14, 2015), <http://www.cnbc.com/2015/06/14/-in-chinas-money-funds-poses-risk.html>.

to reach the “too-big-to-fail” level so quickly, “in an ever interconnected financial system, market size and systemic risk are not necessarily correlated. The Dow Jones flash crash in May 2010 illustrated that smaller players can also become systemic.”<sup>190</sup> The current regulatory landscape does allow for a balance of consumer protection and experimentation, but sacrifices financial inclusivity and innovation, a trade-off that could stand to be improved.

#### IV. THE FUTURE FOR FINTECH: A NEW REGULATORY LANDSCAPE

Today’s regulatory scheme simply lags behind other countries in the way innovation is regulated,<sup>191</sup> despite initial attempts to implement regulatory sandboxes and other regulatory reforms. The President of the American Bankers Association, Rob Nichols, wrote: “Our regulators can learn much from Britain about how to stimulate new ideas from outside banking and to integrate them under a common set of regulatory expectations.”<sup>192</sup> However, the future of fintech should not be a complex reorganization of the banking system that forgoes a focus on safety and soundness for a Wild West setting full of experimentation in search of exponential profits. Instead, reasonable reforms can be made to ensure that the proper regulatory authorities provide the necessary safeguards to contain the risk of innovation, without unnecessarily stifling it. The result could be a system where banks and other financial services incumbents partner with fintech firms to generate value, while

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<sup>189</sup> The concept of “too-small-to-care” to “too-big-to-fail” was initially developed by Douglas W. Arner & Janos Barberis, *Regulating FinTech Innovation: A Balancing Act*, ASIAN INST. OF INT’L. FIN. (Apr. 1, 2015), <http://www.law.hku.hk/aiifl/regulating-fintech-innovation-a-balancing-act-1-april-1230-130-pm/>.

<sup>190</sup> Arner, *supra* note 186.

<sup>191</sup> Richard Magrann-Wells, *Fintech Firms Hurt by Lack of Regulatory Clarity*, AM. BANKER (July 18, 2016), <https://www.americanbanker.com/opinion/fintech-firms-hurt-by-lack-of-regulatory-clarity>.

<sup>192</sup> Rob Nichols, *Bank or No Bank, Fintech Must be Regulated*, AM. BANKER (Feb. 18, 2016), <https://www.americanbanker.com/opinion/bank-or-no-bank-fintech-must-be-regulated>.

increasing financial inclusion and innovation without sacrificing stability or consumer protections.

*A. The OCC as the Primary Supervisor for Fintech Firms*

The creation of a special purpose charter for fintech companies would represent a drastic change from the current regulatory landscape that confronts fintech companies. A charter granted by the OCC would allow fintech companies to avoid the current maze of regulation through the pre-emption of many state-by-state requirements.<sup>193</sup> In exchange for having to seek state-by-state approval for many financial practices, fintech companies would instead be subject to a rigorous, multi-layered scheme of federal regulation that is likely stricter than, and possibly as complex as, the state-by-state system.<sup>194</sup> This layered scheme means that the OCC would need to work in tandem with not only other federal regulators, but also with state authorities in some instances. However, in the words of the head of the Office of the Comptroller of the Currency, Thomas Curry, “[i]t will 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.”<sup>195</sup> Some industry advocates have lauded the OCC’s recent plans, noting that special purpose charters would be an “elegant way to ensure that important prudential and consumer protection standards

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<sup>193</sup> Witkowski & Demos, *supra* note 20.

<sup>194</sup> Jeffrey Hale, et al., *The OCC Confirms Special Purpose National Bank Charters for Fintech Companies*, DLA PIPER (Dec. 5, 2016), <https://www.dlapiper.com/en/us/insights/publications/2016/12/the-occ-confirms-special-purpose/>. Potential activity limitations that would be placed by the Bank Holding Company Act might go into effect if fintech companies don’t accept deposits, and therefore are not insured by the FDIC. Additionally, state laws “aimed at fair or deceptive treatment of customers” would still apply to fintech companies with a national charter, just like normal national banks. *Id.*

<sup>195</sup> Rachel Witkowski, et al., *Regulator Will Start Issuing Bank Charters for Fintech Firms*, WALL STREET J. (Dec. 2, 2016), <http://www.wsj.com/articles/regulator-will-start-issuing-bank-charters-for-fintech-firms-1480691712>.

are consistently maintained while allowing new entrants to bring valuable, innovative products to market.”<sup>196</sup>

While the OCC is the primary supervisor of national banks, it shares some responsibilities with other federal and state agencies. Some of those responsibilities have shifted in the aftermath of Dodd-Frank and recent court decisions. For example, the OCC was once thought to have exclusive visitorial powers for national banks stemming from 12 U.S.C. § 484, an interpretation once solidified in 12 C.F.R. § 7.4000.<sup>197</sup> This authority was challenged in *Cuomo v. Clearing House Ass’n, L.L.C.*,<sup>198</sup> and the U.S. Supreme Court held that a state attorney general was allowed to bring suit against national banks to enforce non-preempted state laws.<sup>199</sup> While state regulators would need to sue in order to get access to info about internal operations of national banks, the decision did signal a slight weakening of the OCC’s power over national banks.<sup>200</sup> In wake of the decision, some argued it could disrupt the “system of consistent nationwide banking regulation”<sup>201</sup> that the OCC is tasked with providing. This disruption may make entry into the national banking field less attractive for potential entrants like fintech firms, but all that can be stated for sure is that the ruling created additional tension within the national banking system.<sup>202</sup> The ruling affirms that states regulatory authorities

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<sup>196</sup> Blair Bernstein, *BAFT Releases Statement on Potential Creation of OCC Fintech Charter*, THE BANKERS ASS’N. FOR FIN. AND TRADE (Dec. 5, 2016), <https://baft.org/events/general/2016/12/05/baft-releases-statement-on-potential-creation-of-occ-fintech-charter>.

<sup>197</sup> See 12 C.F.R. § 7.4000 (2009) (interpreting 12 U.S.C. § 484 (2006)).

<sup>198</sup> *Cuomo v. Clearing House Ass’n, L.L.C.*, 557 U.S. 519, 523, 129 S. Ct. 2710, 2714 (2009).

<sup>199</sup> *Id.* at 528 n.2, 129 S. Ct. at 2717.

<sup>200</sup> See *Cuomo*, 557 U.S. at 523, 129 S. Ct. at 2714 (2009) (affirming that the OCC regulation claiming to pre-empt state law enforcement was not a reasonable interpretation of the NBA).

<sup>201</sup> Louis P. Malick, *Cuomo v. Clearing House Association, L.L.C.: States Enforcing State Laws Against National Banks*, 6 J. Bus. & Tech. L. 487, 510 (2011).

<sup>202</sup> “Although elected state attorneys general may have the best interests of their constituents at heart—if not their own self-interest in reelection—these concerns are likely to conflict with the goal of having an efficient national

maintain an important role in the policing of national banks.<sup>203</sup> For example, state regulations regarding usury, or barring loans above certain interest rates, are a bulwark against abusive lending practices that often target vulnerable populations who do not have regular access to credit.<sup>204</sup> Regardless of other regulatory authorities, the OCC remains the primary supervisor of federal banks. It is responsible for monitoring, inspecting, and examining banks to ensure that they comply with applicable rules and regulations and operate in a safe and sound manner.<sup>205</sup>

### *B. Other Agencies and Laws: Secondary Regulation*

The OCC functions as a day-to-day supervisor of national banks, but three other federal bodies serve to oversee financial activity at a higher level. First, the Federal Reserve Board (“Fed”) provides direct supervision of bank and financial holding companies,<sup>206</sup> any non-banking subsidiary not directly regulated by another state or federal regulator, and state non-member banks.<sup>207</sup> In the context of a special national bank charter, the Fed would

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banking system, especially in the current climate of popular distrust and even animosity toward banks in general.” Malick, *supra* note 201, at 509 (citing See David A. Scheffel, *The National Bank Act: So Much for Preemption*, N.Y.L.J., (Aug. 3, 2009) at 1).

<sup>203</sup> See *Cuomo*, 557 U.S. at 536, 129 S. Ct. at 2721 (state authorities can bring lawsuits to enforce state law against national banks, acting in the role of “sovereign-as-law-enforcer”).

<sup>204</sup> Witkowski & Demos, *supra* note 20.

<sup>205</sup> THE FED. RESERVE, SUPERVISING AND REGULATING FINANCIAL INSTITUTIONS AND ACTIVITIES, [https://www.federalreserve.gov/pf/pdf/pf\\_5.pdf](https://www.federalreserve.gov/pf/pdf/pf_5.pdf) (last visited Mar. 28, 2017).

<sup>206</sup> A bank holding company (“BHC”) is a corporate structure used to control a bank for regulatory and risk-separation purposes. A financial holding company (“FHC”) is a BHC that through the Gramm-Leach-Bliley Act of 1999 can engage in additional activities such as securities underwriting, insurance underwriting, and insurance agency activities. THE FEDERAL RESERVE, SUPERVISING AND REGULATING FINANCIAL INSTITUTIONS AND ACTIVITIES [https://www.federalreserve.gov/pf/pdf/pf\\_5.pdf](https://www.federalreserve.gov/pf/pdf/pf_5.pdf) (last visited Mar. 28, 2017).

<sup>207</sup> See *Bank Holding Companies and Financial Holding Companies*, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, <https://www.fedpartnership.gov/bank-life-cycle/grow-shareholder-value/bank-holding-companies#03d> (last visited Mar. 5, 2017).

likely only interact with a fintech firm on the overarching policy level. Second, the Financial Stability Oversight Council (“FSOC”) is a formal interagency body that includes federal and state regulators, as well as Fed representatives, and is tasked with identifying and responding to emerging threats to U.S. financial stability.<sup>208</sup> It is unlikely that the FSOC would have cause to interact with fintech firms unless they grew exponentially in size or were so crucial to the interconnection of financial institutions that their failure would threaten the stability of the U.S. financial system.<sup>209</sup> Lastly, the CFPB is a federal agency responsible for implementing and enforcing compliance with consumer finance laws, and overseeing financial products and services.<sup>210</sup>

The OCC works in tandem with the FDIC, which is an independent agency created by Congress to insure deposits and examine some large banking institutions such as financial holding companies.<sup>211</sup> While many of the banks that fintech companies partner with are national banks regulated by the OCC, the FDIC requires a separate application from the OCC’s chartering process in order to obtain deposit insurance.<sup>212</sup> “The FDIC requires a thorough, well-developed business plan that is ‘tailored to the institution’s size, complexity and risk profile’ and that ‘present[s] a sustainable franchise.’”<sup>213</sup> The FDIC serves as a secondary supervisor, especially for those institutions who deal in

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<sup>208</sup> See *Financial Stability Oversight Council*, U.S. DEP’T OF THE TREASURY (Apr. 18, 2016), <https://www.treasury.gov/initiatives/fsoc/Pages/home.aspx>.

<sup>209</sup> See *About FSOC*, U.S. DEP’T OF THE TREASURY (June 23, 2016), <https://www.treasury.gov/initiatives/fsoc/about/Pages/default.aspx>.

<sup>210</sup> See *The Bureau*, CONSUMER FINANCE PROTECTION BUREAU, <https://www.consumerfinance.gov/about-us/the-bureau/> (last visited Mar. 28, 2017).

<sup>211</sup> *Mission, Vision, and Values*, FED. DEPOSIT INS. CORP. (May 15, 2015), <https://www.fdic.gov/about/strategic/strategic/mission.html>.

<sup>212</sup> Franca Gutierrez, et al., *Fintech Regulation: Recent Developments and Innovations*, LAW360 (May 9, 2016, 11:01 AM), [https://www.wilmerhale.com/uploadedFiles/Shared\\_Content/Editorial/Publications/Documents/2016-05-10-Fintech-Regulation-Recent-Developments-And-Innovations.pdf](https://www.wilmerhale.com/uploadedFiles/Shared_Content/Editorial/Publications/Documents/2016-05-10-Fintech-Regulation-Recent-Developments-And-Innovations.pdf).

<sup>213</sup> *Id.*

marketplace lending, supplementing work done by the OCC.<sup>214</sup> Despite its secondary status, the FDIC has recently mentioned that the online lending activities may draw increased scrutiny, and that it may pursue enforcement actions if those activities generate too much risk.<sup>215</sup> The FDIC has recently formed committees focused on the retail and wholesale applications of fintech, suggesting that the regulator intends to be more closely involved in supervising the institutions.<sup>216</sup> Regardless of the FDIC's final role in fintech supervision, their involvement creates another element that fintech businesses will have to consider.

An important piece of legislation that fintechs may encounter is the 1977 Community Reinvestment Act ("CRA").<sup>217</sup> The CRA's purpose is "require each appropriate Federal financial supervisory agency to use its authority when examining financial institutions, to encourage such institutions to help meet the credit needs of the local communities in which they are chartered consistent with the safe and sound operation of such institutions."<sup>218</sup> The law is limited to depository intuitions, but according to an OCC spokesperson, "[t]he OCC has the ability to condition approvals (of nonbank charters) to require compliance and activities consistent with laws

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<sup>214</sup> "Online marketplace lending refers to the segment of the financial services industry that uses investment capital and data-driven online platforms to lend either directly or indirectly to consumers and small businesses." See *Opportunities and Challenges in Online Marketplace Lending*, US DEP'T OF THE TREASURY (May 10, 2016), [https://www.treasury.gov/connect/blog/Documents/Opportunities\\_and\\_Challenges\\_in\\_Online\\_Marketplace\\_Lending\\_white\\_paper.pdf](https://www.treasury.gov/connect/blog/Documents/Opportunities_and_Challenges_in_Online_Marketplace_Lending_white_paper.pdf).

<sup>215</sup> Gutierrez, *supra* note 212.

<sup>216</sup> Gregory Roberts, *Fintech Poses No. 1 Threat to Community Banks, Execs Tell FDIC*, BLOOMBERG BNA (July 22, 2016), <https://www.bna.com/fintech-poses-no-n73014445156/>.

<sup>217</sup> See 12 U.S.C. § 2901(b) (2012) (describing the CRA's purpose as requiring "require each appropriate Federal financial supervisory agency to use its authority when examining financial institutions, to encourage such institutions to help meet the credit needs of the local communities in which they are chartered consistent with the safe and sound operation of such institutions").

<sup>218</sup> See 12 U.S.C. § 2901(b) (2012).



like the CRA . . . .”<sup>219</sup> However, a key provision in the CRA means that it applies to a certain geographic area, which may require fintech banks to use “strategic plans” similar to those used by Internet banks with no physical branches.<sup>220</sup> Some industry experts have asserted that this could serve as another barrier to entry for fintech firms considering national charters.<sup>221</sup> However some politicians argue that fintech companies could reinvigorate the CRA, and stimulate a new emphasis on financial inclusion.<sup>222</sup>

Other prudential regulators, such as the CFPB and the FTC, could potentially impose additional regulation on fintech banks.<sup>223</sup> The CFPB was created by Dodd-Frank in 2010 as an independent regulatory agency with rulemaking, supervision, and enforcement authority over nearly all firms involved in consumer financial services, irrespective of their particular legal form.<sup>224</sup> The CFPB, which “aims to make consumer financial markets work for consumers and responsible providers,” recently announced a policy

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<sup>219</sup> Gregory Roberts, *Fintech Federal Charter Could Trigger Community Lending Rules*, BLOOMBERG BNA (Sept. 29, 2016), <https://www.bna.com/fintech-federal-charter-n57982077698/>.

<sup>220</sup> *Id.*

<sup>221</sup> According to Rick Eckman, a partner with Pepper Hamilton LLC in Wilmington, Del., “If they can pull your charter because some examiner doesn’t think you’ve met your CRA obligations, I’m not sure people are going to risk capital and invest in that business.” *Id.*

<sup>222</sup> Gregory W. Meeks & Cedric L. Richmond, *How OCC’s Fintech Plan Can Make CRA Relevant Again*, AMERICAN BANKER (Jan. 18, 2017, 9:40 AM), <https://www.americanbanker.com/opinion/how-occs-fintech-plan-can-make-cra-relevant-again>. Rep. Gregory W. Meeks, D-N.Y., is a senior member of the House Financial Services Committee. *Id.* Rep. Cedric Richmond, D-LA., is chair of the Congressional Black Caucus. *Id.*

<sup>223</sup> Gutierrez, *supra* note 212.

<sup>224</sup> Adam J. Levitin, *The Consumer Financial Protection Bureau: An Introduction*, 32 REVIEW OF BANKING & FIN. LAW 321, 322 (2012-2013), <https://www.bu.edu/rbfl/files/2013/10/Levitin.pdf> (citing *See About Us*, CONSUMER FIN. PROTECTION BUREAU, <http://www.consumerfinance.gov/the-bureau/> (last visited Apr. 1, 2013)); *See* 12 U.S.C. § 5511 (2012) (describing the purpose of the agency as enforcing “Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive”).

where bureau staff is allowed to issue no-action letters to applicants with proposals for innovative financial products.<sup>225</sup> The CFPB plays an important role in the oversight of consumer protection regulations, but the agencies' role could be reduced by the current Republican administration that has accused the agency of overreaching its authority.<sup>226</sup> If the CFPB were forced to reduce its activities, it would create a prime opportunity for state regulators to reassert themselves and fill the role of protecting consumers.<sup>227</sup> The FTC is likely to fill gaps in the federal regulatory scheme, but could also deploy its powerful law enforcement tools in its new focus on consumer protection risks in the fintech industry.<sup>228</sup>

Lastly, the Securities and Exchange Commission ("SEC") could make further adjustments to its crowdfunding regulations, which would affect many fintech firms whose funds come from varied sources.<sup>229</sup> The SEC's mission is to oversee "the key participants in the securities world, including securities exchanges, securities brokers and dealers, investment advisors, and mutual funds. Here, the SEC is concerned primarily with promoting the disclosure of important market-related information, maintaining fair dealing, and protecting against fraud."<sup>230</sup> The SEC has also seen an opening to regulate fintech firms, with Commissioner Michael Piwowar stating that "[he] believe[s] the commission should take the lead regulatory role in the fintech space."<sup>231</sup> Many

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<sup>225</sup> Gutierrez, *supra* note 212. (citing CFPB, CONSUMER FINANCIAL PROTECTION BUREAU, STRATEGIC PLAN FY 2013 – FY 2017 (Apr. 2013), <http://files.consumerfinance.gov/f/strategic-plan.pdf>).

<sup>226</sup> Telis Demos & Rachel Witkowski, *States to Feds: Back Off on New Fintech Bank Plan*, WALL STREET J., <http://www.wsj.com/articles/states-to-feds-back-off-on-new-fintech-bank-plan-1484132401>. (last updated Jan. 11, 2017).

<sup>227</sup> *Id.*

<sup>228</sup> Gutierrez, *supra* note 212.

<sup>229</sup> *Id.*

<sup>230</sup> *What We Do: Introduction*, U.S. SEC. AND EXCH. COMM'N, <https://www.sec.gov/about/whatwedo.shtml> (last modified June 10, 2013).

<sup>231</sup> Rob Tricchinelli, *SEC Sees Opening to Regulate Fintech Developments*, BLOOMBERG BNA (Nov. 15, 2016), <https://www.bna.com/sec-sees-opening-n57982082729/>.

fintech firms are already registered with the SEC in a variety of capacities and are familiar with the agency.<sup>232</sup> The SEC already seeks to “ensure that marketplace lending investors are given enough information to make good investment decisions,” and could regulate fintech firms that operate in marketplace lending.<sup>233</sup> This position conflicts with the OCC’s stance on the matter, but many fintech firms are already registered with the SEC in a variety of capacities.<sup>234</sup> The SEC argues that their agency has a role to play in regulating marketplace lending and firms that use distributed ledgers to facilitate financial transactions, as well as those who use automated investment advisors to give disclosures to clients.<sup>235</sup> The OCC’s chartering authority may ensure that some fintech firms fall under its purview, but it seems clear that the SEC will have at least some role in fintech’s future.

### *C. Pros and Cons of a New Landscape*

Despite the complexity that may come with fintech firms being granted special purpose charters, the potential benefits to the banking system, potential entrants, and consumers far outweigh any potential negative effects. A primary benefit of granting fintech firms access to the national regulatory scheme would be increased competition with older, more established financial firms.<sup>236</sup> While some fintech firms perceive competition with

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<sup>232</sup> *Id.*

<sup>233</sup> *Id.*

<sup>234</sup> *Id.* For example, many automated investment products that automatically transfer investors’ funds between investments are registered under the Advisers Act. The SEC investigates how well fintech firms that provide those products comply with that regulation. See BI Intelligence, *Here’s the SEC’s Plan for the Future of US Fintech*, BUSINESS INSIDER (Nov. 16, 2016), <http://www.businessinsider.com/heres-the-secs-plan-for-the-future-of-us-fintech-2016-11>.

<sup>235</sup> Tricchinelli, *supra* note 231.

<sup>236</sup> Rachel Witkowski, et al., *Regulator Will Start Issuing Bank Charters for Fintech Firms*, WALL STREET J. (Dec. 2, 2016), <http://www.wsj.com/articles/regulator-will-start-issuing-bank-charters-for-fintech-firms-1480691712>.

traditional institutions as a core mission,<sup>237</sup> some of those traditional institutions (and many others) argue that more benefit could be derived from cooperation between the two industries.<sup>238</sup> A single license would make it easier for many companies to do business,<sup>239</sup> while those who did not want to seek a national charter could stick with the current system. Those who forgo the current system could still take advantage of potential developments regarding passporting and regtech, especially if they are smaller companies who could not afford the costs of a national bank charter. While this dual national charter and state-by-state approach seems counter to the idea of a consistent regulatory scheme, the dual-regulation scheme has been a “hallmark of cooperative federalism.”<sup>240</sup> The larger, established companies who arguably are most in need of a more structured regulatory scheme could voluntarily apply for a charter, while smaller firms could take advantage of the state-by-state approach. Fintech firms specializing in payment processing could avoid partnerships with existing national banks, and instead divert the funds expended on that enterprise for growth and expansion. The OCC’s previous experience in regulating risky companies and dealing with systemic risk would serve it well in dealing with fintech firms, and it could even “leverag[e] the work of the National Risk Committee”<sup>241</sup> to augment their experience.<sup>242</sup>

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<sup>237</sup> SoFi’s ongoing campaign in the words of Mike Cagney, its chief executive officer, is to “kill banks.” “We’re trying to make these guys dinosaurs,” Cagney says. “And hopefully I’m the meteor by which they all die.” Noah Buhayar and Natalie Kitroeff, *This Lender Lures Millennials with Free Cocktail Parties*, BLOOMBERG (Dec. 3, 2015), <https://www.bloomberg.com/news/articles/2015-12-03/this-lender-lures-millennials-with-free-cocktail-parties>.

<sup>238</sup> Rob Nichols, *Bank or No Bank, Fintech Must be Regulated*, AMERICAN BANKER (Feb. 18, 2016), <https://www.americanbanker.com/opinion/bank-or-no-bank-fintech-must-be-regulated>.

<sup>239</sup> Rachel Witkowski & Telis Demos, *Fintech Startup Craves More Regulation*, WALL STREET J. (June 9, 2016), <http://www.wsj.com/articles/fintech-startup-craves-more-regulation-1465517775>.

<sup>240</sup> Ryan, *supra* note 87.

<sup>241</sup> The National Risk Committee “serves as a central point of coordination for the [OCC’s] existing and emerging supervision and policy issues, including

Recently, legislatures across the world<sup>243</sup> have begun to introduce a system where fintech companies could “work alongside a regulator when testing a fintech product or service.”<sup>244</sup> These systems termed “regulatory sandboxes,” and give firms a place to test new products or business models without the need for completing the full regulatory process.<sup>245</sup> The sandboxes often allow innovative business to operate exempt from some rules, after being vetted by regulators.<sup>246</sup> Globally, sandboxes vary in the amount of leeway given to fintech firms, with some countries like Hong Kong only allowing banks who utilize fintech to participate.<sup>247</sup> Other countries like Singapore, Australia, and Britain have established incubators that encourage more fintech firms, including startups, to experiment.<sup>248</sup> Some U.S. politicians like Rep. Patrick McHenry (R., N.C.) have pushed for a regulatory sandbox option in order to prevent fintech firms from finding more attractive regulatory environments overseas.<sup>249</sup> However, detractors

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recommended actions to address such issues.” The Office of the Comptroller of the Currency, Fiscal Year 2017 Bank Supervision Operating Plan (2017), <https://www.occ.gov/news-issuances/news-releases/2016/nr-occ-2016-112a.pdf>.

<sup>242</sup> Gutierrez, *supra* note 212.

<sup>243</sup> See, e.g., Tom Zanki, *Malaysian Central Bank Forms Fintech Regulatory Sandbox*, LAW360 (Oct. 20, 2016), <https://www.law360.com/articles/853780/malaysian-central-bank-forms-fintech-regulatory-sandbox>. Malaysia has followed the example of other Asian countries like Hong Kong and Singapore, while the U.K. has been noted as a global leader in pushing fintech sandboxes. *Id.*

<sup>244</sup> Rachel Witkowski, *U.S. House Bill Aims to Set Up ‘Sandbox’ for Fintech Innovation*, WALL STREET J. (Sept. 22, 2016), <https://www.wsj.com/articles/u-s-house-bill-aims-to-set-up-sandbox-for-fintech-innovation-1474539893>.

<sup>245</sup> *Id.*

<sup>246</sup> Alastair Sharp, *Canada’s Securities Regulators Launch Fintech ‘Sandbox’*, REUTERS (Feb. 23, 2017), <http://www.nasdaq.com/article/canadas-securities-regulators-launch-fintech-sandbox-20170223-01813>.

<sup>247</sup> Michelle Chen & Michelle Price, *Hong Kong to Launch Banking Fintech ‘Sandbox’ as Rivals Pull Ahead*, REUTERS (Sept. 6, 2016), <http://www.reuters.com/article/us-hongkong-banks-regulator-idUSKCN11C0EV>.

<sup>248</sup> *Id.*

<sup>249</sup> See Witkowski, *supra* note 244. See Brain Knight, *Innovation Will Stall Without a Regulatory Fintech ‘Sandbox’*, AM. BANKER (Nov. 15, 2016),

argue that a sandbox would only add to a fragmented regulatory system if multiple government agencies each had their own innovation office.<sup>250</sup> While little progress has currently made in establishing a fully realized sandbox in the U.S., some federal regulators, like the Commodity Futures Trading Commission’s (“CFTC”) acting chair, have signaled an interest in establishing the regulatory framework.<sup>251</sup> Thomas Curry, current Comptroller of the Currency, hasn’t wholly embraced the sandbox approach, recently stating that, “we are not talking about giving you a carte blanche, get-out-of-jail-free card in terms of consumer products that may result in harm to individual consumers.”<sup>252</sup> He did indicate that the OCC’s Office of Innovation would work with firms to vet product and technology ideas “in a controlled setting” to limit potential liability.<sup>253</sup> The office will allow the OCC and banks it already supervises to experiment with new technology before it hits the market, and understand how a new product interacts with “existing regulations and implications to the safety and soundness of banks.”<sup>254</sup> While this may be a step in the right direction, it seems for now that a fully realized fintech sandbox is not in the cards, and

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<https://www.americanbanker.com/opinion/innovation-will-stall-without-a-regulatory-fintech-sandbox> (arguing that a U.S. sandbox is necessary to encourage innovation without jeopardizing consumers).

<sup>250</sup> See Witkowski, *supra* note 244. The chief digital officer of SVB Financial Group (parent company of Silicon Valley Bank) noted that he would prefer the Commerce Department to oversee a sandbox lab instead of an agency-by-agency approach. *Id.*

<sup>251</sup> Richard Hill, *Giancarlo’s CFTC May Give Fintech Innovators Their Own Sandbox*, BLOOMBERG BNA (Feb. 22, 2017), <https://www.bna.com/giancarlos-cftc-may-n57982084153/>. Other federal regulators like Comptroller of the Currency Thomas Curry and Federal Reserve Governor Lael Brainard “have been skeptical in public remarks.” *Id.*

<sup>252</sup> Melanie Best, *Supporting Responsible Innovation in the U.S. Financial Sector: An OCC Perspective*, DTCC CONNECTION (Mar. 17, 2017), <http://www.dtcc.com/news/2017/march/17/supporting-responsible-innovation-in-the-us-financial-sector>.

<sup>253</sup> *Id.*

<sup>254</sup> Evan Weinberger, *OCC to Open Innovation Office to Boost Fintech at Banks*, LAW 360 (Oct. 26, 2016), <https://www.law360.com/articles/856117/occ-to-open-innovation-office-to-boost-fintech-at-banks>.

instead government agencies like the OCC will experiment with a more restrictive version of a sandbox.

In summary, this new system would strike a balance between “encouraging innovation while extending traditional protections to new financial products that have boomed since the financial crisis.”<sup>255</sup> Despite concerns voiced by state-level regulators, a new system of regulation could ensure that state-level consumer protection laws are not pre-empted, which would create better protection of consumers due to the overlay of state and federal protection.<sup>256</sup> However, it would still be important that states attempt to institute reforms of their own in order to make a non-national charter option friendlier to growing fintech firms. As mentioned previously, important reforms would include passporting and potentially regulatory sandboxes, which would help make the state-by-state option more viable for smaller companies.<sup>257</sup> Lastly, as mentioned previously, fintech companies have incredible potential to expand access to credit and help reach underserved and unbanked populations.<sup>258</sup>

Creating a new regulatory scheme may have overwhelming positive effects, but there would undoubtedly be negative repercussions. State-level regulators have been quick to point out

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<sup>255</sup> Thomas J. Curry, Comptroller, Office of the Comptroller of the Currency, Remarks Regarding Special Purpose National Bank Charters for Fintech Companies, at 2 (Dec. 2, 2016), <https://www.occ.treas.gov/news-issuances/speeches/2016/pub-speech-2016-152.pdf>.

<sup>256</sup> “[A]ny other state laws that only incidentally affect national banks’ exercise of their federally authorized powers to lend, take deposits, and engage in other federally authorized activities are not preempted. Moreover, the OCC has taken the position that state laws aimed at unfair or deceptive treatment of customers apply to national banks.” OFFICE OF THE COMPTROLLER OF THE CURRENCY, EXPLORING SPECIAL PURPOSE NATIONAL BANK CHARTERS FOR FINTECH COMPANIES (Dec. 2016), <https://www.occ.treas.gov/topics/bank-operations/innovation/comments/special-purpose-national-bank-charters-for-fintech.pdf>.

<sup>257</sup> See *supra* Part III, Section C.

<sup>258</sup> Gabriel Rubin, *Fed’s Brainard: Fintech Has Potential to Expand Access to Credit*, WALL STREET J. (Dec. 2, 2016), <https://www.wsj.com/articles/feds-brainard-financial-technology-has-potential-to-expand-access-to-credit-1480687692>.

that the OCC's unilateral decision to consider national bank charters for fintech firms is absent statutory authorization.<sup>259</sup> Additionally, the same regulators have voiced concerns that “the creation of a federal charter for fintech or other nonbanking companies would put the OCC in the position of picking winners and losers among providers of fintech services, to the general detriment of customers and innovative financial services providers.”<sup>260</sup> Despite assurances to the contrary, the creation of a federal system could preempt state consumer protection laws, like the ones that served to combat predatory lending<sup>261</sup> in the absence of a comparable federal scheme leading up to the 2008 financial crisis.<sup>262</sup> Additionally, the OCC's creation of new charter types could violate the traditional separation of banking and commerce<sup>263</sup> and predispose the financial system to another catastrophic depression, this time precipitated by risk-seeking, growth-oriented companies. Finally, the granting of a charter to fintech firms could adversely affect full service banks who franchise their charters for programs managed by nonbank fintech companies and state banking departments who depend on revenue from regulated institutions.

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<sup>259</sup> “State regulators believe that Section 5.20(e)(1)(i) of the OCC's chartering regulations exceeds the statutory limits of the OCC's chartering authority by authorizing the OCC to charter an institution that engages exclusively in non-depository core banking functions—whether lending money and/or paying checks.” Conference of State Bank Supervisors, *Comment Letter on Proposed Rule on Receiverships for Uninsured National Banks* (Nov. 14, 2016), <https://www.csbs.org/regulatory/policy/Documents/2016/CSBS%20Comment%20Letter%20on%20OCC%20Receiverships%20for%20Uninsured%20National%20Banks%20NPRM.pdf>.

<sup>260</sup> *Id.*

<sup>261</sup> *See, e.g.,* Arthur E. Wilmarth, Jr., *The Dodd-Frank Act's Expansion of State Authority to Protect Consumers of Financial Services*, 36 IOWA J. CORP. L. 893, 909-919 (2011) (arguing that federal preemption of state level consumer protection laws permitted “unsafe and abusive lending practices to flourish”).

<sup>262</sup> Conference of State Bank Supervisors, *supra* note 259.

<sup>263</sup> *See id.* (arguing that a fintech charter would “be exempt from coverage under the BHCA, there would be no federal mechanism to ensure that its activities remain divorced from ownership or control by commercial enterprises”); *see also* 12 U.S.C. § 1843(c)(8) (2012).



## V. CONCLUSION

Regardless of the point in the future when fintech companies gain the ability to apply for national charters, the industry will continue to innovate, grow, and disrupt traditional financial fields. Millennials, an increasingly large part of the population, will continue to rely on internet-based banking options for peer-to-peer payments, loans, and wealth management. While a national charter for fintech companies may have some drawbacks, and may not be the best option for smaller companies, the increased regulation, uniformity, and transparency that come with the charter will benefit consumers and regulators alike. Our regulatory system needs to advance to accommodate an ever-increasing wave on companies who cannot be managed by the traditional geographic barriers that have long governed financial institution regulation.

With a national special purpose charter option, companies will be able to continue to innovate and create new financial products that increase competition and deliver better rates and services to consumers, all while being supported by a robust regulatory structure that will ensure these companies do not endanger their customers' funds or the financial system. The grant of special purpose charters places fintech companies on a more equal playing field with traditional banking entities, many of whom are attempting to respond to the increased competition by investing in fintech products themselves. Despite the battle lines already being drawn by state banking regulators due to their financial interest in continuing to regulate fintech firms, and the flurry of lawsuits that are sure to follow, the OCC's decision to potentially issue national bank charters to fintech companies is the correct choice for fintech companies, consumers, and the financial industry as a whole.

The decision to grant national charters should not focus on the economics of the situation, or the threat that fintech firms may pose to traditional banking institutions. Fintech is a growing industry, and the United States should seize the opportunity to lead the development of a new, job-creating industry. While the recent change in administration could signal "a real possibility for a

significant overhaul of financial services regulation,<sup>264</sup> there is still hope that federal regulators will be able to move forward with plans to incorporate the fintech industry into the financial landscape. The decision to grant a national charter to fintech companies is about what makes the most sense for consumer protection, competition in the marketplace, cost-saving for traditional players, and regulators. The recent step taken by the OCC in explaining how it would apply licensing standards and requirements in existing regulations to fintech companies is a promising one,<sup>265</sup> and indicates that momentum behind the proposal is substantial. Hopefully, the financial services community and the new administration will embrace the sensible choice over specific financial interests.

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<sup>264</sup> Brandon Roman & Patick Kirby, *Major Changes to Dodd-Frank Ahead?; SEC, CFTC, FDIC to Meet*, SQUIRE PATTON BOGGS (Nov. 14, 2016), <http://www.capitalthinkingblog.com/2016/11/major-changes-to-dodd-frank-ahead-sec-cftc-fdic-to-meet/>; see also *Trump's Chance to Redefine the Regulators*, *supra* note 15.

<sup>265</sup> *Evaluating Charter Applications from Financial Technology Companies*, *supra* note 51.