

March 24, 2017

Specialpurposecharter@occ.treas.gov

Beth Knickerbocker
Acting Chief Innovation Officer
Office of the Comptroller of the Currency
400 7th Street, SW
Washington, D.C. 20219

Re: Exploring Special Purpose National Bank Charters for Fintech Companies

Dear Ms. Knickerbocker,

We appreciate the opportunity to share our views with the OCC Office of Innovation. As law students interested in the future of financial services, we have closely followed the OCC's efforts to promote responsible innovation in the banking system. One of us submitted a comment letter to the OCC in May 2016 advocating for the creation of an Office of Innovation.¹ We are pleased that the OCC has taken that step and that we now have an opportunity to engage with the Office.

We have reviewed all the comment letters (totaling more than 100) submitted to the OCC in response to its whitepaper "Exploring Special Purpose National Bank Charters for Fintech Companies." Many of the letters – particularly those submitted by fintech companies in the lending, payments, and digital currency sectors – rightly argue that the OCC should grant Special Purpose Charters. Among other benefits to consumers and fintech firms, this Charter will promote financial innovation and inclusion, provide regulatory clarity and harmony, and enhance safety and soundness. Further, these letters note that the Charter will enable fintech companies to earn greater trust from customers, reduce cost of capital, and more easily partner with other financial institutions. In short, the Charter will achieve the goal of promoting responsible innovation in the U.S. financial system.

However, only a handful of comment letters mention one important additional benefit of the Charter: decoupling fintech startups from dubious bank partnerships. Currently, many fintech startups enter into arrangements with banks friendly to money services businesses ("MSBs"), as a means of avoiding onerous and fragmented state regulation.² These arrangements may be structured as service provider relationships, where the startup is only extending its software services to the bank's customers; the bank controls any movement of funds that may occur. Alternatively, startups may be appointed as a bank agent or the authorized delegate of licenseholders, thereby winning the implicit authorization to conduct regulated activity under the aegis of the bank or licenseholder. Of the more than 100 letters received during the comment period, fewer than ten directly addressed the effects of the Special Purpose Charter on fintech-

¹ See Andrew Ruben, *Supporting Responsible Innovation through an Office of Innovation*, Comment Letter (May 30, 2016), available at <https://www.occ.gov/topics/bank-operations/innovation/comments/comments-andrew-ruben.pdf>.

² See World Economic Forum, *The Future of Financial Services: How disruptive innovations are reshaping the way financial services are structured, provisioned and consumed* 12 (June 2015).

bank partnerships.³ Nevertheless, we think this is a central issue that will prove markedly better for financial innovation and bank safety-and-soundness.

These fintech-bank partnerships tend to be born out of necessity rather than desire.⁴ State-by-state licensing costs are astronomical and entail multi-year processing waits.⁵ Consequently, many fintech startups prefer sharing control of their business program with their bank partners, in hopes of getting their products to market more quickly.⁶ However, this arrangement is suboptimal for all stakeholders involved. First, the OCC and various banking regulators no longer have direct oversight of these startups, which would have been performing bank-like functions (e.g., lending and money transmission). That oversight responsibility is essentially delegated to the partner bank,⁷ which in turn means that oversight quality varies by bank. Second, the partner banks themselves are exposed to additional risk, since there may be conflicts of interest between the desire for fee revenue and establishing sufficiently robust screens and controls over the startup's program. Third, the startup itself could be worse off than if it pursued a one-stop, fintech charter solution. The legal fees involved with designing and implementing a bank-led program, coupled with ongoing mitigation efforts against bank discontinuance (i.e., banks summarily closing accounts due to changes in risk appetite),⁸ impose a significant cost on these startups.

A Special Purpose Charter, with requirements properly calibrated to riskiness, will address these problems for regulators, banks, and startups. The OCC and banking regulators can more effectively supervise fintech companies because, like any full-service national bank, the

³ Several startups and fintech associations noted that the special purpose charters would help bring fintech companies out of the shadow of their bank partners, while banks and banking associations noted that it would hamper efforts of both non-bank financial institutions and banks. See, e.g., Comment Letter, *Comments Regarding Special Purpose National Bank Charter for Fintech Companies*, CIRCLE (Jan. 17, 2017) (highlighting how companies could achieve greater efficiencies through the special charter); Comment Letter, *Exploring Special Purpose National Bank Charters for Fintech Companies*, AMERICAN BANKERS ASSOCIATION (Jan. 17, 2017) (explaining how the special charter would introduce yet more regulators into existing fintech-bank partnerships).

⁴ Lending startups, for example, must turn to bank partners to avoid getting licenses in every state. See Noah Buhayar, *Where Peer-to-Peer Loans are Born*, BLOOMBERG BUSINESSWEEK (Apr. 16, 2015), available at <https://www.bloomberg.com/news/articles/2015-04-16/webbank-where-peer-to-peer-loans-are-born> (“LendingClub and Prosper don’t originate loans themselves because they don’t have—and don’t want—banking licenses. Turning to a third party to create the loans lets them avoid regulatory costs, and being viewed as technology companies rather than financial firms improves their image with investors.”).

⁵ See Thomas Brown, *50-State Survey: Money Transmitting Licensing Requirements*, PAUL HASTINGS LLP (2013), [http://abnk.assembly.ca.gov/sites/abnk.assembly.ca.gov/files/50%20State%20Survey%20-%20MTL%20Licensing%20Requirements\(72986803_4\).pdf](http://abnk.assembly.ca.gov/sites/abnk.assembly.ca.gov/files/50%20State%20Survey%20-%20MTL%20Licensing%20Requirements(72986803_4).pdf).

⁶ Transferwise’s partnership with Community Federal Savings Bank may be one example of how a startup can quickly get its product to the US market while collecting required state licenses. See Rob Price, *One of TransferWise’s US banking partners had unsafe and unsound banking practices*, BUSINESS INSIDER (May 23, 2016), available at <http://www.businessinsider.com/transferwise-us-banking-partner-cfsb-unsafe-unsound-banking-practices-occ-2016-5>.

⁷ The OCC has determined that banks are responsible for incremental risks introduced by their service providers. OCC Bulletin 2013-29, *Third-Party Relationships, Description: Risk Management Guidance* (Oct. 30, 2013), available at <https://www.occ.gov/news-issuances/bulletins/2013/bulletin-2013-29.html>. See Division of Banking Supervision and Regulation, *Guidance on Managing Outsourcing Risk*, FEDERAL RESERVE BOARD (Dec. 1, 2013).

⁸ Press Release, *FinCEN Statement on Providing Banking Services to Money Services Businesses*, FINCEN (Nov. 10, 2014).

fintech company must meet supervisory standards relating to safety and soundness, fair access to financial services and fair treatment of customers, and compliance with applicable laws and regulations.⁹ Banks will take on less risk when structuring partnerships with fintech companies. And startups will gain the opportunity to pursue a national rollout strategy independent of attachment to any bank partner and within a more coherent regulatory scheme.

We believe both the banking industry and fintech startups will benefit tremendously from clear, expeditious, and unitary oversight of fintech activity. We appreciate the opportunity to offer these comments and strongly support the OCC's continued efforts to promote responsible innovation.

Sincerely,

Andrew Ruben and Benjamin Lo
Yale Law School students, Class of 2017
Yale Law School Financial Markets and Corporate Law Clinic¹⁰

⁹ See Michael Nonaka, *OCC to Issue Special Purpose National Bank Charters to Fintech Companies*, COVINGTON & BURLING LLP (Dec. 11, 2016), available at <https://corpgov.law.harvard.edu/2016/12/11/occ-to-issue-special-purpose-national-bank-charters-to-fintech-companies/>.

¹⁰ The views expressed are our own and do not reflect those of any other individual or of Yale Law School.