Portfolio Media. Inc. | 111 West 19th Street, 5th Floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

OCC's Potential Boon For Payment Industry Faces Headwinds

By **Philip Rosenstein**

Law360 (September 10, 2020, 8:54 PM EDT) -- Acting Comptroller of the Currency Brian Brooks has expressed a desire to wrap payments companies into the federal regulatory framework, and while the effort has been lauded as a move to ease compliance costs, state regulators appear prepared to fight to protect their oversight of the industry.

The numerous licensing requirements that exist for payments companies, which are typically regulated at the state level, has led many in the industry to look favorably upon federally chartering companies engaged in money transmission. Doing so would allow them to eschew the matrix of state laws regulating payments and money transmission, minimizing costs and shortening the runway to operation.

The Office of the Comptroller of the Currency has floated the idea of chartering payments companies over the past few months, as Brooks made clear his goal of keeping the agency up to speed with the advent of fintech and digital payments. And responding to reports in Politico last week that the OCC was prepared to accept applications from payments companies for a federal banking charter, the agency told Law360 that Brooks is of the opinion that "existing rules suffice to cover this activity and ensure that it could occur in a safe and sound manner."

However, attorneys say the move would likely create a new front in a battle between state and federal financial regulators as developments in fintech change how consumers interact with financial services.

The New York Department of Financial Services and the OCC are already **in a duel** at the Second Circuit over the legality of the federal agency's related fintech charter — which, at this point unlike the potential chartering of payments companies, arose through a formalized program.

Michelle Gitlitz, a partner at Crowell & Moring LLP and global head of the firm's digital assets and blockchain practice, told Law360 that a similar challenge to payments chartering could be expected.

"It would surprise me if the same thing didn't happen again," Gitlitz said. "I don't see why a regulatory institution like the New York Department of Financial Services would take a different position with respect to a payment charter than they did with the fintech charter."

State-Federal Tension Builds

While the OCC has been steadfast in its opinion that it has the authority to charter nondepository financial institutions, which would include payments companies, state regulators have fought back.

The DFS filed its challenge to the fintech charter program in September 2018, weeks after the OCC officially unveiled the plan. The charter was designed for fintech firms that don't take deposits but do engage in other banking activities, such as lending, and it would allow them to be overseen by the OCC as "special purpose national banks."

The DFS notched a win in New York federal court last year when U.S. District Judge Victor Marrero declined to dismiss the state regulator's lawsuit in May and entered a judgment in October effectively barring the OCC from considering any fintech charter applications on a nationwide basis.

In his ruling, Judge Marrero agreed with the DFS that the fintech charter program exceeded the boundaries of the OCC's powers as laid out in the National Bank Act. That law "unambiguously requires that ... only depository institutions are eligible to receive banking charters from the OCC," he said.

Following the OCC's pronouncements last week that "existing OCC processes for licensing and supervising companies that engage in payments are sufficiently robust to consider applications related to that core banking activity," state regulators were once again up in arms challenging the notion that the federal agency can charter nondepository payments companies.

In a statement, Conference of State Bank Supervisors President and CEO John W. Ryan said "the OCC's proposed payments charter is no different than the fintech charter already rejected in federal court and subject to a nationwide order preventing the OCC from accepting applications from a company that does not take deposits."

"State regulators are opposed to this unconstitutional expansion of power," he added.

DFS Superintendent Linda Lacewell asked for clarification from the OCC on its plans last week, saying the state regulator is reviewing its legal options.

"The federal district court held that the business of banking requires the taking of deposits and rejected the OCC's request to limit the geographic reach of this holding to the Southern District of New York," Lacewell said in a statement. "Above all, New York will continue to protect consumers through state oversight that puts them at the center of all we do."

Despite its openness to chartering payments companies, the OCC has not promulgated any new special purpose national bank charter, and it remains unclear whether it will or whether the existing fintech charter could be applied.

Following the media reports, the agency said there had been no changes to "policy or posture" on the question of federally licensing payments companies. It further outlined that it had yet to receive any such application from a payments company, and that the process would include public notice as well as publication of part of the application with the ability for the public to comment.

Stephen Aschettino, a partner and chair of payments technology at Loeb & Loeb LLP, told Law360 that even in the absence of a resolution in the fintech charter case, states could attempt to pump the breaks on any payments chartering by the OCC.

"There's a risk, of course, that a charter could be invalidated by virtue of litigations working through the courts, but in the interim, if a state takes the position that a charter is not valid, that state could send an enforcement action letter and allege that a company is operating an unlicensed money transmitter business," he said.

Industry Welcomes the Possibility

Despite the legal questions that are sure to tangle the OCC's efforts, attorneys and industry insiders touted the benefits that a smoother licensing regime would have for payments companies themselves as well as for their customers.

"Having a one-stop shop, let alone the one sole regulator to deal with thereafter, has tremendous appeal," Aschettino said. "It would increase the speed in which certain companies moving into that space can obtain a charter."

Should the OCC begin to charter payments companies, however, the compliance efforts should not be understated, Aschettino said.

"It's a significant undertaking to prove to the OCC that you are charter-worthy," he said. "There are numerous requirements. And going forward, you're going to be subject to all of the types of onerous compliance obligations that banks are accustomed to. So it's not for the faint of heart."

Updating the regulatory framework for payments firms would undoubtedly be a boon to such companies, Nick Catino, head of policy and campaigns at global payments company TransferWise, told Law360.

"Under the current regulatory regime, payment providers rely on bank partners — often competitors — to access payment rails," Catino said. "That ultimately results in added costs to the customer and concentrates risk in a handful of the largest banks who process most payments."

"A modern regulatory framework with expanded participation in the payments system ... would also boost financial stability by diversifying risks and eliminating single points of failure within the payments system," he said.

Crowell & Moring's Gitlitz also said consumers stand to benefit from a nationwide, uniform regulatory structure.

For example, the fractured regulatory framework for the trading of digital tokens creates a reality where someone in one state may not have access to a particular token that is available in another, she said.

"Fundamentally, why is it fair that someone in one state has access to different coins than someone in another state?" she asked. "It seems to me that your access to certain digital assets shouldn't depend on where you live."

--Editing by Aaron Pelc and Kelly Duncan.