

Memorandum

FinTech Update: OCC Issues Draft Licensing Procedures

March 31, 2017

Last December, the Office of the Comptroller of the Currency (“OCC”) announced that it would begin granting limited-purpose national bank charters to financial technology, or “fintech,” companies that offer bank products and services. The principal benefit of such a charter is that it would largely allow such firms to operate nationwide under a single set of national standards, without needing to seek state-by-state licenses or joining with brick-and-mortar banks.

In March, the OCC issued draft licensing procedures on the chartering process for fintech companies. These procedures, which would take the form of a supplement to the OCC’s existing Licensing Manual, are an important step in the OCC’s approach to fintech. Ordinarily, the OCC does not solicit comments on procedural manuals and supplements, but it has announced that it will accept comments on these fintech licensing procedures through April 14.

This memorandum summarizes key aspects of the procedures for firms seeking a fintech charter.

Initial Contact with the OCC and Pre-Filing Communications

Applying for a fintech charter will be an iterative process, with extensive interaction with OCC staff. The initial point of contact with the OCC will be its newly formed Office of Innovation. Staff in this office will field preliminary inquiries on chartering matters and arrange for an exploratory meeting with appropriate OCC staff, including staff of the OCC’s Licensing Division. After this exploratory meeting, the OCC will assign a Licensing Division contact to the fintech company. A formal pre-filing meeting would then follow. Before this initial meeting, a company would be expected to provide the OCC with an overview of its proposal, a description of its business plan, and information on the qualifications of organizers and proposed senior management, among other things. Additional pre-filing meetings may be necessary depending on the novelty and complexity of the proposal.

Review of Proposed Activities

A company seeking a fintech charter will need to ensure that it will conduct fiduciary activities or at least one of the following three core banking functions: receiving deposits, paying checks, or lending money. In its draft licensing procedures, the OCC notes that it views the National Bank Act as “sufficiently adaptable” to permit firms to engage in new activities as part of the business of banking or to engage in traditional activities in new ways. For example, as noted in our most recent memorandum on the OCC’s fintech charter, the OCC views the facilitation of payments electronically as the “modern equivalent of paying checks.”¹ In addition, the OCC has indicated that, in some cases, the activities of a potential applicant may include activities that have not been previously determined to be part of, or incidental to, the business of banking or to fall within an established core banking function. In such case, the OCC expects a potential applicant to discuss its activities with the OCC during pre-filing meetings. The OCC also may request that the company prepare a legal analysis to support its view that the proposed activities are permissible and fall within one of the core banking functions.

Filing Procedures – Public Notice and Comment

After the pre-filing phase, an applicant would file its application with the OCC and then arrange for notice to be published in a newspaper of general circulation. A public comment period would run for 30 days after this notice. The public portion of the application, including parts of the business plan, would also be available on the OCC’s public website. Confidential treatment may be requested for portions of the application and business plan that contain proprietary information.

Standards for Evaluating an Application

The OCC will consider several criteria when evaluating an application from a fintech company, including:

- whether organizers and management have appropriate skills and experience;
- whether the company has adequate capital to support the projected volume and type of business and proposed risk profile;
- whether the company’s business plan demonstrates a clear path and timeline to profitability; and
- whether the business plan contains a financial inclusion plan, if applicable.

In addition, the OCC will take into consideration an applicant’s record with other regulators. A pending investigation or enforcement action by another regulator may be grounds for denial of a fintech charter application.

¹ See “OCC Announces New Federal Charter for FinTech Firms” (Dec. 6, 2016), *available* [here](#).

Requirements for the Organizing Group, Management and Directors

The OCC will evaluate whether the organizers of the fintech company, as well as its proposed management and directors, are well-qualified, with diverse experience in banking and other relevant areas. Relevant experience will depend on the specific products or services to be offered by the applicant.

Business Plan Requirements

Every fintech charter applicant will be required to submit a comprehensive business plan as part of its application. The OCC has offered the following guidance for applicants on their business plans:

- ***Risk Assessment:*** A business plan should include an assessment of the specific risks facing the fintech company given its business model. Risks include concentration risk, compliance risk, reputational risk, strategic risk, and operational risk (including cybersecurity risk). The risk assessment should articulate the company's "risk appetite" and how the company would effectively manage any identified risks. The risk assessment should also address what controls exist for monitoring and mitigating risks, including management information systems.
- ***Systems and Controls:*** A description of the fintech charter applicant's IT program and compliance management program will need to be included in the business plan. The OCC is particularly concerned about data security issues and cyber-risk governance, as well as the applicant's commitment to complying with applicable laws and regulations, such as anti-money laundering and sanctions requirements, consumer protection laws, and prohibitions against unfair or deceptive acts or practices. In addition, the plan should discuss whether any functions or services will be outsourced to third-party service providers and how vendor-related risks will be managed.
- ***Financial Management:*** Although a company with a fintech charter will be subject to the OCC's minimum leverage and risk-based capital standards under 12 C.F.R. Part 3, the OCC will also require that a business plan propose minimum capital levels. Consistent with how the OCC charters other special purpose banks, the OCC will condition its preliminary approval of a charter on the applicant meeting minimum capital levels at all times, with the amount of capital depending on the OCC's analysis of various quantitative and qualitative factors. We would expect any initial minimum capital requirement to be an important point of negotiation during the application process. An applicant will also need to discuss how it would address adverse market conditions that could deplete capital, such as broad market volatility or volatility specific to a business line. Moreover, an applicant will need to include a section in its plan on liquidity and funds management.

- ***Financial Inclusion:*** If a fintech charter applicant intends to engage in lending or providing financial services to consumers or small business, then it will need to demonstrate its commitment to financial inclusion. To do this, the business plan must include a separate financial inclusion plan (“FIP”). The FIP will vary from applicant to applicant, and we expect this will be an area of significant discussion with OCC staff during the application process. According to the draft licensing procedures, the FIP will provide detail on “proposed goals, approaches, activities, and milestones for serving the relevant market and community.” Among other things, the FIP should describe the products or services that the applicant will offer, including any products or services that will foster financial inclusion, whether defined by income, geography, or other criteria such as unserved or underserved populations. The OCC will review the adequacy of an applicant’s FIP based on whether it would support “fair access to financial services and fair treatment of customers.” Among other things, the OCC may examine whether the applicant’s policies and procedures are designed to ensure that products and services will be offered and provided on a non-discriminatory basis, with full disclosure to consumers of terms and conditions.
- ***Alternative Business Strategy and Contingency Planning:*** Depending on a fintech charter applicant’s proposed business strategy and structure, the OCC may require a discussion of how the company will manage potential scenarios when expectations (such as operating expenses, marketing costs, or growth rates) differ significantly from the original business plan. In any event, every business plan must discuss realistic contingency and recovery planning and how the company can unwind itself in an organized manner if necessary.
- ***Monitoring and Revisions:*** There should be a discussion on how the fintech company’s board of directors will monitor adherence to the business plan and, if necessary, modify it to accommodate significant or material changes. The OCC expects technology-dependent businesses to have mechanisms in place to accommodate new or evolving technologies.

Chartering Decision

The OCC will grant approval of a charter application in two steps: (i) preliminary conditional approval and (ii) final approval. The draft licensing procedures make clear that a preliminary conditional approval is only an indication that the fintech charter applicant has passed the first phase of OCC review and that the organizers may start raising capital, hiring officers and employees, and developing policies and procedures. In granting preliminary conditional approval, the OCC will typically impose certain requirements on the applicant, such as requiring the adoption of an appropriate internal audit system or requiring that additional capital be raised. An applicant must generally open for business within 18 months of obtaining conditional approval, unless the OCC grants an extension. If the OCC’s final approval is obtained, it means that the fintech company can begin to conduct banking business. The fintech company would then be subject to OCC supervision, including on-site examination and periodic off-site monitoring.

For more information on the OCC's new fintech charter and how comments may be submitted on the OCC's draft licensing procedures, please contact any member of the Firm's Financial Institutions Group.

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