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NYSDFS scores win on federal banking charters for fintech firms

A New York federal district court ruled in favor of the superintendent of the New York State Department of Financial Services (NYSDFS), finding that the U.S. Office of the Comptroller of the Currency (OCC) does not have the authority under the National Banking Act to issue bank charters to fintech companies that do not accept deposits.

The key players:

- The New York Department of Financial Services—a state regulatory agency
- The OCC and Comptroller Joseph Otting—the national banking regulatory agency
- Financial technology companies—financial institutions, money services businesses and other companies that offer financial services but are not considered banks since they typically do not accept deposits; they are subject to various state and federal rules

Background:

In an attempt to update the regulation of financial services, the OCC in 2016 announced that it was considering accepting applications for special-purpose national bank charters from fintech companies. The OCC in 2018 announced its final decision to do so.

Those in favor of the “fintech charter” cited the need to update regulation of financial services to include newer types of financial institutions and make fintech

regulation more consistent throughout the financial sector.

Those who opposed the announcement said that the OCC did not have the authority to grant these charters under the National Banking Act—originally the National Currency Act—an 1863 law, amended in 1864, that established the national banking system and grants the OCC its authority.

Prior to this announcement, fintech companies operated pursuant to state licenses—requiring a license for each state in which they operate—and were subject to state consumer protection and usury laws but did not qualify for a federal charter to operate nationally. That is still the case since no charters have been granted.

The Conference of State Bank Supervisors opposed the OCC’s decision and challenged it in court. In September, the federal district court in Washington, D.C., granted the OCC’s motion to dismiss, for a second time, stating that the issue is not ripe until a charter is actually issued.

The New York case:

NYSDFS filed a separate suit in New York federal court. In May, the OCC asked the New York court to dismiss the suit. The court declined, holding that the National Bank Act’s “‘business of banking’ clause, read in the light of its plain language, history, and legislative context, unambiguously requires that,

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absent a statutory provision to the contrary, only depository institutions are eligible to receive national bank charters from OCC.”

Now the same judge has issued a final order in favor of DFS. The court’s cursory order adopted the reasoning from its May order, which turned on the plain language of the National Banking Act—specifically the “business of banking” clause—and noting that the parties to the case “have conferred and agree that the Court’s May 2, 2019, order resolves the substantive legal issues in this matter and renders the entry of final judgment appropriate.”

One of the chief concerns of NYSDFS was that the OCC’s decision affects individual states’ consumer protection laws, meaning that the OCC would supplant state authority to regulate fintech firms as nonbanks at the expense of consumers since the National Banking Act allows preemption of certain state laws.

Another consideration was the requirement that banks be insured. The Federal Reserve Act requires national banks to have insurance. But in order to

get this insurance, the national bank needs to be “engaged in the business of receiving deposits.” Fintech companies that do not receive deposits are therefore not eligible to receive insurance, making this a catch-22.

The OCC plans to appeal the New York court’s decision. Until then, it is doubtful that any fintech companies will apply for a charter given the arduous process and the possibility that the charter may be invalidated by a later court decision.

Related Professionals

For more information, please contact:

Stephen A. Aschettino saschettino@loeb.com

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