

Preserving the Integrity of the Bank Charter: The Community Bank Perspective

The Independent Community Bankers of America, representing community banks across the nation with more than 52,000 locations, appreciates the opportunity to provide this statement for the record for today’s hearing, “License to Bank: Examining the Legal Framework Governing Who Can Lend and Process Payments in the Fintech Age.” We appreciate you raising the profile of fundamental questions that will determine the future of the American financial services landscape. We are pleased to share the community bank perspective on these critical questions.

Congress Must Assert its Authority Over the Fundamental Legal Framework of Banking

This is a time of transformative change in the financial services marketplace. Community banks welcome technological innovation, but we must also recognize that technological change underscores the importance of a robust legal framework to ensure consumer protection as well as the safety and soundness of our institutions and of the system as a whole. In addition, we must not allow technological change to erode the long-standing U.S. policy of separating banking and commerce, a policy created in the 1930s and in response to concerns about concentration of economic power. Separating banking and commerce ensures that the allocation of credit is independent and impartial. Mixing banking and commerce inevitably creates market distortions and leads to cross-sector consolidation. In the age of big data, social media and e-commerce conglomerates, this threat is greater now than it was in the 1930s.

Because the legal framework of banking is fundamental and the stakes are far reaching and significant, any changes to it should be debated and deliberated in Congress, not merely through oversight but through the legislative process. Only Congress has the requisite authority as well as the power to ensure consistent regulation and oversight across charters issued by different agencies. Agencies should not infringe upon congressional authority by, for example, creating new charters and conferring powers on non-depository institutions that have traditionally and with sound reason been reserved for such institutions. As we argue below, the Office of the Comptroller of the Currency’s (OCC’s) proposed fintech charter and payments charters are examples of “charter slippage” that carry harmful, unintended consequences. In addition, the industrial loan company (ILC), though not a new charter, has historically been limited and is offered by only a handful of states. A state chartered ILC has the power to operate nationwide. Prior to 2020, the FDIC had not approved deposit insurance for a new ILC for more than 10 years. As discussed below, we urge Congress to reexamine the significant risks posed by the ILC charter.

Policy Must Promote Innovation

Innovation in financial services is critical to a modern, and increasingly digital, economy. Innovation offers financial consumers the choices they have come to expect and the speed and ease of transactions that today’s technology makes possible. Such innovation is also the key to the United States’ international competitiveness. But we must not envision a false tradeoff between financial innovation and fundamental consumer and systemic protections. Significant financial innovation is occurring today within traditionally chartered institutions and in partnership with

cutting edge technology companies. As discussed below, the OCC’s proposed rule to clarify which party is the “true lender” would promote such partnerships. Public policy can encourage this form of innovation by creating more flexible regulation for depository institutions.

Limited Purpose Charters: General Skepticism is Warranted

ICBA urges Congress to take a skeptical view of the creation of new limited purpose charters. In view of the evolution of other limited purpose bank charters—such as the ILC which is discussed more fully below—ICBA is concerned that any limited purpose fintech bank charter could end up having all of the advantages and benefits of a full-service bank charter without commensurate supervision and regulation. What begins as a narrow charter crafted to serve a particular demographic or a niche form of banking has the potential to grow and reshape the financial services landscape. Again, this potential calls for the intervention of Congress.

OCC Fintech Charter Would Distort Financial Marketplace

In 2018, the OCC indicated that it was open to accepting applications for national bank charters from non-depository fintech companies engaged in the “business of banking,” though to date the agency has received none. While such a charter would subject online lenders and fintech companies to more oversight and regulation than they now have—particularly in the area of consumer protection—these companies would be subject only to limited safety and soundness supervision and examination and would not be subject to the Community Reinvestment Act (CRA).

A special-purpose national bank charter for fintech firms would create an unlevel regulatory playing field. ICBA supports the development of a fintech regulatory framework that is no less stringent than that which applies to insured depository institutions. The OCC should publish transparent capital and liquidity requirements for these firms that specifically address minimum levels considered appropriate for a fintech firm to be well capitalized. Fintech capital and liquidity requirements should be no less rigorous than those that apply to insured depository institutions. Such a framework would promote a fair regulatory system, protect consumers, and support safety and soundness at these companies.

ICBA strongly supports a District Court ruling that the National Bank Act “business of banking” clause only allows the OCC to issue charters to depository institutions. The OCC is appealing that decision to the 2nd Circuit Court of Appeals. ICBA has filed an amicus brief in support of the New York Department of Financial Services.

OCC Payments Charter Could Compromise the Federal Reserve Payments System

This summer, Acting Comptroller Brian Brooks announced his intent to launch a special payments charter before the end of 2020, which could be used by non-depository companies to access the Federal Reserve payments system and safety net.

The special payments charter raises many of the same concerns raised by the fintech charter. It could be used to access the Federal Reserve payment system and avoid state consumer protection laws. In addition, such a charter, which could be owned by commercial companies, could violate the long-standing principle of the separation of banking and commerce. Would the non-bank parent company of a new special purpose payments bank be subject to the Bank Holding Company Act (BHCA)? If not, the parent company would not be subject to capital and liquidity requirements and would not be required to act as a source of strength to its subsidiary payments bank. For these reasons, the special payments charter would create more risk in the Federal Reserve payments system.

Without explicit authority from Congress, OCC should not proceed with the issuance of these charters.

Industrial Loan Company Loophole Should be Closed

The ILC loophole allows commercial companies to own institutions, which are the functional equivalent of banks and effectively mix banking and commerce.

While no new ILC applications for deposit insurance were approved since the Dodd-Frank Act moratorium expired in 2013 until March of this year when the FDIC approved the applications of Square and Nelnet, we expect more technology and social media companies to seek to exploit the ILC loophole. This would shift the American financial landscape and give rise to a whole new dimension of risk, a threat not only to our prosperity and economic diversity but to consumer privacy and fraud on a massive scale. What's more, commercial owners of ILCs, unlike bank holding companies, are not subject to consolidated supervision. This constitutes a dangerous gap in financial safety and soundness oversight.

A Senate bill, the Eliminating Corporate Shadow Banking Act (S. 2839), would amend the Bank Holding Company Act to close the ILC loophole and grandfather existing ILCs. In addition, ICBA is advocating for a moratorium on ILC applications so that Congress can consider permanent closure of the loophole.

ICBA Supports “Valid When Made” Doctrine and OCC “True Lender” Proposal

The decision of the U.S. Court of Appeals for the Second Circuit in *Madden v. Midland Funding LLC* has created considerable uncertainty about the validity of interest-rate terms after a national or state bank sells, assigns, or otherwise transfers a loan.

In response to this decision, both the FDIC and the OCC are proposing regulations that would clarify that when a bank sells, assigns, or otherwise transfers a loan, interest permissible at the time the loan was made continues to be permissible following the transfer. ICBA strongly supports both the OCC and the FDIC proposed regulations regarding federal interest rate authority. We agree that the bank's power to make loans implicitly carries with it the power to assign loans, and therefore a national or state bank's authority to make loans at particular rates necessarily

includes the power to assign the loans at those rates. Denying an assignee – be it a bank or a non-bank – the right to enforce a loan’s terms would effectively reduce the salability of loans, make lenders less willing to originate loans and thereby curtail access to credit, a critical ingredient of the economic recovery.

ICBA supports the “valid-when-made” doctrine which holds that if a loan is valid when it is made, with respect to the interest rate and other terms of the loan, then the loan remains valid and enforceable when assigned to another party.

The OCC has recognized that the “valid-when-made” doctrine cannot be fully implemented without clarification of the “true lender” in such loan transfers. For this reason, the OCC has issued a proposed regulation concerning when a national bank or a Federal savings association makes a loan and is the “true lender” in the context of a partnership between a bank and third party, such as a marketplace lender. Specifically, the OCC is proposing that a bank makes a loan if, as of the date of origination, it is named as the lender in the loan agreement or funds the loan.

ICBA endorses the OCC’s proposed rule since it provides a clear and simple standard to determine when a bank makes a loan and is a “true lender” and thereby allows banks to fully exercise the authority granted to them under Federal law without incurring significant legal risks.

Moreover, if this proposal is adopted, it will allow the OCC to ensure that consumer regulations are not evaded once a national bank is considered the true lender. ICBA remains concerned with “rent-a-bank” schemes that are often set up for the sole purpose of avoiding state usury laws and other state consumer protections. Clarity surrounding the true lender doctrine would promote accountability and should not absolve either a bank or its third-party partners of their regulatory responsibilities.

Closing

Thank you again for convening today’s hearing. The questions before the committee are fundamental to the future direction of American financial services and should be exclusively within the purview of Congress not the agencies. We urge you to assert your authority over these important questions and offer to work with you to develop and advance appropriate legislation.