

## Client Alert

### Predominantly Engaged: A Modest Proposal for the OCC Payments Charter

August 10, 2020

#### Key Contacts

**Douglas Landy**, Partner  
+1 212.530.5234  
[dlandy@milbank.com](mailto:dlandy@milbank.com)

**James Kong**, Associate  
+1 212.530.5244  
[jkong@milbank.com](mailto:jkong@milbank.com)

The Acting Comptroller of the Currency, Brian Brooks, has in numerous speeches and appearances announced the intention of the Office of the Comptroller of the Currency (the “OCC”) to issue national bank charters to entities engaged in “payments.” These charters would be full national bank charters issued pursuant to the National Bank Act (the “NBA”), as the payments entity would be engaged in at least one of the three enumerated national bank activities: lending, payments or deposits.

The Conference of State Bank Supervisors (“CSBS”) has stated that it does not believe the OCC has the authority to issue a national bank charter under the NBA unless the resulting entity accepts deposits.<sup>1</sup>

#### How would an OCC Payments Charter be treated under banking laws?

Brooks’ proposed interpretation of the NBA in essence threads the needle of a number of banking law requirements. The OCC would charter payments entities as national banks, as a payments company would satisfy the requirement that a national bank be an entity engaged in lending, payments or the taking of deposits.<sup>2</sup>

The payments entity would not in fact accept deposits, which would mean that the payments entity would not fall within the definition of a “bank” under the Bank Holding Company Act of 1956, as amended (the “BHCA”), and entities that control the payments entity would not be bank holding companies and subject to the nonbanking and other restrictions of that statute.<sup>3</sup> However, as the payments entity would be a national bank, it would be a member of the Federal Reserve System.<sup>4</sup> The payments entity also would technically be *eligible* to apply to accept deposits and apply for deposit insurance from the Federal Deposit Insurance Corporation (“FDIC”), and therefore would appear to be eligible for direct

<sup>1</sup> See <https://www.consumerinsights.com/wp-content/uploads/sites/490/2020/07/lacewell-v-occ-br-for-appellee-as-filed.pdf>.

<sup>2</sup> 12 C.F.R. § 5.20(e)(1)(i) (2020).

<sup>3</sup> 12 U.S.C. § 1841(c) (2020).

<sup>4</sup> Id. at § 221. (“The term “member bank” shall be held to mean any national bank, State bank, or bank or trust company which has become a member of one of the Federal reserve banks.”)

access to payments services offered by the Federal Reserve Banks, such as ACH and wire transfer services.<sup>5</sup>

## **What would a Payments Charter look like?**

The idea behind this interpretation of the NBA – which has not been the subject of a formal rulemaking, formal legal interpretation or informal written guidance by the OCC – is to provide a nationwide, borderless payments charter to nonbank entities that currently engage in payments activities on a nationwide basis and maintain individual money transmission licenses in some or all of the required states. The OCC considers payments to be a core banking activity that is better conducted in a chartered entity subject to comprehensive supervision and regulation, including capital, liquidity, Bank Secrecy Act and know your customer requirements, and community reinvestment (-like) requirements. Instead of viewing its proposal as creating an entirely new class of entity, then, the OCC considers a potential payments charter to merely be a proposal for the unbundling of traditional banking services that have long been provided together within a bank (lending, payments and deposits). Now, chartered national banks will be able to provide *only* payments services (or in conjunction with lending).

## **Objections to the OCC’s interpretation of the NBA**

Not surprisingly, certain advocacy groups have lined up in opposition to the OCC’s proposal (in addition to the CSBS’s views described above). Of immediate interest is the joint trades letter sent by the Bank Policy Institute to the OCC (the “BPI letter”) on July 29, 2020,<sup>6</sup> and public comments by Greg Baer, President and Chief Executive Officer of BPI at the Brookings Institute also on July 29, 2020.<sup>7</sup> The BPI letter asked that the OCC run an “open and transparent” process in considering new charters and noted certain policy considerations that the BPI believes should require chartered payments entities to also be subject to the BHCA. Furthermore, Baer noted in his remarks that BPI wouldn’t have any issue with “PayPal” obtaining a payments charter, but would object to a “Walmart” or “Google” being granted one. Baer stated that while banks can do payments processing, not all payments processors are banks, and that the unbundling of financial services in charters is a complex exercise that raises issues of the separation of banking and commerce.

## **So what is the difference between PayPal and Walmart or Google?**

PayPal is primarily a payments and financial services company operating as a nonbank, while both Walmart and Google are primarily commercial entities that may like to bundle financial services with their other commercial offerings. In BPI’s view, it would not raise any policy issues if PayPal were to become a bank, while it would raise significant, material policy issues if large commercial entities were to gain banking powers.

Provided the OCC is receptive to BPI’s comments, is there a simple method for distinguishing between these two sets of entities? Well, in one sense, relevant law already provides for such a distinction. Varo Money was recently granted a full national bank charter, while Square and Nelnet were granted status as federally-insured, state-chartered industrial loan companies (“ILCs”) by the FDIC and the State of Utah. All of these entities appear to be primarily engaged in financial services.<sup>8</sup>

---

<sup>5</sup> Neither the Board of Governors of the Federal Reserve System, which is responsible for interpreting the BHCA, nor the FDIC has confirmed their agreement with these analyses.

<sup>6</sup> See <https://bpi.com/recent-activity/joint-trades-submit-letter-to-occ-in-response-to-proposed-payments-charter/>. The entities signing the letter were the American Bankers Association, the Bank Policy Institute, the Consumer Bankers Association, the Credit Union Association, the Independent Community Bankers of America, the National Association of Federally-Insured Credit Unions and the Clearing House.

<sup>7</sup> See <https://www.brookings.edu/events/fixing-americas-payment-system-the-role-of-banks-and-fintech/>.

<sup>8</sup> See <https://squareup.com/us/en>, <https://www.nelnet.com/welcome> and <https://www.varomoney.com>.

On the other hand, Walmart withdrew its application for an ILC charter, and the application by Japanese commercial entity Rakuten for an ILC has raised controversy.<sup>9</sup> These entities are not primarily engaged in financial services.

So it seems, as a minimal test of whether an entity should be granted a payments charter by the OCC, the OCC should determine whether the entity is primarily engaged in financial services. Such entities are, in essence, performing banking activities outside of the regulated financial system, and both they and existing banks would be well-served by being subject to a level, consistent regulatory playing field for the provision of such services.

### **Is there a relatively simple method for determining whether an entity is predominantly engaged in financial services? There is!**

Fortunately, federal law has already defined a test for whether an entity is “predominantly engaged” in financial activities. This definition was first introduced in the Gramm-Leach-Bliley Act of 1999 (“GLB Act”), which added the following definition as BHCA Section 4(n)(2):

#### **(2) Predominantly financial**

For purposes of this subsection, a company is predominantly engaged in financial activities if the annual gross revenues derived by the holding company and all subsidiaries of the holding company (excluding revenues derived from subsidiary depository institutions), on a consolidated basis, from engaging in activities that are financial in nature or are incidental to a financial activity under subsection (k) represent at least 85 percent of the consolidated annual gross revenues of the company.<sup>10</sup>

This test was adapted and expanded by the Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010 (“Dodd-Frank”) to define nonbank entities potentially subject to designation as “systemically important” pursuant to Title I of Dodd-Frank. The revised definition was promulgated in 12 C.F.R. § 242.3, and provides (in substantial part):

(a) In general. A company is “predominantly engaged in financial activities” for purposes of this section if--

(1) The consolidated annual gross financial revenues of the company in either of its two most recently completed fiscal years represent 85 percent or more of the company's consolidated annual gross revenues (as determined in accordance with applicable accounting standards) in that fiscal year;

(2) The consolidated total financial assets of the company as of the end of either of its two most recently completed fiscal years represent 85 percent or more of the company's consolidated total assets (as determined in accordance with applicable accounting standards) as of the end of that fiscal year; or

(3) The Financial Stability Oversight Council, with respect to the definition of a nonbank financial company for purposes of Title I of the Dodd-Frank Act (other than with respect to the definition of a significant nonbank financial company), or the Board, with respect to the definition of a significant nonbank financial company, determines, based on all the facts and circumstances, that--

(i) The consolidated annual gross financial revenues of the company represent 85 percent or more of the company's consolidated annual gross revenues; or

---

<sup>9</sup> See <https://corporate.walmart.com/newsroom/2007/03/15/wal-mart-withdraws-ilc-charter-application> and <https://bankingjournal.aba.com/2019/08/aba-bpi-rakuten-ilc-application-inconsistent-with-fdic-standards/>.

<sup>10</sup> 12 U.S.C. § 1843.

(ii) The consolidated total financial assets of the company represent 85 percent or more of the company's consolidated total assets.

A slightly different definition was adopted by the FDIC for purposes of implementing certain resolution provisions of Title II of Dodd-Frank.<sup>11</sup> This test also is triggered by an entity's financial activities reaching or exceeding 85 percent of consolidated revenue.

## **Conclusion**

We propose that the OCC's stated purposes of unbundling financial activities and bringing a nationwide banking charter to entities currently outside of the banking system would be well served through adopting the requirement that any payments entity applying for a charter be "predominantly engaged" in financial activities. Application of this test would address many of the objections being raised by banking trade groups that the OCC's actions may violate the Congressionally imposed separation of banking and commerce and create an uneven playing field for entities engaged in similar businesses.

---

<sup>11</sup> 12 C.F.R. § 380.8.

## Financial Institutions Regulation Group Contacts

### New York | 55 Hudson Yards, New York, NY 10001-2163

Wayne M. Aaron	<a href="mailto:waaron@milbank.com">waaron@milbank.com</a>	+1 212.530.5284
George S. Canellos	<a href="mailto:gcanellos@milbank.com">gcanellos@milbank.com</a>	+1 212.530.5792
Douglas J. Landy	<a href="mailto:dlandy@milbank.com">dlandy@milbank.com</a>	+1 212.530.5234
Catherine Leef Martin	<a href="mailto:cmartin@milbank.com">cmartin@milbank.com</a>	+1 212.530.5189
John Williams	<a href="mailto:jwilliams@milbank.com">jwilliams@milbank.com</a>	+1 212.530.5537

### Washington, DC | 1850 K Street, NW, Suite 1100, Washington, DC 20006

Nicholas A. Smith	<a href="mailto:nsmith@milbank.com">nsmith@milbank.com</a>	+1 202.835.7522
-------------------	--	-----------------

### London | 10 Gresham Street, London EC2V 7JD

Joel Harrison	<a href="mailto:jharrison@milbank.com">jharrison@milbank.com</a>	+44 20.7615.3051
---------------	--	------------------

## Financial Institutions Regulation Group

Please feel free to discuss any aspects of this Client Alert with your regular Milbank contacts or any member of our Financial Institutions Regulation Group.

This Client Alert is a source of general information for clients and friends of Milbank LLP. Its content should not be construed as legal advice, and readers should not act upon the information in this Client Alert without consulting counsel.

© 2020 Milbank LLP All rights reserved. Attorney Advertising.  
Prior results do not guarantee a similar outcome.