MILKEN INSTITUTE
CENTER FOR FINANCIAL MARKETS

1101 New York Avenue, NW Washington DC, 20005
WWW.MILKENINSTITUTE.ORG

May 31, 2016

Thomas Curry
Comptroller of the Currency
U.S. Office of the Comptroller of the Currency
400 7th Street, SW
Washington, D.C. 20219
innovation@occ.treas.gov

Re: Responses to the Office of the Comptroller of the Currency's White Paper: Supporting Responsible Innovation in the Federal Banking System

Dear Comptroller Curry,

The Milken Institute Center for Financial Markets would like to thank you for the opportunity to respond to the Office of the Comptroller of the Currency (OCC) white paper *Supporting Responsible Innovation in the Federal Banking System: An OCC Perspective*.[1]

The Milken Institute (the Institute)[2] is a nonprofit, nonpartisan think tank determined to increase global prosperity by advancing collaborative solutions that widen access to capital, create jobs and improve health. The Center for Financial Markets (CFM)[3] promotes financial-market understanding and works to expand access to capital, strengthen and deepen financial markets, and develop innovative financial solutions to the most pressing global challenges.

The Institute commends the work being undertaken by the OCC towards developing a regulatory framework supportive of responsible innovation and recognizes the inherent difficulty of trying to "strike the right balance" between supporting innovation and ensuring that appropriate regulatory protections are in place. FinTech — the use of technology to facilitate the development of innovative financial services and products — is presenting both opportunities and challenges to the financial system and the regulatory frameworks that underpin it.

[1] Available at: http://www.occ.gov/news-issuances/news-releases/2016/nr-occ-2016-39.html
[2] http://www.milkeninstitute.org/
[3] http://www.milkeninstitute.org/centers/markets

Since the launch of CFM's FinTech Program[4] the Institute has worked to understand the innovative changes occurring within the financial system, while providing regulators and policymakers with practical policy and regulatory recommendations derived, in particular, from roundtable meetings that we convene.[5] The Institute is encouraged to hear that the OCC has formed an internal team of experts to study the innovative products and services being developed, as well as to understand the magnitude of the changes occurring within the financial services industry. We offer our support in efforts to develop flexible approaches supportive of responsible innovation.

Our comments focus on the bureau's interest in creating a centralized office of innovation. What follows are recommendations on how the OCC should approach the creation of this office of innovation and suggested topics that should be discussed from the outset.

Building an office of innovation: Defining its Mission

The Institute is supportive of the OCC's interest in the creation of a centralized office of innovation, although its scope and mandate need to be clearly defined. A more-streamlined process for discussion among relevant OCC staff (and departments) could lead to better and more refined communication regarding innovations taking place within and outside of the OCC's purview. A coordinated and streamlined process could provide regulatory clarity to both banks and nonbanks developing innovative products and services. While few details were provided as to the responsibilities for such an office, we would encourage the OCC, if it intends to pursue this idea, to release a draft framework on the office for public comment.[6]

If the OCC is intent on moving toward the creation of an office of innovation, we would offer the following preliminary recommendations:

- **From the outset the OCC should define the mandate for the office of innovation.** Will the office merely be used to facilitate engagement between OCC staff and industry stakeholders? Or will it also provide an environment similar to the Consumer Financial Protection Bureau's (CFPB)

[4] http://www.milkeninstitute.org/fintech
[5] CFM has convened a number of roundtables both in the U.S. and abroad since the launch of our FinTech program in October 2014. Participants include industry stakeholders, regulators and other government officials, policymakers, academics, legal experts, and others. CFM has published a number of white papers based on those discussions which are available on our website. For further details, please contact Jackson Mueller at jmueller@milkeninstitute.org.
[6] If the OCC does move forward on creating an office of innovation, the Institute would recommend that OCC staff review a white paper released at the launch of our FinTech Program which provides a menu of approaches, principles, and processes (their pros and their cons) conducive to the development of regulatory frameworks responsive to financial innovation. Available at: http://www.milkeninstitute.org/publications/view/665

Project Catalyst or the UK Financial Conduct Authority's Project Innovate, in which stakeholders are given the opportunity to test and refine their products and services in a controlled setting prior to full rollout?

- **The OCC should define the scope of its activity.** Given the various regulatory initiatives underway to address innovation across multiple U.S. regulatory agencies, how will the OCC's effort in developing a framework conducive to responsible innovation differentiate? How will the office coordinate with other regulators? Or, going a step further, does the OCC intend for the office to act as lead in an interagency effort to address and support innovative financial products and services?

- **The OCC should define the internal structure of the office of innovation.** Will the current OCC working groups covering marketplace lending and payments systems policy fall under the responsibility of the office? And will the office create additional working groups to focus on innovative products and services that fall outside of the scope of the two current working groups? How can interested parties participate and what are the objectives of each working group?

Building an office of innovation: Suggested Topics to Discuss at the Outset

Separate from the formation of the office and its various working groups, the Institute would also recommend that the following issues be discussed at the outset: interagency coordination amid overlapping regulations and jurisdictions, creation of a regulatory sandbox, the development of a nonbank licensing regime, support for efforts to enhance access to capital through partnerships between nonbanks and traditional financial institutions, international competitiveness for FinTech, and continually evolving customer preferences as they relate to financial products and services.

- ***Interagency coordination.*** The U.S. regulatory system is complex with multiple levels of regulators operating at the state and federal levels, which can often act as a barrier to innovation. For instance, the Federal Reserve Banks of Boston and Atlanta released a report in 2014 on the regulatory landscape for mobile payments. The report identifies roughly 10 federal and state regulatory agencies interested in or engaged in the regulation of mobile payments.[7]

---

[7] Susan Pandy. "Update on the U.S. Regulatory Landscape for Mobile Payments: Summary of Meeting between Mobile Payments Industry Workgroup (MPIW) and Federal and State Regulators May 7, 2014." August 18, 2014. Available at: http://www.bostonfed.org/bankinfo/payment-strategies/publications/2014/summary-of-mpiw-meeting-may-2014.pdf

The question of who regulates is incredibly important. As the Institute stated in a recent white paper:[8]

"The question of who will regulate is both important and challenging. Different types of regulators have different levels of authority, procedures, means of enforcement and jurisdictions. They also tend to operate at different speeds and may possess different levels of sophistication. Finally, the number of regulators with which a market participant must deal can significantly affect the regulatory burden. These differences of type, speed and number can be relevant questions about which regulator is best suited to address a particular issue."

The working groups under the office of innovation should identify areas where OCC jurisdiction overlaps with other federal/state regulators and offer recommendations on how the OCC should work with these bodies in order to provide consistent and transparent communication and guidance, thereby providing clarity to innovators working within and outside of the OCC's jurisdiction. The working groups should also identify whether the OCC should propose a no-action letter policy similar to the CFPBs, but that is more expansive in that it binds or secures the buy-in of other regulators that have jurisdiction in regulating a certain financial product or service in order to reduce regulatory uncertainty on the part of innovators whose products may cross multiple regulatory jurisdictions.[9]

- ***Pilots and trials & regulatory sandbox approaches.*** The cost of having to figure out what rules and regulations apply to innovative financial products and services in a regulatory environment that has grown more complex can act as a barrier, particularly to smaller firms, and often discourages entrepreneurs from entering a certain space. Laws and regulations are in place to ensure the protection of the end-user and the stability of the financial system overall, instilling confidence and providing affected parties with the means to seek redress for any wrongdoing. However, regulations that are too strong or too prescriptive can frustrate efforts to improve upon a certain industry or business segment, thereby denying end-users the benefits that could be derived from such innovation.

[8] Brian Knight. "FinTech: Who Regulates It and Why It Matters." April 2016. Available at: http://www.milkeninstitute.org/publications/view/794

[9] The CFPB released its proposed no-action letter policy in October 2014 and issued its final policy statement in February 2016. The Milken Institute submitted comments on the CFPB's proposal on December 30, 2014. In the final policy statement, the CFPB states: *"While the Bureau may, in some circumstances, have the authority to issue waivers of otherwise-applicable legal requirements, or to establish definitive interpretations of legal requirements, or take similar actions, NALs issued under today's Policy are limited to a statement by Bureau staff that it does not intend to recommend enforcement or supervisory action by the Bureau. As such, they are not intended to bind other agencies. Other agencies will remain free to make independent determinations concerning their respective authorities and concerns."*

Providing space for both banks and nonbanks to test or pilot new products and services in a limited setting prior to full rollout would help educate the OCC on a potential product's risks and benefits and allow the agency to better tailor its policies. Under the direction of the office of innovation, working groups should discuss the creation of a regulatory sandbox where firms can experiment with innovative products and services, and where regulators can see first-hand how the innovations work and what benefits and risks they pose. This effort has the potential to offer regulators the chance to engage industry early on in product or model development while also ensuring adequate protections are built into the product or service prior to full rollout.

Similar efforts are underway at the U.S. Securities and Exchange Commission (SEC) and the CFPB. For instance, the SEC approved a proposal last year "for a two-year pilot program that would widen the minimum quoting and trading increments–or tick sizes–for stocks of some smaller companies." The SEC is interested to discover "whether wider tick sizes enhance the market quality of these stocks for the benefit of issuers and investors."[10] Separately, the CFPB launched Project Catalyst in November 2012. The initiative is designed "to encourage consumer-friendly innovation and entrepreneurship in markets for consumer financial products and services."[11] Internationally, the Institute recommends the OCC follow developments occurring in the UK and Australia where efforts are underway to launch regulatory sandboxes to help FinTech startups navigate the regulatory frameworks in each particular country.[12]

- ***Nonbank licensing regime.*** FinTech firms including online lenders and virtual currency firms have expressed interest in federal licensure or a nonbank charter. This is an issue that the Institute has explored, and has offered a suggested framework on what a national charter could look like for online lenders, for instance.[13] [14]

---

[10] The SEC approved the tick-size pilot proposal on May 6, 2015. On October 6, 2015 the SEC issued an order delaying the implementation of the pilot program by five months. The pilot program will now begin on October 3, 2016.

[11] As stated in the CFPB's November 2012 press release, the CFPB "will establish firm lines of communication with innovators, understand new and emerging products in the market, and engage with innovators." More information available at: http://www.consumerfinance.gov/about-us/newsroom/consumer-financial-protection-bureau-launches-project-catalyst-to-spur-consumer-friendly-innovation/

[12] On May 4, 2016 the Australian Securities & Investments Commission (ASIC) noted in a press release that a public consultation paper on ASIC's regulatory sandbox proposal, part of ASIC's Innovation Hub, will be published in June 2016. Separately, the UK's Financial Conduct Authority (FCA) launched its regulatory sandbox initiative on May 9, 2016. The FCA is currently accepting applications for the initiative's first cohort until July 8, 2016.

[13] Staci Warden and Brian Knight. "Comments on the Department of the Treasury (TREAS) Notice: Public Input on Expanding Access to Credit Through Online Marketplace Lending." September 28, 2015. Available at: http://www.milkeninstitute.org/publications/view/766

[14] Lalita Clozel. "FinTech Firms Ask About National Bank Charters, OCC Official Says." American Banker. March 10, 2016. Available at: http://www.americanbanker.com/news/law-regulation/fintech-firms-ask-about-national-bank-charters-occ-official-says-1079852-1.html

The Institute recognizes the importance of state law and the unique federalist system that the United States is built upon, but in this day-and-age marked by the rise of borderless platforms powered by low costs and low barriers to entry and the rapid advancement of technological innovation, we believe it would promote efficiency and innovation if efforts were made to harmonize regulatory approaches at the state and/or federal level in order to avoid unnecessary duplication of effort and the high costs associated with a patchwork regulatory system.[15]

- ***Promoting capital access***. In its report, the OCC identifies the “great potential” of responsible innovation in broadening access to capital. As comments to Treasury’s RFI on online marketplace lending (Appendix 1) indicated,[16] partnerships between data-driven lending platforms and incumbent financial institutions could spur capital deployment to underserved segments.

  For instance, there are a number of online platforms currently expanding access to credit and building credit profiles for thin-or-no-file customers.[17] Additional comments to Treasury discussed how online lenders focused on small business lending, in particular, are expanding access to capital in the wake of banks’ post-crisis retrenchment. Online small business lenders also discussed how partnerships with traditional financial institutions and community development financial institutions could lead to an even greater availability of capital if those relationships can help secure Community Reinvestment Act credit. Likewise, we are encouraged to hear of the OCC’s interest in “promoting awareness of other activities that could qualify for Community Reinvestment Act consideration.”

- ***International competitiveness for FinTech.*** Global investment in the FinTech industry grew 75 percent to more than $23 billion in 2015. Since 2010, more than $50 billion has been invested across 2,500 firms operating in this space.[18] FinTech investment has primarily concentrated in

---

[15] The Conference of State Bank Supervisors has suggested modifications to its Nationwide Multistate Licensing System (NMLS) to provide a more streamlined framework for licensing FinTech firms as a way to improve upon the state licensing process in a more coordinated, streamlined fashion. However, not every state participates in the NMLS. Only 32 state agencies were managing money transmitter licenses on the NMLS, while 33 state agencies were managing MSB licenses at the end of 2015, for instance. Furthermore, FinTech firms have expressed reservations about the NMLS in the past. For further details on the NMLS see here: https://www.csbs.org/srr/Documents/SRR_2015AR_Web.pdf

[16] Appendix 1 contains a chart containing some of the key takeaways from the roughly 100 comment letters submitted to the U.S. Department of the Treasury in response to its request for information on online marketplace lending. Questions concerning the chart should be directed to Jackson Mueller (jmueller@milkeninstitute.org).

[17] Oportun, Kiva Zip, LendUp and Lenddo, for instance.

[18] Accenture. “Fintech and the evolving landscape: landing points for the industry.” April 2016. (Pgs. 3-4) Available at: http://www.fintechinnovationlablondon.co.uk/pdf/Fintech_Evolving_Landscape_2016.pdf

the personal/SME business segments, with lending (46%) and payments (23%) as the top two business areas for FinTech investment.[19]

The U.S. takes the lion's share of global venture capital investment in FinTech firms, with more than $7 billion in funding to venture capital-backed companies in 2015 representing more than half of the $13.8 billion invested in venture-backed FinTech firms globally.[20]

Competition doesn't just exist within the various segments that make up FinTech, but is also evident among the growing list of countries that are taking steps to develop more agile regulatory frameworks conducive to the development of FinTech within their own borders. CFM continues to monitor both the international and domestic responses to FinTech.[21] In Appendix 2 attached to this letter, we have identified a few countries who have made significant strides over the past two years to put in place the regulatory infrastructure necessary to support the development of FinTech.

The U.S. cannot remain passive while other countries move forward to implement regulatory regimes accommodative to FinTech. That's not to say that the U.S. should "hurry" in its efforts to support innovation. Given the complexity of the U.S. regulatory system and the diverse number of actors involved in the financial system, moving towards a 21st century regulatory framework — or frameworks — will take time. As U.S. regulators and policymakers continue to promote responsible innovation, however, they need to remain mindful of developments occurring elsewhere, apply lessons learned and possibly adapt or modify workable initiatives to fit the U.S. system.

- ***Shifting preferences and tastes for financial products and services.*** The OCC's report identifies changing demographics as one of the reasons propelling both large and small banks and federal savings associations to adapt to changing preferences (i.e. mobile banking) and shifting demands (i.e. speed, automation, efficiency, and transparency). There is no question that

---

[19] Citi GPS. "Digital Disruption: How FinTech is Forcing Banking to a Tipping Point." March 2016. (Pg. 8) Available at: https://ir.citi.com/D%2F5GCKN6uoSvhbvCmUDS05SYsRaDvAykPjb5subGr7f1JMe8w2oX1bqpFm6RdjSRSpGzSaXhyXY%3D

[20] KPMG and CB Insights. "The Pulse of Fintech, 2015 in Review: Global Analysis of FinTech Venture Funding." March 2016. (Pg. 6) Available at: https://assets.kpmg.com/content/dam/kpmg/pdf/2016/03/the-pulse-of-fintech.pdf. *Note: Report only includes all equity rounds to VC-backed fintech companies.*

[21] See Milken Institute *Currency of Ideas* blogs: Will the Real U.S. FinTech Representative Please Stand Up?; FinTech in Asia: The State of Play; Moving East: FinTech establishing a presence in Asia; The UK FinTech build-out 2.0; FinTech: A new year, a promising future; The UK FinTech build-out: What a difference a decade makes; Are regulators laying the groundwork for 21st century regulation?; and UK government backs fintech industry.

changing demographics are one of the main drivers contributing to the influx of innovations occurring in the financial services sector and CFM has reflected on these changes in prior publications.[22] [23]

For instance, smartphone adoption among millennials and Generation X is widespread. Roughly 90 percent of individuals in the U.S. between the ages of 18 and 44 have a smartphone which provides them with multiple virtual avenues from which to bank and be banked, without ever having to step foot in a local branch.[24] Connectivity to financial institutions, services and products over a mobile/internet device is forever changing the shape and layout of retail banking, in particular.[25] The retail bank branch is not dead, but it is changing to fit the digital demands from its customers.

As a result of this digital transformation to banking, customers' relationships with banks are becoming increasingly defined as transactional versus personal. Nearly 80 percent of respondents to a 2015 survey categorized their relationship with their bank as transactional.[26] Financial innovations bring greater promise in terms of connectivity, but they also present both near-term (employment and cost) and long-term (relationship-driven) challenges to institutions overseen by the OCC.

Similarly, smartphone ownership is particularly prevalent in Asian, African American, and Latino communities, some of the same communities that have historically lacked access to basic financial services and products. Mobile technology, in particular, offers great promise in its ability to reach unbanked and underbanked households across the U.S., which currently number close to 35 million.[27] As the OCC continues to develop a framework supportive of responsible innovation, it is essential that the agency does not unknowingly or unintentionally impede the potential for financial innovations to bring more people into the financial system.

---

[22] Jackson Mueller. “"Millennials: A New Approach to Handling Money." Newsweek. February 19, 2015. Available at: http://www.newsweek.com/millennials-new-approach-handling-money-308098

[23] Jackson Mueller. "Millennials: Who They Are and Their Impact on the Financial Services Industry." May 13, 2016. Available at: http://www.milkeninstitute.org/publications/view/801

[24] Board of Governors of the Federal Reserve System. "Consumers and Mobile Financial Services 2016." March 2016. Available at: http://www.federalreserve.gov/econresdata/consumers-and-mobile-financial-services-report-201603.pdf

[25] Jackson Mueller. “FinTech: Branchless banking or banking redefined?” April 15, 2015. Available at: http://www.milkeninstitute.org/blog/view/735

[26] Accenture. “2015 North America Consumer Digital Banking Survey: Banking Shaped by the Customer.” Available at: https://www.accenture.com/us-en/~/media/Accenture/Conversion-Assets/Microsites/Documents17/Accenture-2015-North-America-Consumer-Banking-Survey.pdf

[27] The Federal Deposit Insurance Corporation (FDIC). “2013 FDIC National Survey of Unbanked and Underbanked Households.” October 2014. Available at: https://www.fdic.gov/householdsurvey/

Another important point: Millennials are fickle. Not all of the 80 million or so individuals meet the stereotypes commonly associated with this generation. For instance, millennials are largely defined as the "tech-savvy" generation with strong preference for digital financial products and services. While millennials are more receptive to technological innovation in financial services, as the OCC's report states, the largest generation in the workforce (and overall) continues to use traditional financial products and services as well. Cash is still king and the use of the checkbook is still prevalent, despite all the financial applications and services out there seeking to replace them. The OCC, in developing its framework to promote responsible innovation, should remain mindful of the shifting tastes and preferences for financial services and products across the various generations.

Thank you again for the opportunity to address the OCC's efforts to create a framework supportive of responsible innovation. As stated above, the Milken Institute is submitting, as attachments to this letter, one document that highlights the efforts made by select countries around the world toward developing regulatory frameworks conducive to the development of FinTech, and another document that contains some of the key takeaways from each letter submitted in response to the Treasury Department's request for information on online marketplace lending.

Please let us know if we can provide any additional information, and we would be honored to have the opportunity to continue this discussion in person.

Sincerely,

//S//

Jackson Mueller
Deputy Director, FinTech Program
Center for Financial Markets
Milken Institute

//S//

Staci Warden
Executive Director
Center for Financial Markets
Milken Institute