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OVERSEEING THE FINTECH REVOLUTION: DOMESTIC AND INTERNATIONAL PERSPECTIVES ON FINTECH REGULATIONS

HEARING

BEFORE THE

TASK FORCE ON FINANCIAL TECHNOLOGY

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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WITNESSES

TUESDAY, JUNE 25, 2019

APPENDIX

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

OVERSEEING THE FINTECH REVOLUTION: DOMESTIC AND INTERNATIONAL PERSPECTIVES ON FINTECH REGULATIONS

Tuesday, June 25, 2019

U.S. HOUSE OF REPRESENTATIVES,
TASK FORCE ON FINANCIAL TECHNOLOGY,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The task force met, pursuant to notice, at 2:54 p.m., in room 2128, Rayburn House Office Building, Hon. Stephen F. Lynch [chairman of the task force] presiding.

Members present: Representatives Lynch, Scott, Gottheimer, Lawson, Axne, McAdams; Hill, Luetkemeyer, Emmer, Davidson, and Steil.

Ex officio present: Representative McHenry.

Also present: Representatives Himes, Porter, and Hollingsworth.

Chairman LYNCH. The Task Force on Financial Technology will come to order.

Without objection, the Chair is authorized to declare a recess of the task force at any time.

Also, without objection, members of the full Financial Services Committee who are not members of this task force are authorized to participate in today's hearing, consistent with the committee's practice.

Today's hearing is entitled, "Overseeing the Fintech Revolution: Domestic and International Perspectives on Fintech Regulations.

I now recognize myself for 4 minutes to give an opening statement, and I expect the Full Committee Chair to join us shortly.

This afternoon, we begin the work of the Financial Technology Task Force, the first body to examine in depth how advancements in financial technology are transforming the relationship between the financial services industry and the consumer. A change in financial services is usually driven by a crisis, like we saw in 2008, and during the Depression. However, this change is not driven by crisis, but by consumer preference. It is driven by changes in technology, available to nearly every consumer.

However, the velocity of this change is immense and unprecedented, and we need to encourage responsible innovation. Today, we will receive testimony on how regulators are seeking to harness the potential benefits and mitigate the potential risks of the fintech revolution. Most Members of Congress grew up in a traditional financial world that required us to use a local brick-and-mortar branch and build a relationship with a local banker. That, unfortu-

nately, is no longer the case. Today, someone who wants to open a bank account, apply for a loan, or send money to friends can do all of those things without leaving home.

Many of the innovations can improve consumer well-being. Digital lending can expand the availability of credit to underserved populations and lower the cost of lending for consumers. Advancements in payments technology can increase the speed and convenience of payments for both people and institutions. Open banking can give consumers better control over their own financial situation.

However, these technological advancements come with risks. Without proper oversight, algorithmic qualifiers can turn alternative data into alternative forms of discrimination, and eliminating the human element in all digital applications can lead to confusion about the actual costs of a product.

Fintech covers many activities, but each new advancement relies on an ever-increasing amount of personal data to be collected, stored, and analyzed. Companies are vacuuming up personal information with questionable levels of consumer consent or data protection. Consumers are being asked to agree to unintelligible privacy policies by companies with little or no track record for securing that sensitive financial information. Consumers often are not told, or are deliberately misled about how their data is collected, used, shared, or sold. Financial services regulators are the tip of the sphere in the fight to protect Americans from bad actors in financial services.

Our consumers' faith in the financial system invariably relies on the ability of our regulators to effectively monitor and guide the entities in their jurisdiction. However, recent crises have badly shaken that faith, and report after report has emerged of banks exploiting the personal information of their own customers and abusing the trust that underpins the success of our U.S. financial system.

With this in mind, I look forward to hearing about how we might address the new landscape of financial services, the benefits and risks that you see, and what Congress should be focused on as we move forward.

With that, I would like to recognize my friend and colleague, the ranking member of the task force, Mr. Hill of Arkansas, for 5 minutes for an opening statement.

Mr. HILL. Thank you, Mr. Chairman, I appreciate you convening this hearing today. I want to begin by thanking Chairwoman Waters and Ranking Member McHenry for their collaboration in creating this important task force. I want to thank our regulatory friends for being here for this important first panel. I look forward to working with my colleagues on both sides of the aisle, as well as the regulatory agencies to find a way to promote and foster innovation for both disruptive innovators and incumbent financial services players, large and small, over the next few months.

In my view, our Fintech Task Force can enhance the understanding of this rapidly developing use of big data and data analytics. This task force should be focused on the American consumer as the ultimate beneficiary. Along the way, we will explore ways and means of customer acquisition and better service, and enhancing financial services to the underbanked, all while making compli-

ance less costly and more effective. When Congress passed the Dodd-Frank Act in response to the 2008 financial crisis, it included thoughtful, necessary provisions for the American consumer, but it also had unintended penalties as a consequence of shifting critical, traditional banking services and functions to nonbanking players.

Bank credit availability has suffered since the crisis, and many nonbank financial institutions like private equity firms, SBICs, BDCs, and fintech companies have grown, and their market share has expanded. Fintech companies, in particular, have seen significant evolvement over the past few years. These companies have appeared to be at odds with financial institutions' incumbents as both are fighting for market share and business.

However, in recent years, both have realized the value each brings to the other and have started developing mutually beneficial partnerships. Today, we hear much more about collaboration, rather than disruption. I want to encourage the regulators to promote these partnerships in innovation, while finding ways to reduce the cost of regulatory compliance. Specifically, I am interested in ways that the third-party vendor due diligence process is handled. As a former community bank executive, I understand the regulatory burdens associated with onboarding a new vendor and I hope that the agencies can work together to enhance this process.

That being said, I understand the importance of banks maintaining a robust level of safety and soundness. With technology constantly changing, banks must ensure that they are protecting their customers' privacy against both cyber hacks and other threats. I am interested in hearing your thoughts as it relates to the use of application programming interfaces (APIs), and other ways that banks are using technology to enhance this safety.

A year ago, the U.S. Treasury issued their very informative fintech report that frequently commends the use of APIs to provide a more secure method of data exchange. I would recommend to the members of this committee that they read this financial innovation report as a foundation for their work on the task force. It provides a great overview of the many topics that we will be discussing in the task force related to regulatory sandboxes, necessary harmonization, open banking, and bank charters, just to name a few.

This hearing will not only serve as a way for the task force members to learn about the ways and means that the regulatory agencies are promoting innovation, but also a way for you to learn the best practices from each other.

In my district, we house two accelerator programs at our Venture Center. The two programs are: Fidelity Information Systems, a Fortune 500 company founded 50 years ago, that serves as a community bank core processor; and last year, the Independent Community Bankers of America (ICBA) selected Little Rock's Venture Center to host its program, which focuses on developing fintech opportunities for community bank partnerships.

During the ICBA program, representatives from the prudential regulators traveled to Little Rock to discuss ways they could learn from this innovation center. This is a great example of how best to collaborate by having all of the players in the same room. We need to ensure these dialogues continue, which will ultimately

allow for better compliance efficiencies, benefits to bank consumers, and help services reach the underserved community.

And, with that, I yield the balance of my time to the ranking member of the full Financial Services Committee, Mr. McHenry, for an opening statement.

Mr. MCHENRY. Thank you, Mr. Hill, and I thank you for your leadership on this important issue of financial innovation. I want to also thank Chairwoman Waters for creating this task force and the AI Task Force.

This is an area where she and I have legislated in the past and hope to legislate in the future. We need to build a broader consensus on this committee and across jurisdictions about how we lean into this new era of technology: the computing power, the quantum computing revolution; and the great opportunities that are happening with the innovation economy more broadly.

And I am encouraged that we can actually have, not a nonideological discussion, but a discussion where ideology is secondary to the nature of the reforms and the technology that is coming onboard. So, I think we can build great consensus through committees like this and the AI Task Force, and that can help drive good bipartisan legislation through the process.

And so I thank you, Mr. Hill, for yielding, and I thank you, Chairman Lynch, for your leadership, especially in such a hotbed of innovation as you represent in the great State of Massachusetts. I yield back.

Chairman LYNCH. The gentleman yields back.

Today, we first welcome the testimony of Paul Watkins, who is the Director of the Office of Innovation at the Consumer Financial Protection Bureau. Second, Beth Knickerbocker, who is the Chief Innovation Officer at the Office of the Comptroller of the Currency.

Third, Valerie Szczepanik—is that correct?

Ms. SZCZEPANIK. "Szczepanik."

Chairman LYNCH. What is it?

Ms. SZCZEPANIK. "Szczepanik."

Chairman LYNCH. "Szczepanik." A lot of points in Scrabble, I will tell you that. She is the Associate Director of the Division of Corporation Finance and Senior Adviser for Digital Assets and Innovation for the Securities and Exchange Commission.

Fourth, Charles Clark, who is the Director of the Department of Financial Institutions for the State of Washington.

And finally, making the trip all the way from London, we are joined by Christopher Woolard, the Director of Strategy and Competition for the United Kingdom's Financial Conduct Authority (FCA).

The witnesses are reminded that your oral testimony will be limited to 5 minutes.

And without objection, your written statements will be made a part of the record.

Mr. Watkins, you are now recognized for 5 minutes.

STATEMENT OF PAUL WATKINS, ASSISTANT DIRECTOR, OFFICE OF INNOVATION, CONSUMER FINANCIAL PROTECTION BUREAU (CFPB)

Mr. WATKINS. Thank you so much, Mr. Chairman, and good afternoon, Chairman Lynch, Ranking Member Hill, and task force members. I am Paul Watkins, the Assistant Director for the Bureau's Office of Innovation. Previously, I was the chief counsel of the Civil Litigation Division in the Arizona Office of the Attorney General. There, I managed the State's litigation in areas such as consumer fraud and civil rights. I also designed the State's fintech sandbox.

Today, I am pleased to share what the Bureau is doing in this area. The Bureau created the Office of Innovation in July 2018 to facilitate consumer beneficial innovation. We believe innovation can contribute to the Bureau's statutory purposes by increasing fairness, transparency, competition, and consumer access within financial services. We are working to carry this out through updating the Bureau's innovation policies and creating regulatory sandboxes designed to address regulatory uncertainty that may impede innovation, collaborating with other Federal, State, and global regulators and engaging with stakeholders on innovation issues.

We proposed revisions to the Bureau's existing trial disclosure program in September 2018 and no-action letter program in December of 2018. Those proposed revisions aim to increase the policy's utilization. They generally would streamline the application and review process, focusing on potential risks to consumers. The revisions would also provide increased clarity for recipients.

Also, in December 2018, the Bureau proposed the product sandbox policy. This policy would require participants to share data with the Bureau concerning the products offered, including potential risks to consumers. Similar to the Bureau's current trial disclosure policy, participants would receive safe-harbor protection from liability for certain aspects of the product being tested. Each proposed policy contains provisions designed to deter harm to consumers. We have put the 3 proposals out for public comment and have received about 60 written responses.

Each of our proposed policies states that the Bureau will look to coordinate with other regulators. Internationally, the Bureau, in August 2018, joined the Global Financial Innovation Network (GFIN), an organization of regulatory agencies working to support financial innovation and regulatory best practices. In January 2019, the Bureau became a coordinating member of GFIN.

Since the Office of Innovation was established, I and other members of the office have participated in over a hundred innovation-related meetings and events and have interacted with fintechs, financial institutions, consumer advocacy groups, and Federal, State, and international regulators. Other members of the Bureau have, likewise, participated in such events and meetings, including Bureau leadership, senior officials, and staff. Through these engagements, the Bureau is building a significant knowledge base about innovation in the markets for financial services. Thank you for this opportunity to testify, and I look forward to your questions.

[The prepared statement of Mr. Watkins can be found on page 77 of the appendix.]

Chairman LYNCH. Thank you.

Ms. Knickerbocker, you are now recognized for 5 minutes.

STATEMENT OF BETH KNICKERBOCKER, CHIEF INNOVATION OFFICER, OFFICE OF THE COMPTROLLER OF THE CURRENCY (OCC)

Ms. KNICKERBOCKER. Chairman Lynch, Ranking Member Hill, and members of the Task Force on Financial Technology, I am pleased to appear before you to discuss the initiatives at the OCC to support responsible innovation. Responsible innovation enables a vibrant banking system to meet the evolving needs of consumers, businesses, and communities. It promotes economic opportunity and job creation. When done responsibly, innovation increases consumer choice, improves the delivery of products and services, enhances bank operations, and enables financial institutions, including small and rural banks, to more effectively meet the needs of their customers and communities.

Moreover, responsible innovation expands services to unbanked and underbanked consumers and promotes financial inclusion. Innovation has significantly changed how consumers engage with their financial service providers. How banks innovate is also evolving, particularly in the area of bank and fintech partnerships. The OCC supports partnerships between banks and fintech companies that are safe and sound and meet the evolving needs of consumers, businesses, and communities.

The OCC created the Office of Innovation to implement our responsible innovation framework. As Chief Innovation Officer, I head the Office's work to regularly conduct outreach and provide technical assistance to banks, fintechs, and other stakeholders through a variety of channels. These include office hours, listening sessions, and participation in hundreds of meetings, calls, conferences, and events. My office also works to advance awareness and training for OCC staff on emerging trends to foster a culture that is receptive to responsible innovation and to develop staff competencies.

In addition, we conduct research to assess the financial services landscape to inform OCC policy and supervisory actions.

Finally, we put great emphasis on maintaining open channels of communication and information-sharing, with other domestic and international regulators. The OCC's most recent innovation initiative was announced in April when we proposed a voluntary innovation pilot program to support bank testing of activities that could significantly benefit consumers, businesses, and communities, including those that promote financial inclusion.

The program is designed to assist banks in those situations where regulatory or supervisory uncertainty may be a barrier to deploying a new product, service, or process, and where early regulatory involvement may promote a clearer understanding of risks and related issues.

The pilot program will also allow the OCC to further our understanding of innovative products and services and to assist in identifying supervisory approaches that might unintentionally or unnecessarily inhibit responsible innovation. The OCC invited public

comment on its pilot program and is in the process of evaluating the comments we received.

Many fintech companies such as marketplace lenders, payment processors, and custody service providers offer products and services that historically have been offered by banks. Since the early stages of our work, the companies have consistently asked the agency about options to conduct their businesses on a national scale and promote—and potential to become a national bank. The OCC strongly supports the dual banking system and believes that fintech companies engaged in the business of banking should have the option to conduct their businesses through a national bank charter when it makes sense for their business model. The OCC has options available for firms that can meet our rigorous standards.

Fintech companies may choose to consider a full-service national bank charter to engage in a full array of authorized national bank activities including accepting deposits or to apply for a variety of other limited-purpose charters, if they are engaged in a limited range of banking activities.

Regardless of the particular path that a fintech company chooses, all national banks face rigorous examination and high standards that include capital, liquidity, compliance, financial inclusion, and consumer-protection standards.

My written statement also includes some principles for the task force's consideration that we believe are important, for example, facilitating appropriate levels of consumer protection, including by ensuring transparency and informed consent. In addition, laws or changes to laws should be technology-neutral, so that products and services can evolve regardless of changes in technology that enable them.

The OCC is looking forward to working with the task force and continuing to be a resource as members explore important policy considerations related to financial technology. Thank you again for the opportunity to testify today. I am happy to answer questions.

[The prepared statement of Ms. Knickerbocker can be found on page 54 of the appendix.]

Chairman LYNCH. Thank you very much.

Ms. Szczepanik, you are now recognized for 5 minutes.

STATEMENT OF VALERIE SZCZEPANIK, ASSOCIATE DIRECTOR OF THE DIVISION OF CORPORATION FINANCE AND SENIOR ADVISOR FOR DIGITAL ASSETS AND INNOVATION, U.S. SECURITIES AND EXCHANGE COMMISSION (SEC)

Ms. SZCZEPANIK. Thank you, Chairman Lynch, Ranking Member Hill, and members of the task force. Thank you for the opportunity to testify before you today alongside representatives from some of the SEC's key regulatory partners on the important topic of technological innovation in our financial markets.

In October 2018, the SEC launched FinHub, a strong innovation initiative to centralize efforts and leverage expertise across the Commission and focus on key areas in financial innovation. I am the head of FinHub, and I am happy to be here to tell you about its activities and some of its plans. FinHub has tried to innovate the way we regulate. With FinHub, we have built both a platform

and a portal. As a platform, it is a repository of resources for the public. FinHub broadcasts in one place all of the activities and views of the Commission in various areas in financial innovation.

It is also a portal. It is a place for engagement with the public, academia, other regulators and each other, and we engage in a number of ways. First, through FinHub's webpage, entrepreneurs, developers, and their advisers routinely request meetings with the staff, and we have dozens of such meetings in Washington, D.C. Recognizing that not everyone can travel to D.C., we also travel around the country to meet with these people hosting local, peer-to-peer meetups in cities like San Francisco, Denver, New York, and Philadelphia. Later this week, I will travel to Chicago. In these office hour-type events, we meet with innovators developing new technologies, entrepreneurs looking to bring new business to market, advisers and advocates, universities and academics, SEC registrants and those seeking to register, and others. While we can't give legal advice, we can give guidance. We can tell people how we interpret our laws, and we can point out particular issues with potential projects.

Second, we host public events. On May 31, 2019, we held a public fintech forum dedicated to distributed ledger technology and digital assets. This event brought together academics and industry participants to discuss issues before an audience of the public, SEC staff, and staff from other agencies. Approximately 2,000 people attended or viewed our webcast, and it is still available for viewing.

Third, we publish guidance and seek input on specific issues. On April 3, 2019, FinHub staff published a framework to aid market participants in analyzing whether a digital asset is an investment contract and, therefore, a security. On the same day, the Division of Corporation Finance issued a no-action letter to a market participant seeking to issue a digital asset. SEC staff has issued letters welcoming public input on various topics such as legal and investor protection issues concerning digital assets.

Finally, we collaborate internally and externally on initiatives. For example, FinHub staff partners with the SEC's Office of Investor Education and Advocacy to devise creative ways to reach investors. Recently, we launched a mock-up of a fraudulent ICO called the HoweyCoin, where potential investors were redirected to a web page with educational information.

We collaborate regularly with our sibling domestic and international partners. Our level of coordination in this regard is extensive. We are continually exploring ways to improve our efforts, such as by seeking to hire digital asset experts through our visiting scholars program and regularly participating in industry conferences and academic events.

I am scheduled to take part in two upcoming tech sprints, one of them hosted by the FCA. We are committed to understanding the technologies that impact our markets, and we are taking proactive steps to ensure that we have hands-on opportunities to work with these technologies.

Those who engage with the SEC's FinHub will play a critical role in shaping the future of fintech and assuring that the U.S. capital markets continue to adhere to the high standards that have made them so deep, liquid, fair, and attractive for decades. We are eager

to see new beneficial technologies succeed. The long-term promise of these technologies will be achieved if those implementing them comply with the laws, rules, and regulations Congress and the SEC has put in place to further the agency's core mission: protecting investors; maintaining fair, orderly, and efficient markets; and facilitating capital formation.

We encourage market participants to use the materials on FinHub's website as a resource, to consider consulting with securities counsel, and to request further guidance from the staff if questions remain. Regrettably, while some market participants have engaged with us constructively, others have not. The SEC's Division of Enforcement has been and will continue to recommend enforcement actions for alleged violations of the Federal securities laws in order to protect investors in the market.

Thank you for the opportunity to testify before you today about the work of SEC's FinHub and for your support of fintech innovation. I look forward to answering any questions you may have.

[The prepared statement of Ms. Szczepanik can be found on page 70 of the appendix.]

Chairman LYNCH. Thank you.

Mr. Clark, you are now recognized for 5 minutes.

STATEMENT OF CHARLES CLARK, DIRECTOR, DEPARTMENT OF FINANCIAL INSTITUTIONS, STATE OF WASHINGTON, ON BEHALF OF THE CONFERENCE OF STATE BANK SUPERVISORS (CSBS)

Mr. CLARK. Good afternoon, Chairman Lynch, Ranking Member Hill, and members of the task force. Thank you for holding this hearing. My name is Charlie Clark. I am the director of the Washington State Department of Financial Institutions. It is my pleasure to testify today on behalf of the Conference of State Bank Supervisors. I serve as the Chair of the CSBS nondepository supervisory committee, which provides a forum for State regulators to drive initiatives aimed at ensuring that State supervision of nonbank companies, including fintechs, is effective and efficient. My Department oversees more than 17,000 State-licensed nondepository entities.

I have been at the agency as fintechs have emerged, even before they were called fintechs. Our agency has made sure we have stayed a step ahead of these new business models and ensure that consumers are protected. As a primary regulator, State regulators have expertise, data, and real-time insight into how these companies are interacting with consumers and functioning in the marketplace. I welcome the opportunity to discuss State regulators' approach to regulating fintech and our perspective on the impact of technology on our regulated institutions.

State regulation is activities-based. Whether you go to a storefront or use an app, money transmission is money transmission. Similarly, lending is lending. We don't regulate a company differently, just because it calls itself fintech. We look beyond the labels and marketing to understand the underlying activity and how it fits within our State laws. In many instances, we find that a fintech company's activities fit squarely within existing State financial laws and regulations. The Nationwide Multistate Licensing

System (NMLS) is one of the State's regtech solutions. Through solutions for licensing, regulating fintech firms, and through NMLS, we have seen the ongoing impact of fintech across the marketplace. NMLS is tracking in real time the evolution of the marketplace from brick-and-mortar to online.

We recognize that the current intersection between financial services and technology has accelerated change in the industry and the State system. With industry participation, we are leveraging technology and data to create a more networked system of State regulation that functions more efficiently, with strong consumer protections.

State regulators have broadened the scope of how we work together, especially as we recognize that technology is enabling fintech companies to scale rapidly. That is why State regulators are committed to advancing Vision 2020, a set of initiatives designed to harmonize and strengthen State supervision. Current Vision 2020 initiatives include a transformative exam platform called the State Examination System, and a sweeping cybersecurity training program that will train 1,000 examiners by the end of the year. As part of Vision 2020, State regulators have gathered industry input from fintech firms on how to streamline regulation nationwide, while maintaining strong consumer protections and local accountability. Some of the resulting initiatives are a model State law for money transmitters and new tools and resources to help industry and others navigate the State system. Washington State is leading a streamlined, multistate, MSB, licensing initiative. To date, we have 23 States that have signed on to this effort, which is intended to curb duplications in the licensing process and cut redundant work among State regulators.

Through NMLS, fintechs can submit most license application materials only once, reducing the need to go State to State. As noted in greater detail in my written testimony, the States are committed to implementing regtech solutions and collaborating on new ways to improve oversight and enhance consumer protections while reducing regulatory burden. Thank you for the opportunity to testify today. I look forward to answering your questions.

[The prepared statement of Mr. Clark can be found on page 36 of the appendix.]

Chairman LYNCH. Thank you.

Mr. Woolard, first of all, let me publicly thank you for making the effort to be here. The committee was extremely keen on getting your perspective. You are now recognized for 5 minutes.

STATEMENT OF CHRISTOPHER WOOLARD, EXECUTIVE DIRECTOR FOR STRATEGY AND COMPETITION, UK FINANCIAL CONDUCT AUTHORITY (FCA)

Mr. WOOLARD. Chairman Lynch, thank you very much. Ranking Member Hill, members of the task force, thank you for inviting me to give evidence today. As you said, Chairman Lynch, I am a member of the board and an executive director of the Financial Conduct Authority. I also lead our innovation work. I am also chairman of the IOSCO fintech network, which brings together 92 regulators and other members from around the world.

I have submitted written testimony to the committee, but in the interest of time, I just wanted to highlight three points from that: first, to highlight the FCA's approach to innovation policy; second, the importance that we attach to outcomes; and third, the importance of international cooperation in this sphere. And of course, I would be very happy to answer any questions, as well.

Our approach at the FCA rests upon our competition duty. Put very simply, as well as seeking to prevent risks to the system, which all financial regulators do, we also consider the dangers of potentially beneficial innovations not happening or coming to market. Our journey around innovation started in October 2014, when I established something called Project Innovate within the FCA. We had the objective of fostering innovation in the financial services sector in the interest of consumers. We wanted to make it easier for innovators to get their ideas to market and also encourage larger firms to break the mold. For the most part, that has been about connecting those with innovative business models with our existing rule book. We got a huge response to this, including seeing some ideas that were really cutting-edge. In order to manage these, we established something called the FCA sandbox as a place where firms could trial innovative products, services, and business models in a live market environment, normally for a 6-month test, while ensuring that safeguards were in place.

And the thing I should stress is, certainly from our perspective, we believe that sandbox firms have to work in the real world from day one. So, our full suite of rules apply to them. They are fully regulated, and, indeed, sandbox firms are probably our most heavily supervised.

The second point I just wanted to make is that we believe is real importance in terms of outcomes. As you know, there is a lot of hype around fintech. Our work needs to make a real difference in terms of new entrants to the market, consumer offerings, and our own approach to regulation. Now, we think it is making a difference. Demand from firms have been strong. We have had over 1,500 requests for help. Our sandbox cohorts are oversubscribed around 3 times over. We have given 149 regulatory steers since we started this program, and more than a hundred new firms have come to market or have had variations of permission.

The sandbox is in his fifth cohort. We have had over 110 tests, and around 80 percent of the firms that enter the sandbox go on to operate fully in the market. We have also been able to reduce the time it takes us to take innovative firms into full authorization by around 40 percent, which equates around 3 months' reduction in time. We have seen new services in almost all of the sectors that we regulate for, and we believe that millions of consumers have had access to new products geared around better value or greater convenience. There are examples in the documents that I have submitted to the committee, and obviously, I am very happy to talk about them.

We also use those activities to make sure they inform our own policymaking and how we think about using technology ourselves as a regulator, for example, to deal with questions like anti-money-laundering or transformations like digital reporting.

Third, and finally, international cooperation in this sphere is vital. Many of the firms that we see have business models that are geared around international expansion, rather than traditional, domestic business models. We believe that there is work that we can do through both IOSCO and through the new Global Financial Innovation Network that can allow us to tackle cross-border issues in a really meaningful way.

There is already significant cooperation between regulators, as Val already mentioned in her evidence, and we believe that this needs to continue. Now, I recognize that is a very whistle-stop tour of the issues. I hope it gives you a sense of the scale and value that we see in this space. Thank you, once again, for inviting me here today.

[The prepared statement of Mr. Woolard can be found on page 81 of the appendix.]

Chairman LYNCH. Thank you very much. I will now yield myself 5 minutes for questioning, unless Chairwoman Waters is here. No? Okay.

Ms. Knickerbocker, we had the opportunity to speak with Mr. Otting, who came before the Full Committee a couple of weeks ago, and we discussed the OCC's special purpose charter of fintech companies. It is my understanding that as of now, we have no completed applicants. Is that correct?

Ms. KNICKERBOCKER. That is correct.

Chairman LYNCH. Okay. It was recently reported in the press, however, that Google and perhaps some other larger tech companies had reached out to the OCC about the charter. Is there any truth to that?

Ms. KNICKERBOCKER. Not that I am aware of, Mr. Chairman.

Chairman LYNCH. All right. And, of course, we have just received notice that Facebook announced their plans to launch Libra and Calibra, a cryptocurrency and digital wallet. So, we have this merging of—or potential merging to create some conflicts of interest between the heretofore traditional banking world and the tech space. Does the OCC have any concerns about the blending of these two disciplines where there is a fairly fixed and conservative regulatory framework around banking, and that is not at all sort of the culture within the tech community? Any concerns about that marriage?

Ms. KNICKERBOCKER. Well, a couple of things on that. First of all, one of the things that the Office of Innovation does is we spend a lot of time with companies that are not used to the regulated environment, to explain to them if they want to operate in the regulated environment, what that means. And we provide technical assistance to them and spend a lot of time discussing those expectations.

For those companies that have reached out to us around the special-purpose charter, we have further discussions with them about expectations around capital, liquidity, risk management, governance, and those expectations. But I do think it is important to note that there are a lot of activities that have historically been in the banking industry that are now in a wide variety of different places, and they intersect with the banking industry and the regulated environment. We need to be aware of those.

And with the case of Facebook, I will just point out that at least right now with Facebook Libra, there are no banks that are involved. So, the OCC is just monitoring that activity, but if a national bank was involved with Facebook Libra, we would ensure that its activity would be in compliance with the law.

Chairman LYNCH. Okay. Thank you.

Mr. Clark, the CSBS has sued Ms. Knickerbocker's organization, the OCC, over this issue. What are the concerns that have been—I don't want you to talk about the litigation, but just sort of, from the 100,000-foot level, what are the concerns that the State supervisors have raised?

Mr. CLARK. State regulators oppose the special-purpose charter because it lacks statutory authority. It is up to this body, Congress, to decide whether the OCC should regulate these nonbank entities. I think the example you raise creates a perfect example of how such a charter would pick winners and losers. In a State system, currently a small company can enter the system, scale up, and be competitive with an innovative idea. But with very large companies that would essentially get a preference, that creates an unlevel playing field.

Chairman LYNCH. Let me ask you, Ms. Knickerbocker, you have talked about sort of harmonizing—well, at the end of your testimony, you talked about Congress sort of trying to introduce some of this new technology in a way that is not disruptive or damaging to some of the smaller firms. I think you called it technology-neutral legislation. And I struggle with that because you have huge firms with huge resources and great capacity from a technological side. And then I have community banks, so I have to balance that. It sounds good in theory, but I just struggle with it. What do you mean by that? How do we do that up here?

Ms. KNICKERBOCKER. When I referred to technology-neutral, what I was speaking about was there are a lot of different technologies, whether it is cloud-based technology, or different types of distributed ledger technology, so we shouldn't be choosing what type of technology a bank wants to use.

Chairman LYNCH. Okay. It was a different context.

Ms. KNICKERBOCKER. Right.

Chairman LYNCH. I have gone over my time; I apologize for that.

And I now yield to Ranking Member Hill for 5 minutes.

Mr. HILL. Thank you, my friend. Again, thank you to the panel. I thought your testimony was really well-delivered and well-prepared. Thank you for that.

Mr. Watkins, when I looked at the Treasury report issued last summer that I referenced, there were a couple of major congressional issues that were suggested that Congress needs to deal with. One is regarding the *Madden* v. *Midland Funding* case, a topic that affects people extending credit out there called valid-as-made doctrine. Is that something you think that Congress should deal with legislatively, or do you think that is something that the regulators could collaborate on and clarify?

Mr. WATKINS. Thank you for that question, Ranking Member Hill. I do recall that portion of the Treasury report. It is certainly an important issue. To give you a full answer to that, I would probably need to confer with some of my colleagues at the Bureau, as

well as these other agencies to determine what aspects are implicated by our existing jurisdiction and rulemaking and what aspects would require legislative action.

Mr. HILL. What, in the Treasury report, is the CFPB's top-of-mind item to work on?

Mr. WATKINS. We have been implementing several of the items in that report, starting with regulatory sandboxes, which I mentioned briefly in my opening statement. We have revised two existing policies. We have proposed a third. Another area that the report mentioned that is relevant to the Office of Innovation is collaboration, international collaboration through our membership in the Global Financial Innovation Network (GFIN), and also in each of our policies, we have indicated our intent to collaborate with both State and Federal regulators.

Mr. HILL. I think that is important. I think all of our prudential regulators having a similar approach to sandboxes, with similar rules of the road, would make it a lot easier on private market participants, so I encourage you to pursue that.

Mr. Clark, your testimony was very interesting about the national registry system and how that has expanded since Dodd-Frank and your efforts in the State of Washington to lead on uniform laws. The Treasury report suggests that Congress provide guidance on State uniform laws when it comes to lending and money-transmission services, but it also is very clear that the States ought to have 3 years in which to perfect that effort. Can you give me a feel for—I know you have 23 States working. Can you expand on that and talk a little bit about Treasury's report and what the States are doing beyond that one in your testimony?

Mr. CLARK. Sure, absolutely. We were asked to make substantial progress in streamlining and harmonizing licensing and supervision, and we are absolutely doing that collectively as States. We have the CSBS Vision 2020, which has modernized and is working to modernize the NMLS. We are creating a special State examination system to coordinate supervision for national companies. We are creating a national scheduling effort to better coordinate scheduling of MSBs, and I can tell you, in the licensing area, not only is this MSB licensing agreement streamlining the effort where States are sharing work, there is less duplication, but we are also working on a model MSB law, so that we can better collaborate and create harmony among the State laws.

Mr. HILL. Thank you. I look forward to studying your results.

Mr. Woolard, thanks for crossing the pond and being here with us. I am interested in what—after open banking has been in place now for just over a year, what is the key benefit you have noted from a regulator's point of view, and what is the key shortfall? And is it true that, in your standardized approach, APIs are used universally for the transmission of customers' private data?

Mr. WOOLARD. Thank you, Mr. Hill.

We have, with open banking, the rules finally came in sort of full effect in January. So, it is a bit less than a year. But I think there are a number of things we can observe already. First, we have many of the large banks, which I think had some quite serious concerns about this when it was first proposed, are now actively making offerings to their customers around open banking, to consoli-

date their relationships with one particular bank. So, this isn't purely a sort of fintech versus traditional established banks. This is something that is happening across the market. If I look at it objectively, I think there is something about the limited range of products that are currently covered by open banking in terms of sort of current account, checking accounts, payment accounts. And there is a question there about should that be more banking there that is available? And, yes, to your point, APIs are the principal route by which these interfaces are working in a standardized way across the market, in contrast to perhaps other parts of Europe.

Mr. HILL. Thank you, Mr. Woolard.

I yield back, Mr. Chairman.

Chairman LYNCH. Thank you. The Chair now recognizes the gentleman from Georgia, Mr. Scott, for 5 minutes.

Mr. SCOTT. Thank you very much, Chairman Lynch. Congratulations to you—

Chairman LYNCH. Thank you.

Mr. SCOTT. —as the chairman of our Fintech Task Force, and thanks for holding this hearing, and thank you all for coming here and doing such a wonderful job with your testimonies.

Ms. Knickerbocker, I want to kind of—you seemed to really hit the nail on the head with your opening statement when you said, "When done responsibly, innovation can increase consumers' choice, improve the delivery of products and services, and enable financial institutions to more effectively meet the needs of consumers, including those who are unbanked and underbanked businesses and communities." I think you hit it right on the head there, because this is one of the reasons I have been involved in fintech.

I am chairman of the bipartisan Fintech Caucus. And we have a bill that we are working on, along with the Chair of the full Financial Services Committee, Chairwoman Maxine Waters, and it is called the FINTECH Act. And it is to get us into some guardrail situations. Paramount of what we are trying to do is to make sure, because as you know, you are the chief regulator, you are the OCC, you have this special order going out for the fintech's regulation, so it is very important that with all of the different financial regulators, to a degree, to feel they have a piece of fintechs here, it is important for us to get out front a bill that will give harmonization if there are regulatory agencies that may feel each one has a piece of the action. And, hopefully, as we work through this, a point of entry to come into the regulatory system. And so I wanted to say, if you felt that our bill, the FINTECH Act, again, which would establish harmonization among Federal regulators to eliminate duplication and conflicting regulations impacting fintech companies—bipartisan as I said, with my good friend, Barry Loudermilk, and Mr. Luetkemeyer on that side. We have my good friends, Mr. Gottheimer and Mr. Lawson on this side, and of course, we are working with Chairwoman Waters on this bill. So, I would like for you to comment on that. Did you see, do you agree with us, for regulatory harmonization of fintech companies, to allow for certainty and stability as in our FINTECH Act?

Ms. KNICKERBOCKER. Much of the work that the Office of Innovation does, in fact, the majority of the work that we do is working with banks and fintechs to talk about what the expectations are in

operating in a regulated environment and trying to understand where there are uncertainties. And oftentimes, those uncertainties are perceived. And I think it is important that, in order for us to reach those goals that we all believe are important around fintech and the evolution of banking, to be able to break down those perceptions, so that we can operate in a more efficient and effective manner.

Harmonization is also important. It is a little challenging sometimes when you have multiple regulators that have different mandates, but we all are working, I believe, as effectively as we can, to look at opportunities for harmonization. An example of that is the Treasury report had talked about third-party risk management and having the regulators try to find places where we could be more in harmony, if you will. And we have, in fact, done that. There have been a number of discussions about that, and we are continuing to meet, to focus on that, because it is one of the biggest issues, where banks and fintechs partner.

Mr. SCOTT. And so, if you could, very quickly, how would you look at the efforts that are already under way among the Federal banking regulators within fintech? What would be the landscape right now?

Ms. KNICKERBOCKER. I would say that the landscape right now is that we are working very cooperatively. All of us on this panel talk on a regular basis. The Office of Innovation and those groups of the agencies that are focused on innovation work on a regular basis to talk about how we can improve our programs. We share a lot of information.

In addition, now what we are doing, particularly with fintechs or banks that have particular questions that are for another regulator, is we will do introductions through the Office of Innovation, to either Paul's group or Valerie's group, and that has been very effective in reducing some of that uncertainty.

Mr. SCOTT. Thank you very much.

Chairman LYNCH. Thank you. The Chair now recognizes the gentleman from Missouri, Mr. Luetkemeyer, for 5 minutes.

Mr. LUETKEMEYER. Thank you, Mr. Chairman. We have a great panel today, and a great topic. Thank you all so much for being here.

Mr. Woolard, I'm always curious as to how other countries look at these issues and their approach and what they find whenever they do things. From the regulatory standpoint, how is your country looking regulatorily at trying to either control or not control, to be able to allow, not allow, in this particular environment innovators and the people to be able to access this technology, as well as how do you protect the information that they are out there with, if you don't mind?

Mr. WOOLARD. Thank you very much. I think probably the easiest analogy to think of about our approach is it is rather like a pharmaceutical trial. So, you want to get the benefits here. You want to get the innovation into the market that you think might make things better for consumers. At the same time, we are taking an approach where, particularly through the sandbox, if it is something that is very, very new, we want to make sure that it is actually tested properly on a smaller controlled group before that inno-

vation then works its way into the wider environment. That has been our broad approach.

In all of this, what we are trying to do is, as I said, keep—how do we secure innovation in the interest of consumers? We do occasionally see ideas that are incredibly clever, incredibly innovative, but unfortunately, would not have a good impact on the market. And so, it is about making sure that we try and encourage the vast majority of those players that are really trying to bring something new and add value.

Mr. LUETKEMEYER. How do you control security for customers? Are you looking at that as an issue as well when you are going through this, with your sandbox?

Mr. WOOLARD. Yes. All of our standards apply from day one. So, the same standards that we would expect any other regulated entity in the market to have around things like cybersecurity, around the systems and controls to protect consumer data, for example, we would expect those new firms to have also from day one.

Mr. LUETKEMEYER. Okay. You have had a number of sandboxes in place, according to your testimony, for quite some time, and I was curious, have you had any results from that? Have you found things that did work and things that didn't work? Would you share those, please?

Mr. WOOLARD. Yes, of course. We have published an evaluation of our work around sandboxes, which I have tabled as part of my written testimony. But in broad terms, we have seen ideas that have worked across the range of areas that we—

Mr. LUETKEMEYER. Can you give us an example of one?

Mr. WOOLARD. Yes, of course. So, for example, if you take the insurance market, there is a very small firm called CUVVA, C–U–V–V–A, seven guys originally based up in Scotland, who started a very short-term insurance app. You can get your car covered for a few hours or a few days or whatever it might be. When that launched into the market with some new technology that we obviously had to get very close to and understand, we saw the two largest incumbent firms launch a very similar product within months. And this was something that was significantly cheaper for consumers. It was a significantly better product. But it took the entry of a challenger to effectively prompt other players to come forward with those kinds of innovations.

Mr. LUETKEMEYER. Okay. And did you look at—does England have charters for their banks and savings and loans and credit unions and those other financial institutions and—

Mr. WOOLARD. The way we operate is, as part of our founding legislation, there is something called a regulated activities order, which says, if you engage in a certain kind of activity, then you are regulated.

Mr. LUETKEMEYER. Okay. Are you regulating these fintech innovators then, too?

Mr. WOOLARD. Yes, absolutely. In the particular case of the firm I just mentioned, they are operating as an insurer, so we regulate them as if they are an insurer.

Mr. LUETKEMEYER. Okay. Ms. Knickerbocker, you are with the OCC, and Comptroller Otting has been very aggressive in trying to be out front in saying he wants to put charters out there, but by

doing it, he wants to make sure those entities are regulated like banks as well as anything else. I know that there are some concerns there whenever you do that with regards to limiting the ability of those entities to be able to provide services to community banks, credit unions, the smaller entities, because they can't afford to go out and purchase a fintech company, like Bank of America can, for instance. How do you view their relationship, and how progressive can it be?

Ms. KNICKERBOCKER. The relationship between—

Mr. LUETKEMEYER. Yes, the fintechs and the community banks. Where do you see your place in that?

Ms. KNICKERBOCKER. We see a lot of opportunity for community banks to partner with fintechs. Because you are right, they have challenges in terms of building or buying, and they can have a lot of success in reaching their customers through fintech relationships. A large amount of my time is spent talking to community banks about how to do that in a safe and sound manner, things to think about with respect to their strategy. And there are a number of successes out there that we have seen with community banks.

Mr. LUETKEMEYER. Okay. My time is up. Thank you, Mr. Chairman.

Chairman LYNCH. Thank you. The Chair now recognizes the gentleman from New Jersey, Mr. Gottheimer, for 5 minutes.

Mr. GOTTHEIMER. Thank you very much, Mr. Chairman.

And thank you to all of the witnesses for being here today. As the U.S. and global financial systems continue to evolve at a breakneck pace, this hearing could not come, in my opinion, at a more appropriate time. I want to start with something I have been working on recently, expanding the sources of data included in credit scores, so we can help those who are thin-filed or credit-invisible, get the access to credit they deserve.

Recent advances in digital technology have allowed fintech lending to emerge as a potentially promising solution to reduce the cost of credit and increase financial inclusion. According to an IMF study, one of the best ways fintech has the potential to enhance financial inclusion and outperform traditional credit scoring is by looking at nontraditional data sources to improve the assessment of the borrower's track record. If I can ask everyone this question—we will start over here, Mr. Watkins, if you don't mind—yes or no, would you agree that credit-scoring models have a responsibility in today's financial services world to consider alternative data sources like rent and monthly telecom payments? If I could start with you, sir?

Mr. WATKINS. Thank you for that question, and I know you asked for a yes or no answer, and I don't want to disappoint you right off the bat, but the uses of alternative data certainly pose some of the benefits that you have identified and, I agree, is an essential component of fintech development—

Mr. GOTTHEIMER. Thank you, sir.

Mr. WATKINS. —and is something that we are working on. Thank you.

Mr. GOTTHEIMER. Ma'am?

Ms. KNICKERBOCKER. Banks have been using alternative data to supplement credit scores, like utility and rent payments, for quite

some time. So, with respect to alternative data, to supplement if there is a credit nexus—

Mr. GOTTHEIMER. So you agree?

Ms. KNICKERBOCKER. I would agree.

Mr. GOTTHEIMER. Okay. Thank you. Ma'am?

Ms. SZCZEPANIK. It is not directly within our regulatory remit, but it sounds reasonable to me.

Mr. GOTTHEIMER. It is a good idea. Sir?

Mr. CLARK. Yes, provided that the model doesn't violate the law, including the fair lending law.

Mr. GOTTHEIMER. Thank you. Sir?

Mr. WOOLARD. As part of our innovation work, we have actually authorized the first new credit reference firm in the U.K. for many years that does use alternative sources of data. We also have the Treasury in the U.K. undertaking a trial at the moment of whether you can bring, on a more consistent basis, things like rent payments into a wider credit score.

Mr. GOTTHEIMER. Thank you very much, sir. I have also personally heard from several companies as we have talked about today, in trying to provide regulatory clarity for emerging fintech firms, many have been instructed to set up shop in countries like Singapore, Switzerland, Bermuda, and beyond, to avoid the lack of regulatory certainty we have here in the United States when it comes to digital assets. That is why I partnered with Representative Davidson on legislation that would help provide this much needed clarity.

Ms. Szczepanik, do you believe that the current regulatory authority over digital assets is harming the United States' global standing when it comes to this technology?

Ms. SZCZEPANIK. Thank you for that. We believe that we have been quite clear in how we are viewing things. We have put out guidance, at least on ICOs beginning in 2017, about how we apply the law to the issuance of digital assets. We have put out a number of statements since then, and we believe that the guidance is clear. To the extent folks still have questions, we have been welcoming folks to come talk to us. We have dozens of meetings to talk to people about particular projects and how we would apply our laws.

Mr. GOTTHEIMER. Have you heard also that there is some uncertainty? A lot of people visit us and say, they are not really sure who the regulator is or which rules to follow, and yet we should be the premier destination for blockchain and cryptocurrencies and other digital instruments, and a lot of people raise this as an issue. You have definitely heard there is some fuzziness here, right?

Ms. SZCZEPANIK. Sure. And we look at it, each digital asset is its own animal. It has to be examined on its facts and circumstances to determine what, in fact, it is. It could be a security. It could be a commodity, it could be something else. We stand ready to provide guidance to folks if they want to come talk to us. We encourage them to come talk to us before they do anything so they can get the benefit of our guidance. To the extent that folks move offshore, for example, if they are still conducting business within the United States, we believe our laws would still apply to the conduct that occurs in the United States.

Mr. GOTTHEIMER. Okay. Thank you very much.

I yield back. Thank you.

Chairman LYNCH. Thank you. The Chair now recognizes the gentleman from Ohio, Mr. Davidson, for 5 minutes.

Mr. DAVIDSON. Thank you, Mr. Chairman, and I want to congratulate you and the entire committee on the establishment and first hearing of the Fintech Task Force. It is a bit of an achievement for, really, our committee. I think it is progress for this body and Congress, to tackle an incredibly important sector for America's economy and, indeed, the global economy. As some of you know, almost a year and a half ago, I set out to find a bipartisan solution to properly and effectively regulate digital assets. As Mr. Gottheimer, who is a cosponsor of a bill I created, the Token Taxonomy Act, highlighted, many firms come to us and say that they don't have the regulatory certainty in the United States, and consequently American firms, American innovators aren't leaving the United States to avoid U.S. regulations. They are leaving overwhelmingly to find regulatory certainty that they cannot find in United States markets. It is not a coincidence that Facebook launched outside the United States. Switzerland has some of the most clearly established regulatory framework. They all say that they are looking for this certainty, and they are effectively attracting much more capital than the United States is, Singapore and Switzerland, in particular.

Mr. Woolard, on March 15, 2019, the FCA updated their policy on defining crypto assets to distinguish three types of tokens, as well as recommendations regarding mitigation of illicit activities and cyber threats. Many legal experts have said that FCA's policy is very similar to Switzerland. Would you agree with that?

Mr. WOOLARD. I think our policy actually is still a bit distinct from the Swiss one. They have, I think, gone further in terms of how they have tried to define a jurisdiction around crypto assets. What we are trying to do is actually, I think, 9 million miles away from the approach the SEC outlined, in many ways. So, we see there are three different, distinct kinds of uses and activities. And we regulate according to what is the underlying business that someone is trying to conduct around crypto assets. But there is more work that we are doing in this space and certainly more thinking that we need to do.

Mr. DAVIDSON. Thank you. Some of my colleagues have asked me why I feel such an urgency on putting a legislative text out here, and the reality is that we do differentiate. In the main bill, the base piece is: What is a security, and what is not? A clear definition that is in line with the Howey test, that has long been established in the U.S. but provides a four-point criteria that gives certainty so that not every company is forced to say: Gee, I can go cut my own deal, and it is company by company. This is a third-world developing economy kind of approach to, hey, if you want to launch a company, you go and negotiate with the government, and maybe you can get your deal, and maybe your deal is different than this other person's deal. We need the certainty that if you do these things, you will be deemed an asset, and that has been one of the drawbacks of regulatory guidance. It is guidance, and it is often the case that it is not found to be binding. Then, you wind up with a

patchwork of court decisions that try to discern things after the fact. And, frankly, it scares off capital.

I think we are—personally, I feel passionately that we are well beyond the sandbox stage in the United States, and we need a minimal touch, one of the things that the United States did brilliantly with the Telecommunications Act in the 1990s that allowed technology and innovation to flourish in the United States of America. And thankfully, many of my colleagues agree. We have eight cosponsors, and we continue to grow. It is clearly not an ideological bill. It spans from people on the furthest left of our political spectrum to towards the right end of our political spectrum. And so, I hope that we can move forward and begin to debate this text. As we would potentially say in Ohio, the field has been plowed; we are ready to plant. So, we have a framework. And as talk about international perspectives on fintech regulation and digital economy, we need to talk about a range of things. And I guess, Ms. Szczepanik, you have highlighted some of the work that the SEC has done. Do you feel the sense of urgency, would it add something to have this clarity?

Ms. SZCZEPANIK. Thank you. I think it is good to remember that distributed ledger technology is nascent, and it is fast evolving. Our laws that we have currently are flexible and principles-based and very broad, and they have assisted us over the years in taking in all kinds of new technologies as they occur. This isn't the first time we have had a new technology come to bear. I think we regulate around activity and conduct.

Mr. DAVIDSON. Thank you. And I agree, you have to look at the conduct, but look, it has been 5 or 6 years. It is not nascent. It has been around for a while. And I think some minimal law is out there, and we have a wide range of issues that would need to be dealt with, including how to deal with exchanges, all the anti-money-laundering BSL, know-your-customer provisions, and so this is just the tip of the iceberg. Thankfully, we have this task force on board ready to tackle this and a number of issues in the space. My time has expired, and I yield back.

Chairman LYNCH. Thank you. The Chair now recognizes the gentleman from Utah, Mr. McAdams, for 5 minutes.

Mr. MCADAMS. Thank you, Mr. Chairman, and thank you all for being here today. My State of Utah is home to a thriving technology and financial services industry, largely centered on what we call the silicon slopes. We have lending companies and payment processing and development of artificial intelligence systems, the use of Big Data, and much, much more. This growing fintech industry has been a boon for our local economy, and ultimately, I think a boon for consumers who will benefit from these advances in technology, many of which are already some household names.

I want to encourage innovation and the next generation of technologies here at home, but I also recognize that government does play a role in setting boundaries to make sure consumers are properly protected. It is often a matter of fine-tuning, and fine-tuning that dial between appropriately protecting consumers and unleashing innovation. And so, I want to focus on how we get the dial setting correct in that regard.

I guess my first question would be for Mr. Clark. One of the beauties and challenges of our Federal system is that we have 50 different States sometimes pursuing policy in 50 different ways. And this can lead to some frustration for companies operating nationwide who must comply with a myriad of different requirements. But it does also allow for innovation and experimentation at the State and local level to see what works best. The CSBS represents State regulators who regulate both banks and nonbanks alike. Are there any particular approaches to fintech and innovation that States have pioneered, that work particularly well, that we should look to replicate at the Federal level?

Mr. CLARK. I can tell you that, when Congress has looked at the role that State banking regulators play and their important role in regulation, and looked at the benefits, we have come up with some great solutions. In the mortgage area, you passed the SAFE Act, which provided some uniformity, but it relied on the States to continue to examine and make sure that they are a gatekeeper for bad actors.

Another tool that I think would really help with helping State regulators encourage a partnership between fintechs and banks is if Congress passes H.R. 241, the Bank Service Company Examination Coordination Act. That way, State regulators could be able to more easily share information with Federal counterparts.

Mr. MCADAMS. And I guess a question for any of the panelists, but—maybe a two-part question—do nonbank or fintech companies present any unique challenges in supervision, and is data security and privacy a particular concern? And share with me your thoughts on data privacy in the Congress.

Ms. Knickerbocker, you seem to be—yes, go ahead?

Ms. KNICKERBOCKER. Data security and data privacy are really key, particularly as we move into an environment that is almost exclusively digital. The OCC focuses a great amount of time with respect to cybersecurity and understanding the importance of privacy with respect to consumers, and it really needs to be a part of the work of the task force.

Mr. MCADAMS. I started my comments talking about the fine-tuning of this dial between appropriately protecting consumers—and that can be everything from predatory lending practices to the privacy and data privacy of consumers—but also making sure that we don't have such a heavy regulatory hand that we squelch innovation, that we allow some of this innovation to continue to move forward. And I think that is the quandary between that, of that tuning of that dial is ever present in the area of data security and data privacy. What should we be looking at? You see various States stepping forward with data privacy regulations and protections and some innovations in that regard, but also that is an area where a national framework may be interesting. What should we be thinking about as it relates to data privacy and regulation or freedom of data?

Mr. CLARK. I can tell you that the States are closely watching the FTC's rulemaking with the Federal Safeguards Rule. My understanding is they pulled some provisions from DFI's—or New York's cyber law. And so I think it is important to be looking at what is already there, but when looking at a Federal solution, it

is very important that State regulators have enforcement authority to make sure that financial institutions are complying with those requirements.

Mr. MCADAMS. Thank you.

Mr. Chairman, I see I am out of time. I yield back. Thank you.

Chairman LYNCH. Thank you.

The Chair now recognizes the gentleman from Wisconsin, Mr. Steil, for 5 minutes.

Mr. STEIL. Thank you.

I want to start by thanking Chairwoman Waters and Ranking Member McHenry for starting the Fintech Task Force. I also want to commend Chairman Lynch and Ranking Member Hill for leading us as we look for ways that fintech is changing the way we do business, invest in retirement, and conduct our financial lives.

The fintech revolution is a great opportunity for all Americans. Lenders are using sophisticated data analysis to help more families and entrepreneurs responsibly access their services. Insurers are using new technology and artificial intelligence to improve underwriting accuracy. Payment companies are facilitating transactions quickly and securely for consumers and businesses around the world.

While we need to stay vigilant and protect consumers from abuse, we should make sure that we don't fall into a typical Washington mindset that sometimes views innovation as a threat. With every major innovation, pessimists often decry the hypothetical consumer harm and job losses that haven't historically always materialized. I often think back to the risk of ATMs to the jobs of bank tellers as an example of that hypothetical risk that did not materialize. I think we need to continue to look at ways to create environments that are conducive to continued fintech innovation. And today's discussion, I think, has been a great start to the task force's important work ahead.

I have a couple of questions I would like to ask. I would like to start with you, Mr. Woolard. One of the concerns I often hear about fintech is that some new entrants may seek to operate in a manner similar to a depository institution but without the associated regulatory burden, in effect, regulatory arbitrage. Can you elaborate on the FCA's experience in deterring regulatory arbitrage?

Mr. WOOLARD. Thank you very much, Mr. Steil. From an FCA point of view, the U.K. set-up is very much around regulated activities. Technically, we don't regulate banks. We actually regulate the act of deposit-taking and so on and so forth. And so, frankly, we haven't seen this kind of issue really in the U.K; we have the ability to look through the technology, to look through, if you like, the service that is being offered to what is the underlying activity, and we regulate it on the same basis as if it was a fintech or if it was a more traditional player in the market.

Mr. STEIL. Thank you. I want to jump and ask Ms. Knickerbocker and Mr. Watkins to comment here. Countries around the world, including the U.K., are experimenting with different fintech regulatory structures, and we should learn from the experience of foreign financial regulators as we seek to modernize our rules so the U.S. can remain competitive in fintech. Can you comment on lessons you have learned from policy experiments in other coun-

tries and how those are impacting policy proposals in the United States? I'll start with you, Ms. Knickerbocker.

Ms. KNICKERBOCKER. We spend a lot of time speaking to regulators around the world so that we can learn about their experiences and how we can apply that best in the United States. We also have regular conversations with the Financial Conduct Authority. What we have learned from those conversations, as well as conversations from around the globe, is that it is very important to be able to have a new way of engaging with regulated entities, and that is why we proposed our pilot program back in April, so that there is an opportunity with these complex innovations, to get involved early, to see what are the potential risks and what are the potential possible issues that could come up, and it benefits greatly the institutions that are working on these novel entities ideas as well as those that have regulatory uncertainty, and that has helped us quite a bit.

Mr. STEIL. Thank you.

Mr. Watkins?

Mr. WATKINS. Thank you for highlighting this important issue of tracking what is happening internationally. We have also learned from the FCA and other regulators in developing some of our policies, including our sandbox policies. We are also in communication and monitoring developments around open banking, which is another important issue touching on this area.

Mr. STEIL. Thank you. With my limited time left, I want to come back to you, Mr. Woolard. Can you comment about consumer impacts in fintech in the U.K.? Have customers gained access to the services in instances where they were previously out of reach?

Mr. WOOLARD. Thank you. Yes, we have certainly seen a number of areas where access might be opened up. So, for example, for low-income families around basic contents insurance on their goods that they have in their house, we have seen experiments there, between fintechs and established players. We have also seen some degree of innovation in the basic savings market, where you get very small sums being saved by low-income families. But banks serving that market, again, because technology makes it cheaper to do so.

Mr. STEIL. Thank you very much.

And seeing I am out of time, I yield back. Thank you.

Chairman LYNCH. The gentleman yields back.

The Chair now recognizes the gentleman from Florida, Mr. Lawson, for 5 minutes.

Mr. LAWSON. Thank you, Mr. Chairman, and witnesses, welcome to the task force. And this question can be for anyone. Can you discuss the issues around privacy and consumer protection in regard to regulating fintechs especially when it comes down to peer-to-peer lending, rural advertising, insurance technology, and digital banking?

Mr. CLARK. I can speak to that on behalf of State regulators, that we license money transmitters and consumer lenders, and in those areas—and peer-to-peer lenders would be covered—they are subject to the Gramm-Leach-Bliley Act. So, as far as information security, we examine for that. When we license a company, we make sure that they have an information security program in place before they even start operating, and as I mentioned earlier, CSBS is

training up our examiners around the country, so that they are very skilled in cybersecurity.

Mr. LAWSON. Did anyone else want to respond? Mr. Watkins, did you want to respond to that?

Mr. WATKINS. Absolutely. So, of the examples that you mentioned, peer-to-peer and digital banking most closely intersect with our jurisdiction. The privacy provisions under Gramm-Leach-Bliley 501b are delegated to the FTC, but we do supervise pursuant to our UDAP (Unfair or Deceptive Acts or Practices) authority for privacy-related issues on some nonbank entities. With respect to peer-to-peer lending, a key element that we have looked at is transparency and deception, making sure that consumers understand the terms that are being disclosed.

Mr. LAWSON. Okay. What about robo advertising?

Ms. SZCZEPANIK. I can speak to that. So, to the extent someone is giving investment advice, they would likely be subject to our regulations that are around investment advisers. And we have rules in place that apply to registrants, like investment advisers and broker dealers, that require them to have policies and procedures and controls around customer data, customer identity and information, and so we have an examination staff who goes out and examines our registrants for compliance with those rules, and we have brought enforcement actions where those rules have been violated in appropriate circumstances.

Mr. LAWSON. All right. Can you tell me, how, in your opinion, will fintechs change people's careers? Can anyone respond to that? And that might be the wrong question to ask, but I think it will.

Ms. SZCZEPANIK. I think it certainly changed the careers of the folks at this table because we focus on that, and we make a huge effort to do outreach, both to the industry and to the public, to encourage them to come to talk to us about what they are seeing and to help us be better regulators in that regard. And on the flip side, I think there is a great deal of opportunity out there for folks who want to innovate in the financial industry, and we are here to help them do it in a compliant way.

Mr. LAWSON. Okay. Mr. Woolard, you mentioned in your testimony—and I don't have much time—about how this will affect a lot of minorities and how to get that information to them. What is on the horizon with that?

Mr. WOOLARD. I think one of the questions here is, how does fintech reach into different communities? And, in particular, I think with many of these questions we have been debating, the technology itself, you could always regard as neutral. It is how it is used and it is how it is deployed by the people running the companies that makes it used for either good or for ill. And I think, in particular, one of the things we are seeing is the ability of some of these financial technology solutions to actually provide very cheap, low-cost, efficient alternatives to maybe some of the higher-cost lending that we have seen in the market. We certainly have about three players in the sandbox at the moment who are looking at those kind of alternative provisions. That is often about serving communities that are perhaps harder to reach or excluded from more mainstream financial services products.

Mr. LAWSON. Okay.

Thank you, Mr. Chairman. I yield back.

Chairman LYNCH. The gentleman yields back.

The Chair now recognizes the gentlelady from California, Ms. Porter, for 5 minutes.

Ms. PORTER. Thank you, sir.

Mr. Watkins, 5 months after you were appointed to your position, the Consumer Financial Protection Bureau proposed policies that give the Office of Innovation authority to exempt certain fintech companies from having to comply with laws like the Equal Credit Opportunity Act, and they did this for the purpose of promoting innovation. Specifically, the Bureau revised its no-action letter and its product sandbox policies to give fintech policies a safe harbor from liability so that the qualifying companies would be immune from enforcement actions by Federal or State authorities.

As the head of the Office of Innovation, once these policies go into effect, you are going to wield enormous influence over which anti-discrimination laws companies have to follow. Would you be able to wield that influence in an unbiassed capacity?

Mr. WATKINS. Thank you for that question, Congresswoman. Yes, I would.

Ms. PORTER. You mentioned in your testimony that you consulted with a broad spectrum of stakeholders in designing the proposals, the no-action proposals and the sandbox proposals that you have spoken about, including meeting with civil rights groups. Can you name a few of those groups, please?

Mr. WATKINS. I most recently met with Chicanos Por La Causa. The meetings that we have had—the prior meetings that I am thinking of, regarding civil rights groups, were part of larger groups, and I would be glad to get you that information but I would need to provide that to you at a later time.

Ms. PORTER. Did you meet with the Human Rights Campaign?

Mr. WATKINS. I don't recall if they were at a meeting or not.

Ms. PORTER. Did you meet with Equality California?

Mr. WATKINS. I don't recall if they were at a meeting or not.

Ms. PORTER. Did you meet with any LGBTQ rights groups?

Mr. WATKINS. I would have to look at the meeting participants to be able to answer that question.

Ms. PORTER. Discrimination in lending against LGBTQ borrowers is rampant. One recent study found, in surveying 25 years of mortgage data, that gay couples were 73 percent more likely to be denied a mortgage than heterosexual couples with the same financial worthiness. Mr. Watkins, I studied your—as is my habit, I studied your CV before I came here today. I would like to ask you about this gap in your CV. This is from LinkedIn. What were you doing from 2012 to 2015?

Mr. WATKINS. Thank you for providing me the opportunity to respond to that allegation.

Ms. PORTER. Oh, it is my pleasure.

Mr. WATKINS. There is no gap on the resume that I submitted to the Bureau. The resume that I submitted to the Bureau—

Ms. PORTER. No, I am not—excuse me. I am not—reclaiming my time, I am not accusing you of any resume impropriety. I am asking—let me just ask you directly, is it true that, during that period, you worked for the Alliance Defending Freedom?

Mr. WATKINS. That period that you mentioned was a period when I had left my law firm, when I was disillusioned with the practice of law—

Ms. PORTER. Mr. Watkins, I am not—respectfully reclaiming my time. I am not interested in your life history. I just really want to ask about—have you ever worked for the Alliance Defending Freedom?

Mr. WATKINS. Yes, and I did during that time.

Ms. PORTER. Were you senior legal counsel there?

Mr. WATKINS. I was, and I would be happy to explain what those duties were.

Ms. PORTER. Did you know that the Alliance Defending Freedom has been designated a hate group by the Southern Poverty Law Center?

Mr. WATKINS. I don't recall if that occurred when I was there or afterwards, but I do know that that has happened as I sit here now.

Ms. PORTER. In describing the Alliance Defending Freedom, the Southern Poverty Law Center said that the group, "supports the recriminalization of homosexuality and defends state-sanctioned sterilization of trans people." Mr. Sears, the founder, co-founder, and CEO of the Alliance Defending Freedom, has described the homosexual agenda as evil and has written that homosexual behavior and pedophilia are often intrinsically linked. Do you agree with those views?

Mr. WATKINS. Congresswoman, I do not even believe that the organization holds those views. They would have to speak for themselves. What you have described is clearly unconstitutional, and the practices that you mentioned are clearly unconstitutional, and have no place in the United States.

Ms. PORTER. More than one-third of my staff in D.C., and in Orange County, are gay. Do you have a message to them to assure them how you will champion antidiscrimination at the Consumer Financial Protection Bureau after your advocacy with a gay hate group?

Mr. WATKINS. I did not engage in advocacy; I did not engage in litigation (my job was, as part of a component of that group that advises law students.); I did not represent parties in court; I did not advocate for policies in the legislature. The information that I believe you are basing these questions on is mistaken in many respects. I am committed to upholding the Bureau's policies, both for my internal management of my office, as well as upholding the constitutional and statutory framework as interpreted by the Bureau in my external-facing activities.

Ms. PORTER. Thank you, Mr. Watkins.

My time has expired.

Chairman LYNCH. The Chair now recognizes the gentleman from Minnesota, Mr. Emmer, for 5 minutes.

Mr. EMMER. Thank you.

First, I would like to thank all of you for the work you are doing to encourage financial technology innovation. This Administration has shown at each and every agency that they are open to new innovations that may not necessarily fit within our current regulatory structure. In addition to the SEC, the OCC, and the CFPB,

we have—it is the alphabet soup of letters in this town—seen some great work by Chairman Giancarlo, Daniel Gorfine at the CFTC, and Jelena McWilliams at the FDIC, FINRA, and the amount of agencies on the list could, maybe unfortunately, go on and on. This committee will consider reauthorization, as I understand it, of the Export-Import Bank tomorrow. Many of these financial innovations could be directly applied to the work done there, improving international finance, reducing transaction costs, and minimizing delays.

Despite the recent negative remarks of some lawmakers, the use and support of cryptocurrencies by the U.S. Government could go a long way to improve our efficiency, as well as provide for anti-money-laundering oversight. I want to ask Valerie—I understand you go by Val—a nonsecurity commodity token that runs on an unowned, decentralized network can have its origin in a securities offering. My question is about how that happens. Do securities transform or transmute into commodities? Or does a commodity simply result from a securities offering with the initial investment contract and the commodity token being two separate independent things?

Ms. SZCZEPANIK. That is a great question, and thank you for that. The way that the staff looks at it at the SEC—and I think this is reflected in the remarks of Director Hinman last year—is that it is critical to look at the manner of offer and sale of a digital asset or any instrument. And at one point in time, an instrument can be offered and sold as a security whereas, at a different point in time, it can be offered and sold as something that isn't a security.

One good example is the Division of Corporation Finance issued a no-action letter to a company that wanted to issue a token for jet services. When that company came to us with the no-action letter, it had a completely functional system, it wasn't raising money, it had an operational blockchain. And in that case, the Division issued a no-action letter. Had that company come to us 5 years previously when hypothetically the company didn't have operational technology, didn't have jets, didn't have the ability to provide goods and services in exchange for a token, and instead was issuing that token in order to raise the funds needed to build that ecosystem, had come to issue it at that point in time, the same as—the sale of the same digital token was likely a sale of a security.

Mr. EMMER. As a follow-up, is the token not a security the moment it is handed to investors? Or do you look at the delivered token separately from the investment contract and analyze whether it is a security? And I know you are talking about point in time, and maybe I am just confusing the mechanics and I am asking you the same question again. Clarify for me, if you will?

Ms. SZCZEPANIK. I believe what you may be referring to is the use of a purchase agreement to sell a security or token that perhaps is delivered in the future. Is that correct?

Mr. EMMER. Right. Yes. Sorry.

Ms. SZCZEPANIK. So, typically, we would look at that purchase agreement as a security, depending on the facts and circumstances, and that is not normally that hard of a question. A different ques-

tion is whether the underlying token is a security, and that depends on the facts and circumstances.

Mr. EMMER. Again, that is the timing, right?

Ms. SZCZEPANIK. It could be the timing, but it also—you have to look at the facts and circumstances, for example, when it is purchased and then when it is delivered, and have those changed. It is an analysis that is done really at the point of offer and sale.

Mr. EMMER. Okay. In a talk at South by Southwest earlier this year, you said that some stable coins might be securities. If a stable coin is backed by a reserve of assets, the mix of which is actively managed by the issuer to achieve value stability, does it matter that the purchaser does not have an expectation of profits, or can such a stable coin qualify as a security merely by the purchaser relying on the managerial efforts of the issuer to keep the value stable?

Ms. SZCZEPANIK. Again, I think that hypothetical would need to be fleshed out a little bit in terms of the facts and circumstances of the particular case. Just because something is called a stable coin does not mean that there aren't the efforts of others involved. And so we would look behind the facts and circumstances and also the economic realities to see whether is there a central party, for example, acting to keep a price stabilization. Is the formula that they are using likely to provide a profit over time? Those would be all important factors that we would look at, among others.

Mr. EMMER. I appreciate it. I see my time has expired. Mr. Chairman, thank you for the flexibility. Obviously, this is something that we would love to follow up with more because we need more clarity in this area. Thank you very much.

Ms. SZCZEPANIK. Thank you.

Chairman LYNCH. Absolutely. Thank you.

The Chair now recognizes the gentlewoman from Iowa, Mrs. Axne, for 5 minutes.

Mrs. AXNE. Thank you, Mr. Chairman. And congratulations on the task force, and thank you to our witnesses for being here today.

I am happy to be here at the first of the Fintech Task Force hearings, and I am excited to help shape the role of the Fintech Task Force and how it plays in our financial system and, of course, with our economy.

Obviously, fintech is a very broad term. My husband and I do own a digital design firm, so we dabble somewhat with some of our customers related to this. I get it to some degree, but it is a broad term and, of course, this is new to a lot of folks. And so it is a burgeoning opportunity for this country that, obviously, those of us here feel very compelled to make sure is going to work appropriately.

My question is more specifically for Mr. Clark and Mr. Watkins. Can you explain just a little bit more about how you differentiate between entirely new services and something that is, in fact, really an old service, but delivered in a new way?

And then if the team, the group here itself or either one of you would like to explain further how you would deal with those differentiators differently as regulators?

Mr. CLARK. Sure. It starts with communication. And I can tell you, speaking for the State of Washington and bank regulators

generally, we want to learn from companies, learn what is going on with new services.

CSBS wanted to learn more from fintechs in general and understand the industry. So, they created a Fintech Industry Advisory Panel, where they had representatives from 33 companies come in and talk about their products.

Our staff have come up-to-speed on much of the technology that is out there so we can keep pace as a new company comes in and describes what they are doing. But the key factor that we try and do is decide, given their business model, are they engaged in money transmission, which we regulate, are they engaged in consumer lending, which we regulate, or mortgage or loan servicing? And we work with them to come to that conclusion.

CSBS is working on a licensing wizard to help companies and their counsel learn some of that on their own. So, we are making progress and we are using regtech to do that. And once we determine whether we have jurisdiction, we either help them through licensure—and by the way, we communicate this with other State regulators. So it is not just Washington making those decisions. We share the information through NMLS. And if we don't have jurisdiction, we do not regulate them, we let them go forward.

Mrs. AXNE. And then my question that comes up as a result of that is, will we have access to—could we see what the licensing wizard is about? It might be helpful.

Mr. CLARK. Sure. We would be happy to give you some information. It is in development right now, but it is very promising.

Mrs. AXNE. Okay, thank you.

Mr. Watkins, did you have anything to add to that?

Mr. WATKINS. Only that you have touched on one of the toughest questions in this whole area, which is, how do you define innovation? I think we try to approach that because of our jurisdiction and our focus on the consumer.

So one way to look at this question is, what is in it for the consumer? What is new? What is the benefit here? Is it ease of experience? Is it better pricing? Is it some sort of functionality that makes this product more attractive for the consumer? That is what we try to understand as an initial matter.

Mrs. AXNE. Thank you.

Do any other witnesses have any other comments?

Mr. WOOLARD. I could offer one, if you like. We have dealt in the U.K. with around 1,500 individual firms through our projects. I would say the vast, vast majority of those, probably all but two, are offering at the end of the day traditional financial services products ultimately when you strip it all away, when you analyze back to sort of really what is the core of what is being done here.

However, the thing we are looking for is, are they being delivered in a particularly innovative way? Is there a particular consumer benefit from the way in which the firm is operating? And, also, does that drive a particular efficiency or a change in the market that could be beneficial for consumers? But I think the underlying core product, it is quite hard to distinguish between things that are somehow completely new and ultimately financial services products that probably have been around for hundreds of years but delivered in very different forms.

Mrs. AXNE. Thank you very much.

Chairman LYNCH. The gentlelady yields back.

What I would like to do is, I would like to give the ranking member of the task force an opportunity. He has recently returned from the Floor and was unable to join us for the last portion of this, but I certainly welcome him. The Chair recognizes Mr. Hill for 5 minutes.

Mr. HILL. I thank my friend from Massachusetts.

Ms. Knickerbocker, I had asked Mr. Watkins earlier about valid-as-made. I wonder if you have any comments on that?

Ms. KNICKERBOCKER. With respect to valid-as-made, the OCC joined a Solicitor General opinion where we believe that the decision in *Madden* was incorrect. And I believe that Mr. Otting has told the committee that we are looking into all of the options around that.

Mr. HILL. If you have a legislative proposal, I would hope you would invite its consideration by the committee.

And in a similar vein, the issue of the concept of a true lender, which is a similar issue in our fintech world on extending credit, where the bank remains the true lender under a fintech depository institution partnership, is that something you believe that the regulatory agencies, the prudential regulators could clarify that definition of true lender?

Ms. KNICKERBOCKER. Just like with valid-when-made, we will be looking at that issue. I would point out that the true lender litigation right now is with State banks and not national banks, but it is something that we would be willing to look at.

Mr. HILL. Good. Thank you for that.

Mr. Woolard, I noticed that, in some of the work I read about your testimony in preparation for the hearing, that loan volume declined by 11 percent in the United Kingdom after the introduction of a national consumer rate cap, and that that was, I think, the expectation. But the actual decline was it dropped 56 percent, 5 times what the regulatory authorities estimated within 18 months, and that the number of borrowers dropped by 53 percent versus an initial estimate of only 21 percent.

Given the regulators' forecast, thinking about the optimal outcome as it relates to payday borrowing, can you speculate how those impacts are all from that interest rate cap and what lessons has the FCA taken from that?

Mr. WOOLARD. Thank you very much.

That obviously applies, as you said, to the payday lending market, where we are under duty to institute a cap.

What we have seen there is some significant benefits to consumers in terms of costs that have been avoided, so several hundred millions of pounds of charges a year. We have also seen when we surveyed, actually, consumers have adjusted their behaviors. So, looking either to effectively cope with a lack of access to potential credit in some cases or to look for alternatives to that market that actually might be cheaper. So, on the whole, I think we have seen in the area of our evaluation work actually positive benefits that have come from that cap.

It is worth saying across the high-cost credit market, where we have a much wider program that includes a whole range of dif-

ferent products, there is only one other space where we have taken a parallel kind of intervention, which is around the rent-to-own lending market, which is about how people buy household goods at very high rates of interest.

In the remaining areas, we have tended not to use caps. We only use those, really, as a last resort. And it is really about trying to find interventions that constrain the harms that we see in that high-cost end of the market versus the wider access that there might be for the public to credit.

Mr. HILL. Thank you for that response.

Ms. Szczepanik, let me ask you a question in regard to the SEC and this issue of data privacy. I mentioned earlier about Application APIs for use on protecting consumers' data. Do you believe that is a best practice for people who are trying to do data aggregation in the wealth management or full financial picture mode?

Ms. SZCZEPANIK. Sure. As we mentioned, or as I mentioned earlier, we do have rules around keeping policies, procedures, and systems in place to protect the data privacy of customers, for example, investment adviser customers or broker-dealer customers and others. And we typically don't prescribe the means that they do. We want the firms to look at what makes sense for their business, what is state of the art, what is the best practice. That could evolve over time.

So we expect that they are constantly reevaluating the systems they have in place to make sure that they are sufficient, adequate, and state of the art to meet their obligations under those rules to protect data privacy.

Mr. HILL. Thank you. I appreciate that.

Mr. Chairman. I yield back.

Chairman LYNCH. The gentleman yields back.

I now recognize myself for 5 minutes.

Ms. Knickerbocker, I expressed at the beginning in my opening statement the dichotomy sort of, the different cultures in the tech world and the traditional banking world. In traditional banking, we in many cases apply a fiduciary standard, which is very exacting, and the obligations to the customer, to the client are quite clear, a bright line.

On the other hand, in the tech world, we have adhesion contracts. We have, you know, you click, I agree to 73 pages of obligations, and you are basically giving away your privacy rights. The privacy agreement is an agreement to give away your privacy; it is not to keep it.

How do we reconcile those two worlds, and who wins? Is the fintech merger more like the banking world in that respect, or is it more like the tech world, where you have big companies like Facebook and Google vacuuming up personal data, this behavioral surplus, as Shoshana Zuboff has described in her book. They are sucking up all this data.

And I am told that I think it is Facebook, on their regular users, has like 5,000 data points on every one of their regular users. And now we are going to allow them to link up with a banking firm, and they will have all that information to exploit.

How do we reconcile that?

Ms. KNICKERBOCKER. One of the things that the OCC did with respect to a special purpose charter was look at some of those particular issues, where you have companies that are engaged in traditional banking activities but are not subject to bank-like regulation and examination.

And so one of the things that we looked at with respect to the charter was the fact that if they were engaged in these activities—and, again, it is a choice in the United States. But if they wanted to become a national bank, which we had a lot of folks that were interested in that, they should be subject to regulation. We believe that regulation is strong. It can promote innovation that is done responsibly. And that is one of the reasons why we propose the special purpose charter.

Chairman LYNCH. Okay. I just want to make sure we get that part of this right. There is a lot of risk in sort of that dimension of things.

Ms. KNICKERBOCKER. I would—I'm sorry.

Chairman LYNCH. No, go ahead.

Ms. KNICKERBOCKER. I would agree with that. I think that data protection, as the task force is looking at these issues, should be a key issue that you should look at, particularly with how fast things are moving now.

Chairman LYNCH. Right. Google and Facebook, they don't like friction. And so all of these requirements—Mr. Woolard, you have the General Data Protection Regulation (GDPR) in the U.K. What kind of friction do you see in terms of the fintech firms operating in that space under that regulation?

Mr. WOOLARD. Thank you. I think there is a range of friction, if you want to use that label, that comes not just from GDPR. It also comes from the Payment Services Directive, where the underlying assumption is that data belongs essentially to the consumer. And you think about how that is being protected and how that is appropriately deployed and used.

The reality is we can see models emerging where large amounts of data are being used by firms, artificial intelligence is being deployed on an increasing basis by firms in the financial services markets and, indeed, elsewhere.

Again, as I also said earlier, I think a lot of these technologies have, if you like, a neutral purpose. It is how they are used and deployed is whether we think they would raise a regulatory concern or whether, actually, they could provide a benefit to consumers.

So I think we would all be in favor of better, more tailored services, which that data could provide. But if that information is then used to price gouge people, if it is used to work out whether they are less tolerant to price increases, for example, then it obviously becomes a concern.

Chairman LYNCH. All right. Thank you.

I do appreciate all of the testimony. The task force appreciates that. I think you have suffered enough. Some regulators were more prepared to come today than others. We regret that the Federal Reserve and the FDIC were not able to participate. One was a last-minute scheduling problem that I understand.

But, without objection, the statements of the two agencies provided to the task force for this hearing are hereby entered into the record: the statement for the record of the staff of the Board of Governors for the Federal Reserve System submitted to the task force on June 25, 2019; and the statement of the Federal Deposit Insurance Corporation, similarly dated.

We also have letters and testimony from the Credit Union National Association, the National Association of Federally-Insured Credit Unions, and the Financial Data and Technology Association, which are all hereby entered into the record.

Without objection, it is so ordered.

I would like to thank our witnesses for their testimony today.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And this hearing is now adjourned.

[Whereupon, at 4:45 p.m., the hearing was adjourned.]

A P P E N D I X

June 25, 2019

TESTIMONY OF

CHARLES CLARK

DIRECTOR

WASHINGTON DEPARTMENT OF FINANCIAL INSTITUTIONS

On behalf of the

CONFERENCE OF STATE BANK SUPERVISORS

On

OVERSEEING THE FINTECH REVOLUTION: DOMESTIC AND INTERNATIONAL PERSPECTIVES ON FINTECH REGULATION

Before the

TASK FORCE ON FINANCIAL TECHNOLOGY

HOUSE COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

Tuesday, June 25, 2019

2:00 P.M.

Room 2129 Rayburn House Office Building

I. Introduction

Thank you, Chairman Lynch, Ranking Member Hill and distinguished members of the Task Force. My name is Charles Clark. I am the Director of the Washington State Department of Financial Institutions. My department is responsible for the regulation, supervision and examination of Washington's more than 17,000 state-licensed non-depository entities and more than 90 state-chartered depository institutions, including 38 state-chartered banks. Our department also provides education and outreach to protect consumers from financial fraud.

Today, I represent the Conference of State Bank Supervisors (CSBS), the nationwide organization of banking regulators from all 50 states, the District of Columbia, Guam, Puerto Rico, American Samoa and the U.S. Virgin Islands. CSBS was established in 1902 to support and improve the dual banking system by bringing state banking regulators together and promoting state-federal regulatory coordination.

State regulators charter and supervise 79% of all U.S. banks and are the primary regulators of a diverse range of nonbank financial services providers, including mortgage lenders, money transmitters and consumer lenders. CSBS, on behalf of state regulators, also operates the Nationwide Multistate Licensing System (NMLS), a licensing regulatory platform for state-licensed nonbank financial services providers in the money services, mortgage, consumer finance and debt industries.

I serve as the chair of the CSBS Non-depository Supervisory Committee, which provides a forum for state financial supervisors to discuss interstate non-depository supervisory matters and is driving several initiatives aimed at ensuring that state supervision of nonbank companies – including many who call themselves "fintechs" – is effective and efficient.

Thank you for holding this hearing on fintech regulation. Nonbank financial services are a large part of the state regulatory ecosystem. As the primary regulator of many nonbank companies who consider themselves fintechs, the state system has expertise, data and real-time supervisory insight into how these companies are interacting with consumers and functioning in the marketplace.

My testimony today will discuss state regulators' perspectives on the fintech industry and how state regulators have, over the years, approached innovation in financial services. I will detail the following:

- How state regulators, as the primary regulators of a diverse range of nonbank entities, including mortgage lenders, money transmitters and consumer lenders, approach fintech and innovation in financial services.
- How fintechs fit within the context of existing state financial regulatory and consumer protection laws.
- How state regulators are actively involved in ongoing efforts to leverage technology and data as regulatory tools to transform state supervision.

- The impacts of technology on our regulated industries, with a focus on state-licensed money services businesses.
- How state regulators are committed to advancing Vision 2020, a set of initiatives designed to harmonize the multistate licensing and supervision for nonbanks, including fintechs.

II. State Regulators and Fintech – Understanding the Opportunities and Risks

State regulators are locally accountable, sitting in close proximity to consumers and the communities they are charged with protecting. This perspective makes us uniquely situated to recognize and act upon consumer financial protection issues. When consumers have an issue, they contact us first. Our goal is to help prevent consumer harm before it happens.

Financial regulation and supervision serve as a mechanism for protecting consumers, ensuring financial system stability and assisting law enforcement. The legal framework for state regulation of nonbank financial services industries is activities-based. We have found that the business models of most fintechs can be placed in the context of existing state laws. For example, mortgage and other lending laws apply whether the borrower interaction is online or in person. Likewise, we apply money transmission laws to any company that moves money from Point A to Point B, whether the customer is in person at an agent location or using an app on their phone.

For most fintech products and services, the value added is not product-based, but rather time, ease of use and cost. We can move money across the country or across the globe with a tap of our thumb. It is faster for consumers to fill out an application online, and it is faster for underwriting to be performed using algorithms created to implement credit policies. When the costs historically associated with financial services are reduced by technology, products can be cheaper and delivery can be faster, but the potential for consumer harm remains – and can be exacerbated by the speed of transactions. As regulators, our job is to see through the shiny stuff to understand the underlying activity and corresponding risks and benefits.

State regulators recognize that the current intersection between financial services and technology has accelerated change in the industry and poses challenges for the state system. We began to address growth in, and the multistate nature of, the fintech industry in December 2013, when the CSBS Board of Directors approved the formation of the CSBS Emerging Payments Task Force. This group of regulators was charged with:

- Serving as the state system's focal point for fintech developments and issues.
- Evaluating changes in the financial services sector – particularly in payments – and the impact of these developments on state supervision and state law.
- Developing and driving projects and initiatives related to fintech.

At its formation, the task force recognized that external stakeholder engagement was integral to its work. One of the task force's first initiatives was a public hearing on payments that

included testimony from a variety of industry and outside experts. Additionally, during the task force's first two years, we issued Model Consumer Guidance on Virtual Currencies and Model Regulatory Framework for Virtual Currency, both with public input. In December 2016, the task force changed its name to the Emerging Payments and Innovation Task Force to reflect the task force's work beyond the payments industry.

To continue the Task Force's focus on external engagement, in the spring of 2018, CSBS hosted its first ever Fintech Forum. A day-long conference involving regulators, consumer groups and industry focused on discussing fintech business models and their opportunities and risks.

In May 2017, CSBS announced Vision 2020, a commitment to drive towards an integrated, 50-state system of licensing and supervision for nonbanks through a set of initiatives designed to harmonize state regulation, while enhancing the efficiency and effectiveness of the state system and maintaining strong consumer protections.

III. Vision 2020 – A Mindset and Roadmap for a Stronger, More Efficient Regulatory System

In recent years, state regulators have broadened the scope of how we work together, especially as we recognize that technology has progressed so quickly, allowing fintech companies to scale rapidly. In 2017, state regulators formally launched Vision 2020, our plan to bring more harmonization into the multistate experience as a means for regulatory efficiency and better supervision. Key to Vision 2020 is preserving the states' role in protecting the financial system and consumers, while addressing inefficiencies in current licensing and regulatory processes.

Vision 2020 is also a regulatory mindset – a clear vision of how the states are working together to advance nonbank licensing and supervision. It is the states' commitment to work toward a more consistent, coherent and networked system of state regulation, leveraging technology and data, while reinforcing strong consumer protection regulation and enforcement.

State regulators currently are acting on several Vision 2020 initiatives. Those include:

- **Developing robust technology tools** that enable regulators to leverage human resources more efficiently.
- **Prioritizing IT and cybersecurity training** through a sweeping $1.5 million CSBS cybersecurity training program that will train 1,000 examiners in both the bank and nonbank space at no costs to the states by the end of 2019.
- **Improving third-party supervision** by integrating state regulators into appropriate federal laws such as the Bank Service Company Act.
- **Seeking industry input from fintech firms** to identify licensing and regulatory challenges and develop actionable responses, while maintaining strong consumer protections and local accountability.

- **Formulating a vision and roadmap for implementing regtech solutions** that will integrate technology, industry self-assessment and "real-time" supervision to dramatically increase oversight effectiveness while reducing regulatory burden.

I would like to highlight for this Task Force's attention on element of Vision 2020 – our focus on enabling banks, particularly smaller banks, to leverage innovation responsibly and effectively. To that end, CSBS has been working with Congress for a few years on legislation that would improve bank third-party supervision by integrating the states into the Bank Service Company Act. Members of the Task Force may recall that this Committee unanimously approved the Bank Service Company Coordination Act in the 115th Congress. We urge the Committee to advance H.R. 241, the current version.

IV. Modelling a Commitment to Diversity and Inclusion

In Washington State, Governor Inslee has set a focus on diversity and inclusion, issuing an Executive Order reaffirming our state's commitment to tolerance, diversity and inclusion. My agency values diversity and inclusion among our staff in carrying out our mission and in all the industries we regulate. I and my entire agency have a responsibility to promote and advocate for a strong and visible culture of diversity and inclusion by creating a welcoming and respectful environment where every person is valued and honored. Additionally, in order to be an advocate for diversity and inclusion with our regulated industries, we have a responsibility to model within our agency that commitment. We have a variety of initiatives aimed at achieving this goal, including:

- Two years ago, we formed a DFI Diversity Advisory Team (DAT) which includes staff from every level of the organization. This group disseminates information promoting diversity and educates staff on diversity topics.
- We have updated our agency policies in areas including harassment prevention, training and developments and hiring to ensure that we are following the most up to date practices in encouraging a respectful and inviting workplace.
- We implemented an intensive training effort on understanding implicit and explicit bias.

Looking at the industries we regulate, we have a variety of structured and informal means for promoting industries and companies that are diverse and welcoming of all individuals.

- My agency participates in our statewide Business Resource Groups – groups of agency staff and external stakeholders with a common interest or characteristic that, among other benefits, bring knowledge and perspectives in areas such as recruitment and retention.
- We participate in a variety of initiatives aimed at improving industry diversity including Women in Banking and Minorities in Banking conference.
- And, we maintain an ongoing dialogue with individual institutions about increasing board and management diversity.

Collectively, we hope that each of these initiatives helps send a message – that DFI is tolerant of all people and supports diversity and inclusivity and that we expect the same of our regulated industries.

V. Reimagining Nonbank Licensing and Supervision

This section discusses state regulators' ongoing efforts to leverage technology and data as regulatory tools to transform state supervision.

A. Regtech for a Stronger and More Networked System of Regulation

For state regulators, regtech is the use of technology to improve the efficiency and effectiveness of regulation. State regulators across multiple states that use the same data points and definitions reduce regulatory burden and improve supervision by harmonizing state-specific requirements, participating in multistate exams and analyzing risk across state lines.

1. NMLS as a Licensing and Registration System

A critical juncture for state supervision and regtech occurred more than a decade ago, when state regulators recognized growing problems in the mortgage industry as bad actors were taking advantage of a lack of regulatory coordination. Working together, states created uniform mortgage loan originator license application forms in 2006. A year later we began building a common licensing platform to better manage and monitor licensed mortgage lenders, mortgage brokers and individual mortgage loan originators (MLOs) doing business in one or multiple states. That became the Nationwide Mortgage Licensing System, launched in January 2008.

Congress recognized its value and incorporated what is now called the Nationwide Multistate Licensing System (NMLS) in the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (the "SAFE Act"). Today, NMLS is a comprehensive system of licensing and registration of all state-licensed mortgage companies and MLOs and for MLOs working in all depository institutions, including banks and credit unions.

In 2012, state regulators began using NMLS to license a broader range of nonbank financial services providers, including money services businesses, consumer finance lenders and debt collectors. Last year, NMLS licensed 24,000 companies. While the majority are mortgage related, about one-third of the companies are from the money services, consumer lending and debt industries.

In addition to serving as a regulatory platform, NMLS has a public facing portal (nmlsconsumeraccess.org) where consumers review individual and company licensing status and publicly available regulatory actions.

2. Improving Regulation through Data and Analytics

NMLS also supports state efforts to improve regulatory data and information about nonbank financial services providers. States are using this data to understand and evaluate trends and risks in their regulated industries and to better risk-scope licensing and supervisory priorities and activities.

In 2011, we launched the Mortgage Call Report, which is a quarterly report of originations covering more companies than is covered by the Home Mortgage Disclosure Act. In 2017, we launched a Money Services Business (MSB) Call Report, which is the first and only nationwide report of MSB information especially important in understanding the money transmission industry. These reports create a standardized reporting requirement across all participating states that allow for nationwide trend analysis and risk identification. We are also in the early stages of developing a Consumer Finance Call Report.

The data has given state regulators a deeper perspective into the mortgage industry landscape and has helped us identify applications that might require more scrutiny. As a result, state regulators have become more efficient and more focused on risk. NMLS is useful for federal regulators as well. The Consumer Financial Protection Bureau (CFPB) relies on NMLS to register more than 420,000 mortgage loan originators and almost 10,000 banks and credit unions, for example.

3. SES – The Next Generation of State Licensing Technology

Building on the success of NMLS as a licensing system, the states are developing a new technology platform called the State Examination System (SES) that will integrate with NMLS. This secure, end-to-end technology platform will be the first nationwide system to bring both regulators and companies into the same technology space for examinations. Doing so will foster greater transparency throughout supervisory processes. The system will improve collaboration while reducing redundancy and burden.

B. Improving Multistate Supervision through Coordination

As the nonbank financial services industry has grown, state regulators have evolved our approach to examining nonbank financial services companies, particularly those that operate in multiple states. In 2008, state mortgage regulators formed the Multistate Mortgage Committee (MMC) to formalize and improve the supervision of mortgage companies that operate in multiple states. This improved the effectiveness and efficiency of state supervision and facilitated the states' collaboration with federal regulators, including the CFPB. And, it was through the MMC that state regulators helped lead the 2012 National Mortgage Settlement, which provided billions of dollars in relief and restitution to consumers related to the servicing of mortgage loans.

Based on this experience and using the MMC model, in 2014 we formed the Multistate MSB Examination Task Force to coordinate supervision of multistate money services businesses.

VI. Additional Regulatory Tools

A. A Focus on Cybersecurity

Cybersecurity risk cuts across the full range of state licensed, chartered and regulated institutions. Through industry outreach and coordination, as well as the development of supervisory tools, state regulators – collectively and individually – have been focused on this priority for several years.

As mentioned above, CSBS is in the midst of a massive, far reaching cybersecurity training program for state examiners. In addition, several years ago, CSBS launched an initiative to educate bank executives on cybersecurity through face-to-face dialogue between state regulators and industry, issuance of a resource guide and other information and tools for industry. Through the states' role on the Federal Financial Institutions Examination Council (FFIEC), we participated in the development and deployment of the FFIEC Cybersecurity Assessment Tool for banks.

B. Enforcement

Our interaction with industry covers a continuum – including enforcement as a key tool regulators use to carry out our responsibilities. Just as our regulatory regimes are activities-based, our approach to enforcement is activities-based. Since January 2017, 69 individual enforcement actions at money transmitters have been uploaded to NMLS.

Most recently, state regulators devoted significant resources to a multi-state examination addressing the massive data breach Equifax experienced in 2017. Last year, eight states took action against Equifax, requiring the company to take various actions to improve risk management and information security.

VII. Strengthening the State System through Industry Engagement

As a part of Vision 2020, CSBS formed a Fintech Industry Advisory Panel (FIAP). Through an open and transparent process, CSBS sought FIAP members willing to commit to focused work on identifying the challenges of a 50-state system and to offer concrete solutions. The panel ultimately had 33 fintech firms representing both the payments and lending industries. After more than 100 hours of meetings, the FIAP made a series of recommendations to the CSBS board in December 2018. CSBS announced its plans to move forward with 14 of the recommendations in February 2019. A summary of the FIAP recommendations and next steps is included as an appendix to my testimony. Key among these efforts:

- **Develop a Model State Payments Law.** We currently are developing a model state law for money transmitters with uniform, risk-based requirements. Though each state generally uses the same framework for money transmission laws, each statute has its own unique definitions and requirements for money transfers. States also might interpret and implement laws differently, even when the statutory language is the same. A model law will enable money transmitters to build national scale more easily, improve state supervision and ensure consumer protections.

- **Rationalize Multistate Exams.** Through the **One Company, One Exam** pilot, a nationally operating money transmitter – instead of undergoing multiple state examinations – will be examined only once in 2019 in a manner that meets the supervisory needs of many states. The process incorporates the requirements of multiple states into one exam and will identify areas where increased communication and advanced information sharing will improve state efficiency and significantly reduce burden for firms. The program will help states improve their processes – a crucial element of states protecting consumers while promoting national business models – and will inform the continued development and future deployment of SES. Building on the one company/one exam pilot in 2019, we are working on a three-year national examination schedule for larger MSBs in which states will conduct joint examinations staggered with offsite examinations and reliance by non-examining states on the results of the joint reviews. Once established, this national schedule will be real and substantive coordination that will improve oversight and significantly reduce regulatory burden.

- **Streamline Multistate MSB Licensing.** My agency, the Washington Department of Financial Institutions, devised and has been leading this effort, which the CSBS board last month agreed to make a CSBS initiative. To date, 23 states have signed on to the MSB licensing initiative, which is intended to curb duplications in the licensing process. If one of these signatory states reviews key elements of state licensing for a money transmitter, other participating states agree to accept the findings. By utilizing NMLS, applicants now have a process for submitting most license application materials only once instead of submitting them separately to each participating state. For licensing requirements that are common among the states, the applicant will also have a single point of contact with the state selected to review the common licensing requirements.

- **Develop Tools for Navigating the State System.** The FIAP urged the states to provide more tools to help companies better understand licensing and regulatory requirements as well as more easily navigate the licensing process. Two tools are now in development: an online repository of state licensing guidance, which will be available on csbs.org, and a license wizard, which will enable applicants to quickly identify licensing options based on their business model. Related to these tools, we are committed to continuing to build stakeholder understanding of the growing nonbank industry. CSBS is in the process of publishing a series that looks at how the nonbank financial services industry is currently supervised and ways to enhance supervisory approaches. In early June, we

published our first chapter, "Introduction to the Nonbank Industry[1]," which provides an overview of market segments within the nonbank industry.

VIII. States Have a Firsthand View of How Technology is Transforming State Regulated Nonbank Industries

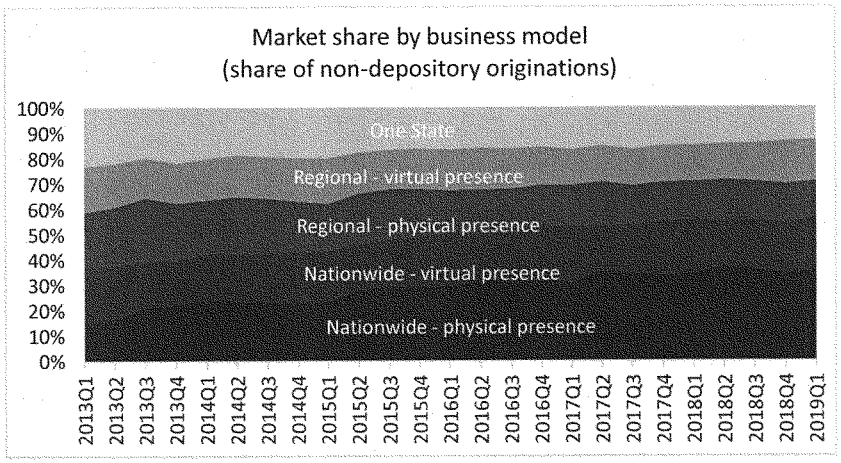
The convergence of innovation and financial services has affected every industry within the state regulatory portfolio. Data from NMLS has helped state regulators understand these changes and spot trends. This section spotlights trends in two major areas of state nonbank regulation: the nonbank mortgage industry and state-licensed money services business.

A. Technology, including Regtech, has Driven Expansion and Growth in the Mortgage Industry

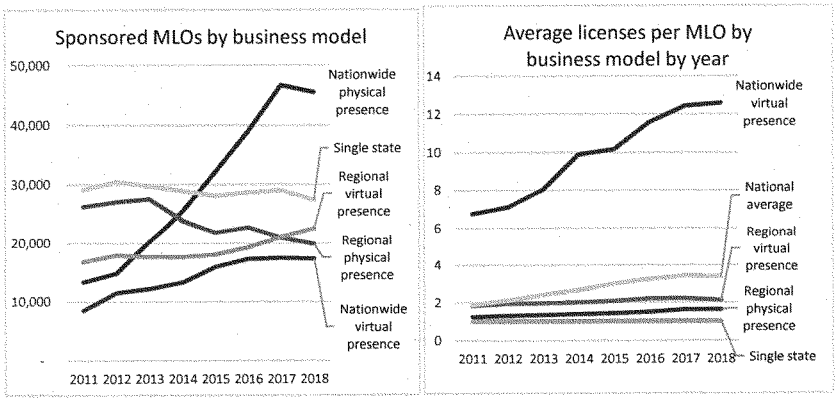
Using NMLS data, we analyze mortgage company business models based on two main criteria: regional vs. nationwide and physical vs. virtual presence. We consider a company to be nationwide if it has a license in at least half of the states. A company has a virtual presence if it has fewer branches than state licenses and therefore does not maintain a physical presence in every state where it does business.

One change brought about by technology is the increase in the number of firms operating nationwide, as technology helps companies reach customers and NMLS has helped bring uniformity to state licensing. The number of nationwide companies with a physical presence has approximately doubled over the past six years, as has the number of nationwide companies with a virtual presence. Similarly, the nationwide companies have won market share from regional companies in mortgage originations.

[1] See *"CSBS Paper Series Focuses on Reengineering Nonbank Supervision,"* https://www.csbs.org/csbs-paper-series-focuses-reengineering-nonbank-supervision.



The number of mortgage loan originators employed by nationwide companies with a physical presence has nearly doubled over the past four years, while the number of MLOs employed by other business models has remained steadier. On the other hand, the average number of licenses per MLO has nearly doubled for nationwide companies with a virtual presence, while remaining steady for other types of mortgage companies.



These two trends show that companies using technology to reach customers, including fintechs, are acquiring more licenses for their MLOs, thereby growing their virtual presence (via phone or technology). Meanwhile, nationwide branch-heavy companies are growing their actual MLO population.

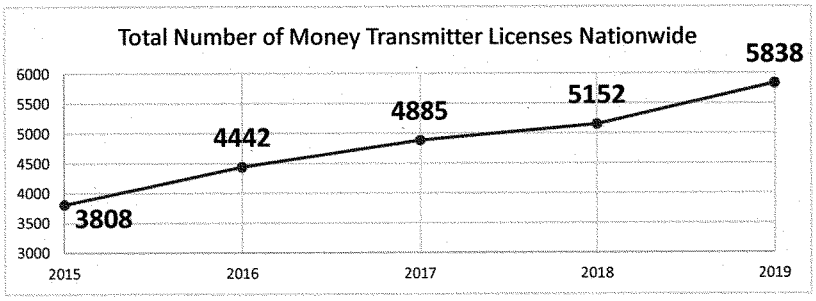
B. The Evolution of the State-Regulated Payments Industry

Many early fintechs came from the money transmitter space, leveraging technology to create new business models, new delivery channels, automated decisions and partnerships with traditional banks. Moving money across continents and across oceans inherently requires technological innovation. While MSBs are at the cutting edge of technology today, their history of deploying advanced technology goes far back in time to the telegraph and international undersea cables for transmission of money.

1. Technology-Driven Changes to the MSB Industry

The states have held exclusive jurisdiction over MSBs for over 100 years. State supervision of MSBs began at the turn of the 20th century when states began protecting their residents' funds as immigrant populations sent money by steamship back to Europe and Asia. The earliest state money transmitter laws date back to 1907.[2]

In recent years, technology has driven changes and growth in the MSB industry, as seen in the chart below.



This growth represents an increase of 53% over five years. While the number of licenses has increased, NMLS data show that the number of companies at any given time has been relatively stable. Therefore, the increase in the number of licenses means that existing companies are expanding their geographic footprints by obtaining licenses in more states. This is reflected in both the growth of multistate money transmitters (18% growth) and the average licenses per company (55% growth), as shown in the following chart.

[2] *See* Immigrant Banks, Reports of the Immigration Commission, p. 318, (Dec. 5, 1910). *Available at* https://archive.org/stream/cu31924021182500#page/n333/mode/2up/search/immigrant+bank.

	2019	2018	2017	2016	2015
Multistate Money Transmitters	272	250	245	243	231
Average Licenses per Company	11.5	12.9	10.5	9.7	7.4

This licensing data signal two trends. First, mergers and acquisitions (M&A) have played a significant role in the industry. As startups grow, they are being bought by larger, established companies. Second, companies frequently undergo orderly wind-downs, change business plans to activities that do not require a license, or roll up multiple subsidiaries into one license. Perhaps most regrettably, several companies have been de-risked, a trend that has slowed but still affects the industry.

2. The State System of MSB Supervision

Altogether, from May 31, 2014, to May 31, 2018, NMLS data show a total of 173 companies exited the licensed money transmission space. A similar number of companies became licensed over the same time period. Because state laws are designed to protect consumers while companies try and sometimes fail, these numbers reflect a state system that works. Policymakers do not hear about money transmitter failures because state safety and soundness requirements protect both the taxpayer and the consumer from risk of loss.

Case in point: during an examination that involved coordination with the Brazilian Central Bank and two private Brazilian banks, it was determined that a licensed money transmitter was using falsified records, evidencing an even broader pattern of illegal activity. As a result, the states coordinated on enforcement, stopping the company from accepting and transmitting money across 37-states.[3] All consumers who lost money were made whole, even without deposit insurance.

Since 2015, the average state has seen a 68% increase in licensees, from 69 licenses to 116 licenses. The state-by-state licensing increase reflects the geographic expansion of a handful of very large companies that now dominate the market. As of Q1 2019, a total of 71 companies are licensed in 40 or more states, compared to just 37 companies in 2015—an increase of 92%. These 71 companies are responsible for 80% of the $1.39 trillion transacted in the United States in 2018. The six very largest companies were alone responsible for 66% of all funds transferred or stored, moving more than $900 billion in 2018.

While states have exclusive jurisdiction within their borders, the money transmission business is national – and often global – in nature. As the industry has evolved, so too have state

[3] *See, e.g.* Braz Transfers Cease and Desist Order, *available at* http://www.mass.gov/ocabr/business/banking-services/banking-legal-resources/enforcement-actions/2013-dob-enforcement-actions/braz04012013.html.

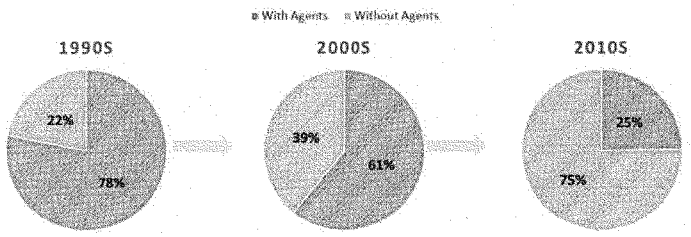
regulators to create a more networked "state system" utilizing collective resources on a national basis.

The MSB Call Report, launched in 2017, collects quarterly activity and financial data from MSB companies, including nationwide totals for money transmission, stored value, payment instruments and virtual currency transactions. In addition to information about the size of the MSB market, the MSB Call Report provides a picture of industry composition.

Year end 2018 MSB Call Report data show that six companies moved 66% of the funds transferred or stored by all MSBs. Three of these companies are licensed in every state, one is licensed in 49 states and the last is a crypto company licensed in 42 states. These companies are not alone – 69 companies are licensed in 42 or more states.

Despite the market dominance of these few companies, the majority of MSB companies are licensed in only one state. These small licensees take on many different roles in state economies, including payment services in local stores, startups and remittance providers for local ex-pat populations. Given this high level of competition, it is no surprise that 173 companies ceased licensed operations over a five-year span.

A dynamic shift has occurred in the money transmission industry over the past decade. Of the 64 currently operating licensees that were formed in the 1990s, 78% utilize an agent-based business model, where people handle the transaction from physical locations. Since 2010, conversely, 75% of the 133 newly formed companies utilize a business model without agents but facilitated by online technology.



New businesses continue to move away from agent models

Using this data, state regulators developed a means of identifying MSBs that could be identified as "fintech" companies. If a company has two or fewer agents and is operating in four or more states, the best logical conclusion is the company is utilizing the internet for its operations. These companies collectively accounted for more than 55% of all transaction volume in 2018.

Sector	Sector Total	Fintech Total	Fintech Market Share
Money Transmission	$831.5 billion	$448,131,604,535	54%
Payment Instruments	$175.2 billion	$ 3,500,525,533	1.9%
Stored Value	$294.9 billion	$254,356,621,671	86%
Check Cashing	$14.1 billion	0	0%
Currency Exchange	$5.4 billion	$469,040,022	9%
Virtual Currency	$69.5 billion	$64,649,566,505	93%
Total	**$1.39 trillion**	**$771,107,358,266**	**55.5%**

Importantly, this fintech market share has grown since 2017, with money transmission leading the way from a volume perspective and virtual currency leading the pack in overall growth.

IX. State Perspectives on Federal Fintech Initiatives

A. State Regulators and the U.S. Department of Treasury's Innovation Report

The U.S. Department of Treasury recognized the importance of harmonizing state financial regulation and the progress state regulators have made in its July 2018 report: *Nonbank Financials, Fintech, and Innovation.*

In the report, Treasury voiced support for state regulators' efforts to build a more unified licensing regime and supervisory process across the states and floats that such efforts might include adoption of a passporting regime for licensure. State regulators are already engaged in implementing several of the recommendations, which include drafting a model law, using NMLS to foster a more cooperative approach among state regulators in the supervision of nonbank financial services companies and streamlining examinations.

Importantly, the report recognized Vision 2020 as a response to the state regulatory challenges raised by the nonbank financial services industry and encouraged states to continue our focused effort to implement a variety of Vision 2020 initiatives.

> *"It is important that state regulators strive to achieve greater harmonization, including considering drafting of model laws that could be uniformly adopted for financial services companies currently challenged by varying licensing requirements of each state. Treasury encourages efforts to streamline and*

coordinate examinations and to encourage, where possible, regulators to conduct joint examinations of individual firms. Treasury supports Vision 2020, an effort by the Conference of State Bank Supervisors that includes establishing a Fintech Industry Advisory Panel to help improve state regulation, harmonizing multi-state supervisory processes, and redesigning the successful Nationwide Multistate Licensing System[4]."

B. State Regulators' Concerns with the OCC's Proposed "Fintech" Charter

There is one aspect of the Treasury report we particularly disagree with, however. It supports the Office of the Comptroller of the Currency's (OCC) decision to accept applications for special purpose national bank charters from nonbank fintech companies that do not and would not engage in receiving deposits or be insured by the Federal Deposit Insurance Corporation. We strongly oppose the OCC's decision and have filed litigation against it.

Our reasons are clear. First, The OCC does not have the statutory authority to issue federal banking charters to nonbanks. Only Congress can make such a decision, especially as the charter creates public policy implications that must be debated in Congress. Second, a federal fintech charter would disrupt the market by picking winners and creating losers, drawing a handful of large, established entities and give them a competitive advantage over new market entrants that have historically injected innovation into our financial system. Third, a federal fintech charter would preempt important state consumer protections. Fourth, such a charter would harm taxpayers by exposing them to the risk of fintech failures.

X. Conclusion

As the primary supervisors of nonbank financial providers, state regulators appreciate the commitment of both this Task Force and the Committee to ensuring effective supervision of financial technology companies.

As I have outlined, state regulators are engaged and proactive in ensuring that state supervision of fintechs is effective and efficient in this rapidly growing space. State regulators oversee a diverse ecosystem of bank and nonbank entities, including mortgage lenders, money transmitters and consumer lenders. State regulators are committed to using technology and data to make the states more effective as regulators by advancing toward a regulatory system that spots trends early, prioritizes resources to address risks and supports the emergence of pro-consumer innovation.

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[4] *A Financial System That Creates Economic Opportunities Nonbank Financials, Fintech, and Innovation*, U.S. Treasury Department, https://home.treasury.gov/sites/default/files/2018-08/A-Financial-System-that-Creates-Economic-Opportunities---Nonbank-Financials-Fintech-and-Innovation.pdf.

APPENDIX

CSBS VISION2020

Fintech Industry Advisory Panel Recommendations and Next Steps		
Payments & Lending Industry Recommendations	**Regulator Response**	**Next Steps**
Use CSBS regtech for licensing and exams		
Expand use of NMLS across all license types	Support	**Drive** 50-state adoption of NMLS for nonbank financial services
Expand use of all available NMLS functionality	Support	**Drive** 50-state adoption of NMLS for nonbank financial services
Develop menu of state licensing requirements for multi-state consistency, including: - renewal timelines and requirements - supplement paper-based notice and disclosure requirements with online delivery/posting options - electronic surety bonds - electronic fingerprint cards - electronic payments to state agencies	Support	**Build** into ongoing work to develop the new NMLS
Build the State Examination System	Support	**Launch** SES with pilot states during 2019
Increase multi-state exam coordination	Support	**Establish** quantitative targets for multi-state exams **Launch** SES with pilot states during 2019 One-company, one-exam pilot launched January 2019
Harmonize owner and management vetting		
Explore standardized approaches to control and control persons including: - change of control application process - approaches to international persons - treatment of passive investors	Support	**Establish** a regulator-industry working group on control **Develop** a 50-state model MSB law
Increase transparency		
Create central repository of licensing and fintech-related state guidances	Support	**Build** an online database of state licensing and fintech guidance
Conduct 50-state surveys of consumer finance, MSB exemptions	Support	**Publish** an online source for current licensing requirements and exemptions; encourage a common standard
Establish vehicle/forum for conversations — prelicensure and/or outside the formal exam cycle — on technology, companies and products	Support	**Coordinate** information sessions for regulators and industry to discuss fintech developments

Payments-Specific Industry Recommendations	Regulator Response	Next Steps
Create uniform definitions and practices		
Standardize definitions and interpretations of the activities that require MSB licensure	Support	**Develop** a 50-state model MSB law
Standardize exemptions and procedure(s) for exemptions to MSB licensure	Support	**Develop** a 50-state model MSB law
Form regulator working group to evaluate differences in state MSB prudential requirements and explore harmonization opportunities through regulatory and state legislative action	Support	**Develop** a 50-state model MSB law
Lending-Specific Industry Recommendations	**Regulator Response**	**Next Steps**
Create uniform definitions and practices		
Consistent reporting timelines and requirements for state-licensed consumer finance lenders	Support	**Create** a standardized consumer finance call report
Continue industry/regulator conversations		
Facilitate regulator education regarding lead generation as an acquisition channel for online lenders	Support	**Include** lead generation in professional development training
For future consideration		
Develop menu of state licensing requirements for modernization and/or multi-state consistency, including: - eliminating physical office requirements - supplement paper-based notice and disclosure requirements with online delivery/posting options	Consider for future action or implementation	
Examine interpretive differences among states with similar consumer finance statutes	Consider for future action or implementation	
Small business lending: Create a consistent definition for commercial loan based on use of proceeds	Consider for future action or implementation	
Small business lending: Apply commercial loan definition to loans to sole proprietorships	Consider for future action or implementation	
Small business lending: Develop consistent approaches to disclosure	Consider for future action or implementation	

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TESTIMONY OF

BETH KNICKERBOCKER

CHIEF INNOVATION OFFICER

OFFICE OF THE COMPTROLLER OF THE CURRENCY

before the

TASK FORCE ON FINANCIAL TECHNOLOGY

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

June 25, 2019

Statement Required by 12 U.S.C. § 250:
The views expressed herein are those of the Office of the Comptroller of the Currency and do not necessarily represent the views of the President.

I. Introduction

Chairman Lynch, Ranking Member Hill, and members of the Task Force on Financial Technology, thank you for the opportunity to participate in today's conversation on innovation in financial services. As the Chief Innovation Officer at the Office of the Comptroller of the Currency (OCC), I am pleased to discuss our Office of Innovation and the OCC's key innovation initiatives.

Pursuant to the National Bank Act, the Home Owners' Loan Act, and other federal statutes, the OCC supervises more than 1,200 national banks, federal savings associations, and federal branches and agencies of foreign banks operating in the United States. These institutions range in size from small community banks to the largest, most globally active U.S. banks. A majority of American families have one or more relationships with a national bank or federal savings association (bank).

Innovation and evolving customer preferences have significantly changed these relationships, including the way products and services are delivered. While innovation has been a constant feature of the federal banking system, the current pace and magnitude of the change is unprecedented and serves as a powerful catalyst for economic growth and financial inclusion. When done responsibly, innovation can increase consumer choice, improve the delivery of products and services, and enable financial institutions to more effectively meet the needs of consumers, including those who are unbanked and underbanked; businesses; and communities. Innovation can also enhance a bank's ability to compete by introducing operating efficiencies and increasing effectiveness.

Over the past four years, the OCC has dedicated significant resources to supporting "responsible innovation," a term that we use in part to acknowledge the importance of balancing

innovation with prudent risk management. The OCC believes that responsible innovation enables a vibrant federal banking system that meets the evolving needs of consumers, businesses, and communities and that promotes economic opportunity and job creation, while continuing to operate safely and soundly, provide fair access to financial services, treat customers fairly, and comply with applicable law and regulations. We are focused on ensuring that banks have a regulatory framework that is receptive to responsible innovation, as well as a supervisory approach that appropriately accounts for the opportunities and risks of changing business models and new products, services, and processes. We are strengthening our core competencies and effecting a cultural change that will better position the agency to meet its responsibilities in this evolving environment.

Today, I would like to provide an overview of several OCC initiatives that demonstrate how the agency is proactively encouraging responsible innovation in the federal banking system. These initiatives include (1) the agency's responsible innovation framework and the establishment of the Office of Innovation; (2) the OCC's support of appropriate partnerships between banks and financial technology (fintech) companies;[1] (3) our voluntary Innovation Pilot Program to facilitate testing of innovative products, services, and processes that could significantly benefit consumers, businesses, and communities; and (4) opportunities for fintech companies to become full-service or special purpose national banks. These initiatives form the foundation, and demonstrate the evolution, of the OCC's regulation and oversight of innovation in the federal banking system. Through these initiatives, the OCC has become a leading voice on

[1] For ease of reference, this document refers specifically to fintech companies. However, much of the discussion applies equally to other nonbanks that provide financial products and services. In addition, references to partnerships in this document are not limited to legal partnerships and include a variety of other arrangements through which banks can work with fintech companies, such as vendor relationships and investments.

responsible innovation. Finally, I would like to highlight some principles and areas for further study for the Task Force to consider.

II. The OCC's Responsible Innovation Framework and Office of Innovation

In order to remain relevant and competitive in a dynamic financial services industry, financial institutions must understand how the industry is evolving and develop strategies to adapt responsibly. At the same time, financial regulators must be able to respond appropriately and in a timely manner to the innovation affecting the institutions and industry they regulate.

In light of these imperatives, in 2015, the OCC started an initiative to develop a comprehensive innovation framework that would improve the agency's ability to identify, understand, and respond to trends and changes in the industry and the evolving needs of consumers, businesses, and communities. As part of this initiative, the OCC assembled a cross-functional team of agency experts that met with banks of varying size and complexity, fintech companies and other innovators, consumer groups, trade associations, academics, and regulators. In March 2016, the agency published a white paper summarizing the major themes that emerged from this research.[2] The white paper defined "responsible innovation" to mean "[t]he use of new or improved financial products, services, and processes to meet the evolving needs of consumers, businesses, and communities in a manner that is consistent with sound risk management and is aligned with the bank's overall business strategy."[3] This definition framed the OCC's approach to innovation and demonstrated the agency's commitment to balancing the benefits of innovation with its risks, including cyber risk. The white paper also set forth principles to guide the OCC's development of a responsible innovation framework and invited public comment.

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[2] *Supporting Responsible Innovation in the Federal Banking System: An OCC Perspective*, https://www.occ.gov/publications/publications-by-type/other-publications-reports/pub-responsible-innovation-banking-system-occ-perspective.pdf.

[3] *Id.* at 5.

In June 2016, the OCC hosted a forum on responsible innovation, which was attended by over 400 stakeholders. The forum addressed a variety of topics, including trends, opportunities, and challenges in innovation, as well as how innovation can expand access to financial products and services. In October 2016, after considering comments received on the March white paper, feedback from the June forum, and additional research, the OCC published its responsible innovation framework, which set out strategies for the agency to support responsible innovation in the federal banking system.[4] This framework promotes an OCC culture that is open to responsible innovation and where stakeholders are encouraged to exchange information on innovation and related topics. It also supports a workforce that understands and balances both the risks and opportunities of innovation, as well as clear, consistent, and transparent policies and practices.

The OCC created the Office of Innovation to implement this framework and to serve as a clearinghouse for innovation-related issues, as well as a central point of contact for stakeholders. As the OCC's Chief Innovation Officer, I head this Office and lead a diverse team of specialists located in Washington, DC, New York, NY, and San Francisco, CA. I report directly to the OCC's Chief Operating Officer, who oversees the agency's supervisory and policy functions. Importantly, this reporting structure facilitates the Office's ability to implement the framework across all OCC business units.

The responsible innovation framework addresses five areas—outreach and technical assistance; awareness and training; coordination and facilitation; research; and interagency collaboration.

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[4] *Recommendations and Decisions for Implementing a Responsible Innovation Framework*, https://www.occ.treas.gov/topics/responsible-innovation/comments/recommendations-decisions-for-implementing-a-responsible-innovation-framework.pdf.

Outreach and technical assistance. The Office of Innovation has established a robust outreach and technical assistance program. Through our outreach efforts, we remain knowledgeable about emerging trends, consumers' evolving financial needs, and the challenges banks face in responding to a rapidly changing landscape. These efforts have allowed us to establish an open and continuing dialogue with a diverse group of interested parties, including banks of all sizes and complexities, fintech companies and other innovators, consumer groups, trade associations, and regulators. The Office leverages this knowledge and perspective to serve as an effective resource for both internal and external stakeholders.

The Office of Innovation also provides technical assistance to banks and fintech companies to promote awareness and understanding of OCC expectations. We assist banks with understanding how to consider responsible innovation when evaluating, developing, and implementing appropriate business strategies. This may include considering innovative approaches to meeting their regulatory obligations, including those related to the Bank Secrecy Act and anti-money laundering requirements,[5] or opportunities to work collaboratively with other banks to leverage combined resources and expertise to responsibly innovate.[6] The Office is also focused on engaging with community banks regarding the risk of not assessing, or of adapting too slowly to, innovation, technological advancement, and evolving customer preferences.

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[5] OCC, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation (FDIC), Financial Crimes Enforcement Network, and National Credit Union Administration, *Joint Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing* (Dec. 3, 2018), http://el.occ/news-issuances/news-releases/2018/nr-occ-2018-130a.pdf.

[6] *An Opportunity for Community Banks: Working Together Collaboratively* (Jan. 13, 2015), https://www.occ.gov/publications/publications-by-type/other-publications-reports/pub-other-community-banks-working-collaborately.PDF; OCC, Board of Governors of the Federal Reserve System, FDIC, Financial Crimes Enforcement Network, and National Credit Union Administration, *Interagency Statement on Sharing Bank Secrecy Act Resources* (Oct. 3, 2018), https://www.occ.treas.gov/news-issuances/news-releases/2018/nr-ia-2018-107a.pdf.

We also help banks understand relevant laws, regulations, and guidance, such as the agency's third-party risk management guidance.[7] In addition, we provide information to fintech companies—including those seeking to partner with or become banks—about the OCC's expectations and how to operate effectively in a regulated environment. In the future, the OCC intends to provide more resources on emerging trends to external stakeholders and to develop additional material that will assist both banks and fintech companies interested in partnering with banks.

The Office of Innovation engages in outreach and provides technical assistance through a variety of channels. For example, over the past two years, we have hosted eight "office hours" events in five different cities, which facilitated individualized interaction between OCC staff and approximately 125 stakeholders. We have held two widely-attended "listening sessions" that focused on issues, trends, and best practices related to bank-fintech company partnerships and third-party risk management. We have held approximately 250 additional meetings and calls with stakeholders, and we have presented at over 100 conferences and other events. These events include the OCC's minority depository institution and mutual savings association advisory committees, as well as outreach organized through OCC district and field offices. Importantly, these events provide the OCC with opportunities to engage directly with community banks, which is a particular focus for the Office of Innovation.

In addition, the OCC has consistently invited public comment at critical junctures in the development of its responsible innovation initiatives, which has increased transparency and allowed the agency to benefit from a broad range of expertise.

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[7] OCC Bulletin 2013-29, "Third-Party Relationships: Risk Management Guidance" (Oct. 30, 2013), https://www.occ.gov/news-issuances/bulletins/2013/bulletin-2013-29.html; OCC Bulletin 2017-21, "Third-Party Relationships: Frequently Asked Questions to Supplement OCC Bulletin 2013-29" (June 7, 2017), https://www.occ.gov/news-issuances/bulletins/2017/bulletin-2017-21.html.

Awareness and training. The Office of Innovation works to advance awareness and expertise among OCC staff regarding innovation and emerging trends in order to foster a culture that is receptive to responsible innovation, develop staff competencies across the agency, and leverage experience and expertise in order to effectively supervise the federal banking system.

The Office of Innovation has employed a variety of tools to accomplish these goals. We have developed educational resources that explain the fundamentals of emerging products and services, and we have increased awareness among OCC policy, supervision, and other staff on related issues. Agency staff can undertake rotational assignments in the Office of Innovation, which provide an opportunity for cross-training and allow the Office to leverage existing OCC expertise. In addition, we have assembled extensive online content on emerging trends and industry innovations, published white papers, hosted webinars, and collaborated with other OCC business units to deliver in-house training, including on payments and distributed ledger technology.

Coordination and facilitation. The Office of Innovation helps coordinate across OCC business units to ensure that the appropriate internal stakeholders are represented when the agency evaluates issues related to responsible innovation. By bringing a range of perspectives together, this facilitation enhances the agency's ability to proactively understand and react to emerging trends. For example, the Office convenes representatives from various OCC business units to develop a coordinated OCC strategy on particular topics and forms working groups to consider particular issues.

In addition, the Office of Innovation is assisting with the agency's effort to develop a streamlined and transparent process to coordinate the agency's responses to innovation inquiries. This process will facilitate responsible innovation in the federal banking system by reducing

uncertainty, inconsistency, and opacity. The agency's assessment of bank-fintech company partnerships, its proposed Innovation Pilot Program, and its evaluation of chartering options—all of which are discussed in greater detail below—have required and will continue to require this type of coordination.

Research. The Office of Innovation conducts research to assess the national and international financial services landscape and identify trends in financial innovation. We analyze how innovation affects individual banks and the federal and global banking systems. This research helps to inform OCC policy and supervisory decisions, and it helps the agency identify and address potential regulatory and supervisory gaps, so that we remain current and responsive to the evolution of the industry.

Interagency collaboration. The Office of Innovation works to ensure that the OCC has open channels of communication to share information and collaborate with other domestic and international regulators. The OCC, often through the Office of Innovation, routinely shares information and communicates with other U.S. agencies on emerging trends and ways to improve our innovation initiatives. This exchange of ideas promotes common understanding and consistency, which is particularly important where agencies have overlapping jurisdictions and harmonization is appropriate.

The OCC also participates in various regulatory forums, such as the Financial Stability Board's Financial Innovation Network, and serves as co-chair of the Task Force on Financial Technology established by the Basel Committee on Banking Supervision (BCBS). Further, the OCC collaborates on cybersecurity issues domestically and internationally through the Federal Financial Institutions Examination Council, the Financial and Banking Information Infrastructure Committee, and the BCBS. We benefit a great deal from learning about the experiences of

regulators around the globe and the different approaches they have taken to address innovation in their jurisdictions.

The Office of Innovation also provides assistance to agencies interested in establishing innovation offices. When asked, we share our experiences in developing our Office and stress the importance of aligning an innovation office with the mission of the agency, having support from agency leadership, and focusing on the long-term development of agency competencies.

III. Partnerships

Partnerships between banks and fintech companies can support responsible innovation in the federal banking system by providing banks with an alternative to building or buying innovative products, services, or processes. Through these partnerships, banks of all sizes and complexities can improve the efficiency and effectiveness of their operations; contribute to financial inclusion by increasing access to savings, credit, financial planning, and payment products and services; and deliver a broader range of innovative products and services. For example, a bank can partner with a fintech company that has the technical capability to offer products and services that the bank could not otherwise reasonably offer on its own. These relationships are particularly important for community banks, which may not have the requisite resources in-house.

The OCC supports bank-fintech company partnerships that are safe and sound and that are designed to meet the evolving needs of consumers, businesses, and communities. The OCC continues to emphasize appropriate third-party risk management, given its importance to the success of bank-fintech company partnerships. For example, in June 2017, the OCC issued frequently asked questions to supplement its existing third-party risk management guidance, in

which it specifically addressed relationships between banks and fintech companies.[8] In addition, the Office of Innovation's outreach and technical assistance program has addressed best practices to help inform bank-fintech company partnerships.

Partnerships between banks and fintech companies play an important role in the development of responsible innovation in the federal banking system. Recognizing and supporting these partnerships is one way that the agency facilitates the evolution of this system.

IV. Innovation Pilot Program

Building on its existing innovation initiatives, in April of this year, the OCC proposed to establish a voluntary Innovation Pilot Program (Program) to support the testing of innovative products, services, and processes that could significantly benefit consumers, businesses, and communities, including those that promote financial inclusion.[9] The Program would complement the OCC's vision of adding value through constructive, proactive supervision and serving as a valuable resource to industry stakeholders. The Program would be open to banks, their subsidiaries, and federal branches and agencies, including those partnering with third parties to offer innovative products, services, or processes. It would also be open to banks working together, such as in a consortium or utility.

As noted above, innovation has been a longstanding hallmark of the federal banking system, and banks frequently pilot new products and services without regulatory involvement. These pilots are an important means of testing and validating the effectiveness of innovative approaches. In certain situations, however, uncertainty regarding the application of existing

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[8] OCC Bulletin 2017-21, "Third-Party Relationships: Frequently Asked Questions to Supplement OCC Bulletin 2013-29" (June 7, 2017), https://www.occ.gov/news-issuances/bulletins/2017/bulletin-2017-21.html, supplementing OCC Bulletin 2013-29, "Third-Party Relationships: Risk Management Guidance" (Oct. 30, 2013), https://www.occ.gov/news-issuances/bulletins/2013/bulletin-2013-29.html.

[9] *OCC Innovation Pilot Program*, https://www.occ.gov/topics/responsible-innovation/occ-innovation-pilot-program.pdf.

rules or supervisory expectations may be a barrier to the development and implementation of a new product, service, or process, and early regulatory involvement may help address this uncertainty. In addition, the Program would allow the OCC to further its understanding of innovative products, services, or processes and assist the agency in identifying supervisory approaches that might unintentionally or unnecessarily inhibit responsible innovation. For these reasons, the OCC developed this voluntary Program as an additional tool for banks that choose to participate.

The Program would offer timely engagement between the OCC and banks of all sizes and complexities regarding safety and soundness expectations, risk management principles, and compliance requirements. It would facilitate the development of appropriate risk management controls that can be scaled up as necessary. Regulatory tools that the OCC may use during a pilot to communicate with a bank would include interpretive letters, supervisory feedback, and technical assistance from OCC subject matter experts—but would not include statutory or regulatory waivers. The OCC may also address the legal permissibility of a product or service that a bank proposes to test as part of the Program. Furthermore, the OCC would expect banks to include specific controls and safeguards to address risks to consumers and would not permit proposals that have potentially predatory, unfair, or deceptive features into the Program.

When the OCC announced the Program, it invited public comment. The OCC specifically requested feedback on the value of the Program in light of existing agency processes, as well as the types of products, services, and processes that would most benefit from the Program. The comment period closed on June 14, and the agency received 18 comments. We are currently reviewing these comments, considering any refinements to the Program, and

determining our next steps. Although the Program is not yet operational, we have received some very positive feedback about this initiative.

V. Chartering

The OCC recognizes that fintech companies can play an important role in responsible innovation in the federal banking system by becoming OCC-chartered institutions. Many fintech companies (such as marketplace lenders, personal finance companies, payment processors, asset managers, and custody service providers) offer products and services that have historically been offered by banks. Since the early stages of the OCC's work to support responsible innovation, these companies have consistently asked the agency about options for becoming national banks.

For a fintech company that engages in the business of banking and meets the rigorous standards to become a national bank, there are several paths available to apply for a national bank charter. First, a fintech company may apply for a full-service national bank charter if it seeks to engage in the full array of national bank activities, including accepting deposits. To date, two fintech companies have applied to the OCC to operate as full-service national banks.

Alternatively, a fintech company may apply for a special purpose national bank charter. Generally, a special purpose national bank engages in a limited range of banking or fiduciary activities, targets a limited customer base, or has a narrowly targeted business plan. Examples of special purpose national banks currently supervised by the OCC include trust banks, banker's banks, and credit card banks.

In July 2018, the OCC announced that it would consider charter applications from fintech companies seeking to become special purpose national banks that would engage in one or more of the core banking activities of paying checks or lending money but that would not take deposits

or be insured by the FDIC.[10] The OCC's decision to consider these applications was the product of considerable research and extensive outreach with stakeholders over a two-year period, including the publication and solicitation of public comments on a December 2016 white paper[11] and a March 2017 draft licensing supplement.[12]

The OCC has stressed that a fintech company that receives this type of special purpose national bank charter would be supervised like a similarly-situated national bank, including with respect to capital and liquidity requirements. It would also initially be subject to heightened supervision, similar to other *de novo* banks. In addition, it would be expected to fulfill a financial inclusion commitment similar to the Community Reinvestment Act's expectations for national banks that take insured deposits. This expectation will help the OCC ensure that these newly chartered banks provide fair access to financial services and treat customers fairly. The nature of the financial inclusion commitment would depend on a bank's business model.

The OCC has not received any formal applications for this type of special purpose national bank charter. I note that the OCC is involved in ongoing litigation on this issue.

Regardless of the particular path that a fintech company chooses to pursue a national bank charter, all national banks face rigorous examinations and are subject to high standards for capital, liquidity, consumer protection, and financial inclusion. The OCC also will take appropriate action, including enforcement action, in response to any violation of applicable laws and regulations. This consistent application of laws and regulations ensures that consumers, businesses, and communities are treated fairly regardless of the type of OCC-chartered entity and

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[10] News Release 2018-74, "OCC Begins Accepting National Bank Charter Applications From Financial Technology Companies" (July 31, 2018), https://www.occ.treas.gov/news-issuances/news-releases/2018/nr-occ-2018-74.html.
[11] *Exploring Special Purpose National Bank Charters for Fintech Companies*, https://occ.gov/topics/responsible-innovation/comments/pub-special-purpose-nat-bank-charters-fintech.pdf.
[12] *Comptroller's Licensing Manual Draft Supplement: Evaluating Charter Applications From Financial Technology Companies*, https://occ.gov/publications/publications-by-type/licensing-manuals/file-pub-lm-fintech-licensing-manual-supplement.pdf.

that all national banks operate in a safe and sound manner. More broadly, by providing a path for fintech companies to become national banks, the OCC is promoting consumer choice, economic growth, modernization, and competition—all of which strengthen the dual banking system and support the nation's economy.

A national bank charter is only one option among many for fintech companies. Other options may include state banking charters, appropriate business licenses, and partnerships with other federal and state financial institutions. These options allow fintech companies to choose the best business model and regulatory structure for their business and strategic goals, which will help them meet the needs of their customers.

VI. Principles and Areas for Further Study

As the Task Force begins its work, I would like to take this opportunity to highlight some principles and areas for further study that it can consider. With respect to principles that we have found important, laws should be technology-neutral, so that products, services, and processes can evolve regardless of changes in the technology that enables them. In addition, facilitating appropriate levels of consumer protection, including by ensuring transparency and informed consent, is critical. Principle-based, rather than prescriptive, requirements are important to enable effective management of evolving risks and to reduce the potential that requirements quickly become outdated.

It is also important to evaluate existing laws to determine which statutes should be modernized to better reflect the current financial services industry and how customers prefer to interact with financial product and service providers. Modernization should balance the risks to

privacy and security with the benefits of change. Finally, the Task Force should consider mechanisms to encourage regulators to develop programs that support responsible innovation.

VII. Conclusion

Thank you again for the opportunity to discuss the OCC's responsible innovation initiatives. The Office of Innovation will continue to help the federal banking system remain vibrant and meet the evolving needs of consumers, businesses, and communities. I commend the Committee on Financial Services for creating this Task Force, as well as the Task Force on Artificial Intelligence, and I look forward to working with you in the future.

Testimony on "Overseeing the Fintech Revolution: Domestic and International Perspectives on Fintech Regulation"

Before the United States House of Representatives Committee on Financial Services Task Force on Financial Technology

Valerie A. Szczepanik, Senior Advisor for Digital Assets and Innovation and Associate Director, Division of Corporation Finance, U.S. Securities and Exchange Commission

June 25, 2019

Chairman Lynch, Ranking Member Hill, and Members of the Task Force, thank you for inviting me to testify before you today about the work of the U.S. Securities and Exchange Commission's (SEC) Strategic Hub for Innovation and Financial Technology (FinHub).[1] I am the SEC's Senior Advisor for Digital Assets and Innovation and an Associate Director in the SEC's Division of Corporation Finance, and I head the FinHub, which is staffed by representatives from across the SEC's divisions and offices who have expertise and involvement in FinTech-related issues. I am honored to appear before you and pleased that the Task Force is holding this hearing to study technological innovation in our financial markets and the efforts of the SEC and its staff to foster beneficial changes while protecting investors and the strength of the U.S. markets. I am also pleased to see in attendance those who represent similar roles as my own from among the SEC's regulatory partners as we continue to closely collaborate in these efforts.[2]

We are at a remarkable inflection point—a convergence of transformative technologies such as cloud computing, predictive analytics, artificial intelligence, Internet of Things, and distributed ledger technology. We enjoy an environment in which developers can collaborate across the world on open-source projects so that knowledge, talent, and hard work is globally crowdsourced. New technologies are in effect driven by a borderless, human supercomputer and they are moving rapidly. In the securities markets, a generation of digital natives is demanding new ways to interface with markets and to own a piece of the future of financial innovation.

These innovative technologies promise the potential to enhance efficiency, cost savings, integrity, performance and transparency in our markets, among other things. They may help facilitate capital formation, streamline trading, and provide promising investment opportunities for institutional and retail investors alike. We strive for these improvements in our U.S. markets.

This convergence also can result in disintermediation of regulated entities and automation of functions historically performed by traditional gatekeepers. This may create new modes of

[1] The views expressed in this testimony are those of the author, and do not necessarily reflect those of the SEC, the Commissioners, or other members of the SEC staff.

[2] *See, e.g.*, Jay Clayton and J. Christopher Giancarlo, "Regulators are Looking at Cryptocurrency," Wall St. Journal (Jan. 24, 2018), *available at* https://www.wsj.com/articles/regulators-are-looking-at-cryptocurrency-1516836363?mod=searchresults&page=1&pos=2.

governance, allocations of risk, and theories of accountability. These transformations compel us, as regulators, to collectively and carefully think through their effects—intended and unintended—and to contribute to important discussions. Developers, entrepreneurs and advisors who take the time and effort to engage with the SEC staff, and with the staff of our fellow regulatory agencies who have their own innovation initiatives and statutory mandates, will play a critical role in shaping the future of FinTech and in assuring that the U.S. capital markets continue to adhere to the high standards that have made them so deep, liquid, fair, and attractive for decades. The possibilities for developers and entrepreneurs who want to create products and systems in a compliant way are theirs to imagine and build. We encourage them to do so.

Our job as regulators is to strike the right balance between fostering efficient new ways to raise capital and trade securities, on the one hand, and preventing potentially harmful and illicit practices against investors, on the other. If we get this balance right, we help our capital markets and investors flourish. If we do not, harm and inefficiency will follow. Investor harm and other adverse developments could cast a shadow on these new technologies and potentially curtail investment in them or arrest their development altogether. No one who believes in the promise of FinTech would want that result. Rather, we want to choose the path that promotes investor confidence in our markets as they incorporate innovations. We hope that through thoughtful engagement with innovators and practitioners, the right balance can be struck.

Just over eight months ago, on October 18, 2018, the SEC announced the launch of FinHub to serve as a resource for public engagement on the SEC's FinTech-related issues and initiatives, such as distributed ledger technology (including digital assets), automated investment advice, digital marketplace financing, and artificial intelligence and machine learning.[3] FinHub replaced and built upon the work of several internal working groups at the SEC that had focused on similar issues for a number of years. I welcome this opportunity to now describe some of FinHub's activities and future plans.

FinHub provides a portal for industry and the public to engage directly with SEC staff on innovative ideas and technological developments.

When it launched, SEC Chairman Jay Clayton called FinHub "a central point of focus for our efforts to monitor and engage on innovations in the securities markets that hold promise, but which also require a flexible, prompt regulatory response to execute our mission."[4] We have set up FinHub to do just that. As financial technologies, methods of capital formation, market structures, and investor interfaces evolve, FinHub plays an important role in the SEC's active engagement with the industry. Through FinHub's webpage, entrepreneurs, developers and their advisors routinely request meetings with the staff, and we have held dozens of such meetings to provide one-on-one engagement with industry participants. In this way, we are essentially leveraging this discourse to help us do our job better.

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[3] *See* Press Release 2018-240, *SEC Launches New Strategic Hub for Innovation and Financial Technology* (Oct. 18, 2018), *available at* https://www.sec.gov/news/press-release/2018-240.

[4] *Id.*

FinHub also organizes events through which the public can participate in FinHub's work.

FinHub has implemented a number of ways— and will continue to proactively explore new ways—to engage with the public. For example, as I mentioned, we actively invite engagement with FinHub staff through our web portal and, as a result, have conducted numerous calls and in-person meetings with entrepreneurs, developers, and their advisors. This year, we began hosting local peer-to-peer meetings to engage with FinTech communities across the country. These "P2P meet ups," as we call them, offer the opportunity to speak in person with FinHub staff at a local venue to discuss a general issue or specific question, or to give a presentation about a particular project. Already, we have traveled to cities across the United States—including San Francisco, Denver, New York and Philadelphia—to give interested stakeholders a chance to interact one-on-one with FinHub staff at a place convenient to them. We have conducted nearly two dozen separate local P2P meet ups with a broad range of participants, including innovators developing new technologies, entrepreneurs looking to bring new businesses to market, advisers and advocates interested in discussing a host of issues, universities and academics starting FinTech programs, SEC registrants or those seeking to become registered, and more. Later this week, we will host another P2P meet up in Chicago. While FinHub staff cannot give legal advice, we can provide helpful guidance and feedback. We often describe how we interpret the federal securities laws and point out potential issues for consideration with respect to a particular proposal.

On May 31, 2019, we hosted a public FinTech Forum, which was simultaneously webcast through the SEC's website.[5] This event brought together academics and industry participants to discuss a host of important issues before an audience of the public, SEC staff, and staff from a number of other government agencies.[6] Approximately 2,000 people attended in person or viewed our webcast. The Forum featured four panels moderated by SEC staff, which covered a wide range of topics concerning technology, asset classes, market structure, and application of the securities laws.[7] Each panelist brought unique expertise and perspective that helped inform the audience of the scope of issues and their import and complexity. As was evident by the breadth and depth of the topics discussed at the forum, the staff has a sophisticated understanding of the technology, continues to engage frequently with industry stakeholders, and has been thoughtful in their approach in this area. The Forum included remarks by Chairman Clayton, Commissioner Hester Peirce, and the Directors of the Divisions of Corporation Finance, Trading and Markets, Investment Management, and the Office of Compliance Inspections and Examinations, who demonstrated the significance of FinTech issues at the highest levels of the SEC.

FinHub acts as a clearinghouse of information regarding the SEC's activities and initiatives involving FinTech.

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[5] *See* Press Release 2019-35, *SEC Staff to Hold FinTech Forum to Discuss Distributed Ledger Technology and Digital Assets* (Mar. 15, 2019), *available at* https://www.sec.gov/news/press-release/2019-35.

[6] *See* Press Release 2019-59, *SEC Staff Announces Agenda for May 31 FinTech Forum* (Apr. 24, 2019), *available at* https://www.sec.gov/news/press-release/2019-59.

[7] *See id.*

On FinHub's webpage, we link to publications, statements, speeches, testimony, requests for public input, and cases relevant to each area of technological innovation we feature.[8] One area on which we have been focusing a significant amount of attention and resources relates to digital assets and initial coin offerings (ICOs)—issues which implicate many SEC divisions and offices. We recognize that distributed ledger technology holds great promise to help facilitate capital formation. In order to assist those seeking to comply with the U.S. federal securities laws, on April 3, 2019, FinHub staff published a framework to aid market participants in analyzing whether a digital asset is an investment contract, and, therefore, is a security.[9] On that same day, the Division of Corporation Finance issued a staff no-action letter to a market participant in connection with a proposed offer and sale of a digital asset.[10] Further, the SEC has solicited comment in connection with proposed rule changes by self-regulatory organizations to list new products, such as exchange traded products involving digital assets.[11] The Division of Investment Management has issued letters welcoming public input on various topics, including one identifying significant legal and investor protection issues that potential funds with cryptocurrency-related holdings present under the Investment Company Act and its rules.[12] Another Division of Investment Management letter seeks to engage with the public on digital asset custody under the Advisers Act Custody Rule.[13]

The staff recognizes that knowing in what regulatory space you stand when it comes to a new product or system requires careful analysis. For example, determining whether a new type of financial instrument, including a digital asset, is a security requires an analysis of the nature of the instrument and how it is offered and sold. That is why we encourage market participants to use the materials on FinHub's website as a resource, to consider consulting with securities counsel, and to request further guidance from staff if questions remain. Regrettably, while some market participants have engaged with us constructively, others have not. The SEC's Division of

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[8] *See* https://www.sec.gov/finhub.

[9] *See* Framework for "Investment Contract" Analysis of Digital Assets (last modified Apr. 3, 2019), *available at* https://www.sec.gov/corpfin/framework-investment-contract-analysis-digital-assets.

[10] *See* Response of the Division of Corporation Finance re: TurnKey Jet, Inc. (Apr. 3, 2019), *available at* https://www.sec.gov/divisions/corpfin/cf-noaction/2019/turnkey-jet-040219-2a1.htm.

[11] *See* SEC Release No. 34-85093; File No. SR-NYSEArca-2019-01 (Feb. 11, 2019) (notice soliciting comment on the listing of Bitwise Bitcoin ETF Trust shares), *available at* https://www.sec.gov/rules/sro/nysearca/2019/34-85093.pdf (comments posted at https://www.sec.gov/comments/sr-nysearca-2019-01/srnysearca201901.htm); and SEC Release No. 34-85119; File No. SR-CboeBZX-2019-004 (Feb. 13, 2019) (notice soliciting comment on listing of VanEck SolidX Bitcoin Trust shares), *available at* https://www.sec.gov/rules/sro/cboebzx/2019/34-85119.pdf (comments posted at https://www.sec.gov/comments/sr-cboebzx-2019-004/srcboebzx2019004.htm).

[12] *See* Staff Letter Engaging on Fund Innovation and Cryptocurrency-related Holdings (Jan. 18, 2018), *available at* https://www.sec.gov/investment/fund-innovation-cryptocurrency-related-holdings.

[13] *See* Staff Letter Engaging on Non-DVP Custodial Practices and Digital Assets (Mar. 12, 2019), *available at* https://www.sec.gov/investment/non-dvp-and-custody-digital-assets-031219-206.

Enforcement has been and will continue to recommend enforcement actions for alleged violations of the federal securities laws relating to digital assets.[14]

The SEC's Office of Investor Education and Advocacy (OIEA) regularly partners with the FinHub to identify areas of potential risk and to issue investor alerts, as appropriate. For example, OIEA launched a mock ICO to alert investors about potential fraud in the ICO market. OIEA advertised "HoweyCoin," on a website called HoweyCoins.com that imitates the common features of scams, such as guaranteed returns, "get in early" notices, celebrity endorsements, and assurances of "SEC compliance." If a visitor attempts to purchase a coin through the website, the visitor is automatically redirected to the SEC's investor education webpage, which alerts the investor to the existence of scams and contains links to pages with warnings from other of our regulatory partners. FinHub staff continues to work with OIEA to devise creative ways like this to reach investors and maximize the impact of our messaging.

FinHub acts as a platform for SEC staff to acquire and disseminate information and FinTech-related knowledge within the agency.

When evaluating the impact of rapidly-evolving and often unpredictable new technologies, it is critical to on-board knowledge and necessary tools and expertise. As the financial landscape continues to evolve, the skillset regulators need becomes increasingly multi-disciplinary. Innovations in today's markets require knowledge of finance, law, market structure, economics, computer science, cryptography and more. FinHub staff continually seeks to stay apace of new developments and to acquire and deploy expertise where it needs to go within the SEC's various Divisions and Offices.

To help with this effort, we have been exploring ways to enrich our academic collaborations and leverage all the groundbreaking work being done by scholars conducting research at the cutting edge. Our staff regularly participates in conferences and forums hosted by industry and academia. And, we are seeking to hire digital asset experts through our visiting scholars program to work alongside FinHub staff in our day-to-day work. In this way, we hope to continue the strong tradition of government and academic partnership. We are committed to understanding the technologies that impact our markets and we are taking proactive steps through FinHub to ensure that SEC staff has hands-on opportunities to work with these technologies.

FinHub serves as a liaison to other domestic and international regulators regarding emerging technologies in financial, regulatory, and supervisory systems.

In the United States, a number of different regulators may have jurisdiction over different aspects of FinTech. In the digital asset space, as in the broader financial space, for example, it is not uncommon for a particular activity to implicate the one or more of the respective jurisdictions of the SEC, the U.S. Commodity Futures Trading Commission (CFTC), the Financial Crimes Enforcement Network (FinCEN), and various state authorities with jurisdiction

[14] *See* U.S. Securities and Exchange Commission, Cyber Enforcement Actions, *available at* https://www.sec.gov/spotlight/cybersecurity-enforcement-actions.

over money transmission and investor protection issues. Accordingly, it is important for the SEC to work together with other regulators and to coordinate our activities to the extent possible and appropriate under the circumstances. Our level of coordination in this regard has been extensive. For example, the FinHub staff plays a key role in the Financial Stability Oversight Council (FSOC) Digital Asset and DLT Working Group. This group brings together federal financial regulators whose jurisdictions are relevant to the oversight of digital assets and their underlying technologies. The group seeks to enable the agencies to collaborate regarding these issues, including to promote consistent regulatory approaches and to identify and address potential risks.

FinHub staff actively monitors international developments related to FinTech, and engages with foreign regulators on a bilateral and multilateral basis to further our understanding of issues. Bilaterally, SEC staff regularly meets with foreign counterparts to share experiences and lessons learned on a wide range of FinTech topics. Multilaterally, staff directly participates in a number of ongoing initiatives by international bodies such as the Financial Stability Board (FSB), the International Organization of Securities Commissions (IOSCO), and the Financial Action Task Force (FATF).

To highlight some of the work we have done with IOSCO, in 2017, SEC staff initiated the launch of the ICO Network, a forum to facilitate a cross-border dialogue on ICO and related issues. The ICO Network is also developing a support framework to assist members as they consider ways to address such issues in their jurisdiction. Staff also actively participates in the IOSCO FinTech Network, created in May 2018 to facilitate collaboration among IOSCO members on FinTech. The group focuses on trends and potential implications for regulators in four areas: distributed ledger technology; artificial intelligence and machine learning ethics; regulatory technology (RegTech) and supervisory technology (SupTech); and lessons learned from innovation initiatives. Staff also contributed to a recently published consultation paper on risks and regulatory considerations relating to crypto-asset trading platforms.[15] This paper includes a "toolkit" of possible strategies that individual IOSCO member jurisdictions could use when developing their own regulatory approaches.[16]

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We are eager to see new beneficial technologies succeed, and do not view them as inconsistent with the SEC's core mission of protecting investors, maintaining fair, orderly and efficient markets, and facilitating capital formation. However, the long term promise of these technologies will be achieved only if those developing and implementing them comply with the laws, rules, and regulations that Congress and the SEC has put in place to further the agency's core mission.

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[15] *See* Board of the International Organization of Securities Commissions, *Issues, Risks and Regulatory Considerations Relating to Crypto-Asset Trading Platforms* (May 2019), *available at* https://www.iosco.org/library/pubdocs/pdf/IOSCOPD627.pdf.

[16] *See id.*

I cannot overstate the level of thought and effort that FinHub staff devote to evaluating the potential benefits and risks to investors and the markets associated with technological developments. Our goal, working with fellow regulators and market participants, is to thoughtfully assess how these new technologies impact the securities regulatory regime and to provide a path—and encouragement—for participants engaging in securities-related activities to promptly transition into compliance with regulatory requirements. We also evaluate requests for no-action letters and regulatory relief.

Thank you for the opportunity to testify before you today about the work of the SEC's FinHub and for your support of FinTech innovations. I appreciate the opportunity to work with the Task Force to engage with market participants on new approaches while continuing to enhance investor protection and market integrity. I look forward to answering any questions you may have.

Testimony of Paul Watkins
Assistant Director, Office of Innovation
Bureau of Consumer Financial Protection

Before the House Committee on Financial Services
Task Force on Financial Technology
"Overseeing the Fintech Revolution:
Domestic and International Perspectives on Fintech Regulation"

June 25, 2019

Good afternoon, Chairman Lynch, Ranking Member Hill, and members of the Task Force. Thank you for the opportunity to testify today. My name is Paul Watkins. I am the Assistant Director for the Office of Innovation at the Bureau of Consumer Financial Protection (Bureau). I bring to this role a background in consumer protection. Prior to my time at the Bureau, I was the Chief Counsel of the Civil Litigation Division in the Arizona Office of the Attorney General, where I managed the State's litigation in areas such as consumer fraud and civil rights. I also designed the State's FinTech Sandbox. I welcome this opportunity to talk with you about the Bureau's financial innovation work.

The Bureau created the Office of Innovation (OI) in July 2018 to facilitate consumer-beneficial innovation. Congress included facilitation of innovation and access to financial products and services in the Bureau's objectives. Innovation can also contribute to the Bureau's statutory purpose by increasing fairness, transparency, competition, and consumer access within financial services. In concert with other Bureau offices, OI aims to fulfill this mission through:

- Revising the Bureau's innovation policies and creating regulatory sandboxes, which are designed to address regulatory uncertainty that may impede innovation;
- Collaborating with other Federal, State, and international regulators; and
- Engaging with stakeholders on issues related to innovation.

Innovation Policies

To date, where the Bureau has proposed policies to fulfill this mission, it has sought public comment in order to solicit feedback from a broad spectrum of stakeholders. The Bureau has received approximately 60 comments from a variety of parties, including consumer advocates, civil rights groups, state officials, and business groups. Each of the proposed policies that I will discuss are just that – proposals. The Director has not yet decided whether to finalize them or in what form. While I cannot comment on the Bureau's internal and on-going deliberations about the proposals, I can say that the Bureau approaches the public's comments with an open mind and is carefully considering all input we have received on the proposed policies.

With that said, let me briefly describe each of the Bureau's proposed policies in turn. In September 2018, as a first step in revising the Bureau's innovation policies and creating regulatory sandboxes, the Bureau proposed the creation of a Disclosure Sandbox through

revisions to the Bureau's existing Policy to Encourage Trial Disclosure Programs.[1] Both the existing and proposed policies are based on the same statutory authority in Section 1032(e) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), which allows the Bureau to deem a covered person conducting a trial disclosure program to be in compliance with or exempt from a requirement of a Bureau rule or certain federal laws.[2] The existing Policy was issued in 2013 to enable firms to conduct in-market testing of innovative disclosures, but the Bureau has not approved any trial disclosure programs under the Policy.

In order to more effectively encourage companies to conduct trial disclosure programs, the proposed revisions would seek to, among other things:

- Streamline the application process and review time frame;
- Increase guidance regarding the testing time frame;
- Specify procedures for extensions of successful trial disclosure programs; and
- Provide for coordination with existing or future programs offered by other regulators designed to facilitate innovation.

The Bureau is proposing to focus the review process primarily on the extent to which the trial disclosures are likely to be an improvement over existing disclosures, and the extent to which the testing program mitigates risks to consumers. To facilitate the Bureau's awareness of the effects of trial disclosures on consumers, the proposed Policy would require participants to notify the Bureau of material changes in complaint patterns or other information that the Bureau should investigate. The terms of participation could also include additional data sharing requirements. In addition, under the proposed Policy the Bureau could revoke its permission to conduct a trial disclosure program in certain circumstances, such as failure to comply with the Bureau's terms and conditions of participation.

The proposed Policy would also inform potential applicants of the Bureau's expectation that a two-year testing period would be appropriate in most cases and include specific procedures for requesting an extension for successful trial disclosure programs. Finally, the proposed Policy would add a new section regarding Bureau coordination with other regulators that offer similar programs designed to facilitate consumer-beneficial innovation.

As a second step in improving its innovation policies, in December 2018, the Bureau proposed revisions to its existing Policy on No-Action Letters.[3] The existing Policy, which was issued in 2016, provides for the issuance of No-Action Letters consisting of non-binding staff-level supervision and enforcement no-action recommendations. The Bureau has issued only one such No-Action Letter under the existing Policy.[4] To increase the utilization of the Bureau's No-Action Letter program and to bring certain elements more in line with similar no-action letter programs offered by other agencies, the Bureau proposed revisions to the policy that would, among other things:

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[1] 83 FR 45574 (proposed Disclosure Sandbox policy); 78 FR 64389 (existing policy).
[2] 12 U.S.C. 5532(e)(2).
[3] 83 FR 64036 (proposed Policy); 81 FR 8686 (existing Policy).
[4] https://www.consumerfinance.gov/about-us/newsroom/cfpb-announces-first-no-action-letter-upstart-network/.

- Streamline the No-Action Letter application process;
- Streamline the Bureau's review of No-Action Letter applications, and focus the review on the potential benefits to consumers and the extent to which the applicant identifies and controls for potential risks to consumers;
- Revise data-sharing requirements and time-period limitations to more closely align the Bureau's no-action letter program with no-action letter programs offered by other Federal agencies; and
- Replace staff-recommendations of no-action with Bureau commitments of no-action.

While the proposed Policy would not expect applicants to share data as a condition for receiving a No-Action Letter, and would not assume that No-Action Letters would be time-limited, it is important to note that elements similar to those of the 2016 No-Action Letter Policy would be imported into the Bureau's proposed Product Sandbox (discussed below). Moreover, under the proposed No-Action Letter Policy, the Bureau would be adding requirements regarding notification of material changes to application information, which would enable it to monitor for risks to consumers. The proposed Policy also includes grounds for revocation similar to that in the proposed Disclosure Sandbox Policy.

At the same time it proposed revisions to the Bureau's existing Policy on No-Action Letters, the Bureau proposed the creation of a Product Sandbox that would require participants to share data with the Bureau concerning the products or services offered or provided, including information about potential risks to consumers.[5] In exchange for allowing Bureau monitoring that would otherwise not be required, the proposed Product Sandbox would include various forms of "safe harbor" protection from liability. The provision of these "safe harbors" would be for a limited time (two years in most cases) and would provide greater liability protection than that available through the No-Action Letter proposal. Like the proposed Disclosure Sandbox, the Bureau's proposed Product Sandbox would specify procedures for applying for extensions. It also includes grounds for revocation similar to that in the proposed Disclosure Sandbox.

Finally, like the proposed No-Action Letter program, the Bureau's proposed Product Sandbox would have a streamlined application and review process. It would also include a similar provision concerning Bureau coordination with other regulators that offer similar programs designed to facilitate innovation.

As I stated earlier, all three of these policies are still in the proposal stage and the Director has not yet decided whether to finalize them or in what form.

Collaborating with Other Regulators

In addition to the Bureau's work on the proposed policies, the Bureau is also working to better collaborate with other regulators, which is an important part of the Bureau's mission. Section 1015 of the Dodd-Frank Act instructs the Bureau to coordinate with Federal agencies and State regulators, as appropriate, to promote consistent regulatory treatment of consumer financial and investment products and services. Similarly, Section 1042(c) of the Dodd-Frank Act instructs

[5] 83 FR 64041.

the Bureau to provide guidance in order to further coordinate actions with the State attorneys general and other regulators. Consistent with those statutory provisions, each of the three aforementioned proposed innovation policies includes a section stating the Bureau's interest in actively partnering and coordinating with State, Federal, or international regulators on their own innovation-related initiatives.

On the international front, in August 2018, the Bureau joined the Global Financial Innovation Network (GFIN), an organization of regulatory agencies worldwide working together to support financial innovation. In January 2019, the Bureau became a Coordinating Member of GFIN. GFIN currently has more than 30 members and helps the Bureau coordinate with international regulators to facilitate innovation and promote regulatory best practices in consumer financial services. The Bureau currently participates in a GFIN work stream related to regulatory and supervisory technology.

Stakeholder Engagement on Innovation

The Bureau also seeks to facilitate innovation by engaging directly and in a variety of forums with stakeholders representing a diverse range of experiences and perspectives, including companies developing or providing innovative products and services, consumer advocacy groups, civil rights organizations, Federal and State regulators, trade associations, think tanks, and academia. In this aspect of its mission, the Office of Innovation works closely with other Bureau Divisions and Offices, including the External Affairs Division, the Office of Fair Lending, and various Markets offices in the Division of Research, Markets and Regulations.

More specifically, since the Office of Innovation was established, I and other members of the Office have participated in over 100 innovation-related meetings and events, and have engaged with FinTechs, financial institutions, consumer advocacy groups, and Federal, State, and international regulators. As part of its outreach functions, the Office of Fair Lending also meets regularly with stakeholders to discuss potential ways that innovation can expand access to credit to underserved populations. Other members of the Bureau have likewise participated in such events and meetings, including Bureau leadership, senior officials, and staff. Through these engagements, the Bureau is building a significant knowledge base about innovation in the markets for financial products and services.

Conclusion

The Bureau looks forward to advancing its statutory purpose by facilitating innovation and access to financial products and services.

Thank you again for the opportunity to testify today at this important hearing. I look forward to answering your questions.

Testimony of Christopher Woolard,
Executive Director for Strategy and Competition,
UK Financial Conduct Authority

To:

The U.S. House of Representatives; Committee on Financial Services;
Task Force on Financial Technology

"Overseeing the FinTech Revolution: Domestic and International Perspectives on FinTech Regulation"

June 25, 2019

Washington, D.C.

Summary

This testimony will set out some of the key work and supporting documents that the FCA and other UK agencies have published in relation to Innovation and Open Banking.

Innovation

1. **Project Innovate** Feedback Statement **(October 2014)**

   - Project Innovate was established in 2014 with the objective to foster innovation that can genuinely improve the lives of consumers. We observed that a wave of innovation was taking place in financial services, largely due to the increasing application of digital technologies and the growth of the FinTech sector, so in July 2014 we published a Call for Input that outlined the FCA's establishment of Project Innovate and ask for views on our proposals.
   - In October 2014 we published a Feedback Statement summarising the feedback we had received and setting out our response, which included the launch of our Innovation Hub to provide support directly to firms as they develop and launch their innovations, and to give the FCA a function with which to engage proactively with the FinTech ecosystem.

2. **Sandbox** Consultation Paper **(November 2015)**

   - Following recommendations by the Government Office for Science, the FCA was asked by Treasury to investigate the feasibility of developing a regulatory sandbox for financial services.
   - This paper set out the FCA's recommendations for implementing the regulatory sandbox. The sandbox allows firms to test innovative products, services and business models in a live market environment, while ensuring that appropriate safeguards are in place.
   - It aims to deliver more effective competition in the interests of consumers by:
     - reducing the time and, potentially, the cost of getting innovative ideas to market
     - enabling greater access to finance for innovators
     - enabling more products to be tested and, thus, potentially introduced to the market, and
     - allowing the FCA to work with innovators to ensure that appropriate consumer protection safeguards are built into their new products and services

3. Feedback Statement on supporting the development and adopters of RegTech **(July 2016)**

   - RegTech involves the development and application of technologies to help overcome regulatory challenges in financial services.
   - In 2015 we issued a Call for Input to find out more about how we could support the adoption and development of RegTech.
   - In this paper, we summarise key themes from the responses to that Call for Input, and outlined the FCA's approach in relation to RegTech and the role that we would play.

4. Sandbox Lessons Learnt **(October 2017)**

   - The sandbox is an experiment for us as well as for the firms testing in the sandbox. It was the first time we had allowed firms to test in this way, and as such at the start of the sandbox we undertook to publish lessons learned from its early stages of operation.
   - This report further explains how the sandbox operates, discusses the impact on the market and our insights from testing, and explains some limitations firms have faced when testing in the sandbox.

5. Impact and effectiveness of Innovate **(April 2019)**

   - Since launching Innovate, we have provided support to nearly 700 firms of varying shapes and sizes, have played an active role in the global FinTech ecosystem, and have produced policy on innovation in financial services markets.
   - In this report, we aim to shed light on the work we do through Innovate, why we do it, and why we think it advances the FCA's objectives in an effective manner. The report outlines evidence that suggests our work:
     - gives firms the regulatory certainty they need to develop their innovations and deliver them at speed
     - improves outcomes for consumers by firms we support bringing innovation to market and incumbents responding to compete harder and improve their own offerings
     - encourages positive innovation domestically and internationally.

Opening Banking

6. **Retail banking market investigation:** Final Report **(August 2016)**

   - The CMA is implementing a wide-reaching package of reforms. Central to the CMA's remedies are measures to ensure that customers benefit from technological advances and that new entrants and smaller providers are able to compete more fairly.
   - The key measure, which will benefit personal and small business customers, is:
   - Requiring banks to implement Open Banking to accelerate technological change in the UK retail banking sector. Open Banking will enable personal customers to manage their accounts with multiple providers through a single digital 'app', to take more control of their funds (for example to avoid overdraft charges and manage cashflow) and to compare products on the basis of their own requirements.

7. Open Banking: A Consumer Perspective **(January 2017)**
   - This report was written by Faith Reynolds, members of the FCA Consumer Panel and Consumer Representative for the Open Banking Implementation Entity.
   - The report provides a good introduction to the concept of Open Banking and the implications it will have for the payments market.

8. The future of competition and regulation in retail banking **(November 2017)**
   - This is a speech given by Christopher Woolard at the Future of Retail Banking 2017 event.
   - Retail banking is on the cusp of some of the most significant change the sector has ever seen in the form of PSD2 and Open Banking.
   - These changes are welcome, as competition has long been a concern in the retail banking industry.
   - As the regulator, we need to understand the impact of these changes on firms' business models, and how they may affect consumers.
   - PSD2 and Open Banking offer opportunities for incumbents, as well as challengers.

9. Payments after PSD2: evolution or revolution **(March 2018)**
   - This is a speech given by Karina McTeague at a conference in London.
   - From a consumer protection and market integrity perspective, we have a real interest in the Open Banking Implementation Entity's successful delivery of the CMA's Open Banking API requirements and wider adoption of APIs by the industry.

- Customer communications should be balanced, and not seek to dissuade customers from using third party AIS or PIS providers through their communications or terms and conditions.
- We welcome the development of industry arrangements designed to facilitate the successful delivery of PSD2 objectives (including voluntary guidelines and dispute management system).
- We will be looking to see that firms' culture prioritises treating customers fairly, and doesn't take inappropriate advantage of ill-informed, naïve or vulnerable consumers.

10. Modernising consumer markets: Consumer Green Paper **(April 2018)**

- Whitepaper published by BEIS, they are due to publish their smart data review in June 2019. This work is being considered alongside our work on Open Finance.
- Open Banking was launched in early 2018 and is offered by the nine largest UK banks and an increasing number of challenger banks. It allows consumers to provide third party providers, regulated by the FCA, with secure access to their current accounts in order for them to seamlessly provide a range of innovative new products tailored to the needs of consumers. It will make it easier for people to manage their money, putting them in control of their data. For example:
  - an app could monitor their spending and make payments
  - they could be alerted to saving and investment opportunities across accounts
  - they could authorise the movement of money between accounts to prevent overdraft charges and even access cheaper overdraft facilities without switching current account provider.
- In the UK, new innovative financial service providers are making use of this data, and plan to expand their offer to consumers by partnering with providers in other essential markets such as energy and telecoms.
- Key to Open Banking are the underpinning Application Programming Interfaces (APIs) which are standardised, making it easier for innovative new firms to deploy their products.

11. Strategic Review of Retail Banking Business Models: Final Report **(December 2018)**

- Our Final Report confirms our view that the Personal Current Account (PCAs) is an important source of competitive advantage for major banks.
- PCAs bring cheap funding from customer deposits and additional revenues from overdraft fees and other changes.
- Major Banks with large PCA networks have a net advantage even when the costs of providing the PCA and branch network are taken into account.
- Innovative business models like Open Banking, and competition could deliver better value and enhanced customer service, including:
  - cheaper or more convenient payment or overdraft solutions separate from current accounts;
  - budgeting and money management tools based on analysis of customer data;
  - enabling consumers to search and switch for better deals on savings and lending, and potentially switch to new providers.

12. Unlocking Digital Competition: Report of the Digital Competition Expert Panel **(March 2019)**

- The Digital Competition Expert Panel was established in September 2018 to consider the potential opportunities and challenges the emerging digital economy may pose for competition and pro-competition policy, and to make recommendations on any changes that may be needed.

- In the report, they make several references to the UK and FCA as good places for FinTech firms to go for their business development.
  - *"Clearer principles, rules and standards can support and enhance competitiveness and success in the global economic arena. UK is a leader in global banking in part thanks to its regulatory environment."*
  - *"The UK is a great place to start a FinTech company in part because of Open Banking, and the approach of the Financial Conduct Authority and the Payment Systems Regulator. Applying similar regulatory principles can improve the economic environment in the UK for digital start-ups and scale-ups while creating more predictability for large incumbent firms."*

13. Weighing the value of data – trade-offs, transparency and competition in the digital marketplace **(May 2019)**
    - This is a speech given by Robin Finer at a conference in London.
    - Data can have economic value for the consumer – it is a personalised input that reduces search costs and helps individuals to obtain products and services that better match their needs.
    - While consumers have difficulty understanding the value of their own information, the value of data to firms is augmented by their ability to combine data sources on individuals and then aggregate across consumers. The better they are at this, the more they'll attract new business and more information.
    - By increasing our understanding of these markets and the role and value of data, we can help empower consumers to choose what to share, where, and for what, as well as informing debates about how to deal with technology firms' market power.

14. Payment Services and Electronic Money – **Our Approach (June 2019)**
    - Our published guidance which can be used by firms to ensure compliance with PSD2. We make several allusions to Open Banking and the potential it has to change the payment industry in the UK.
    - We also explicitly state our preference for firms to make use of an API in order to provide a dedicated interface.

International Engagement

15. **Global Financial Innovation Network (GFIN)** – Consultation Document **(August 2018)**
    - The Global Financial Innovation Network founding members[1] published a consultation paper inviting responses on the proposal of a 'Global Sandbox' in the form of the Global Financial Innovation Network.
    - The paper set out the proposed mission statement and functions of GFIN, as well as details about how the Network would operate.
    - 99 responses from 26 jurisdictions were received. The response from industry and other international regulators was overwhelmingly positive in favour of establishing the GFIN to

[1] Founding members: Abu Dhabi Global Market (ADGM), Autorité des marchés financiers (AMF - Quebec), Australian Securities & Investments Commission (ASIC), Central Bank of Bahrain (CBB), Bureau of Consumer Financial Protection (BCFP, USA), Dubai Financial Services Authority (DFSA), Financial Conduct Authority (FCA, UK), Guernsey Financial Services Commission (GFSC), Hong Kong Monetary Authority (HKMA), Monetary Authority of Singapore (MAS), Ontario Securities Commission (OSC, Canada) and Consultative Group to Assist the Poor (CGAP).

facilitate a new practical method of regulatory collaboration on innovation and creating an environment for cross-border testing.

16. GFIN Terms of Reference for governance and membership (February 2019)

- The GFIN terms of reference set out the 3 primary functions:
  - To act as a network of regulators to collaborate and share experience of innovation in respective markets, including emerging technologies and business models, and to provide accessible regulatory contact information for firms.
  - To provide a forum for joint RegTech work and collaborative knowledge sharing/lessons learned.
  - To provide firms with an environment in which to trial cross-border solutions.
- Following the consultation feedback GFIN opened a 1 month application period for a pilot phase of cross-border testing. Interested firms were invited to submit applications to relevant participating regulators by 28 February 2019.

17. GFIN cross-border pilot testing – next steps (April 2019)

- 44 unique applications were submitted across the 17 participating regulators. Every regulator participating in the pilot was the subject of at least one application. Each regulator has considered whether a proposed test meets its individual screening criteria, areas of interest, and they have considered their ability to support the activity.
- After this initial screening, GFIN members will continue working with 8 firms. The next phase is for the firms to develop testing plans with the relevant regulators for their cross-border trial, some of which will involve live transactions. Firms that develop a testing plan satisfactory to each jurisdiction's criteria will take part in the pilot testing phase.

House Committee on Financial Services Taskforce on FinTech

June 2019

Christopher Woolard

Executive Director Strategy and Competition

Board Member, Financial Conduct Authority

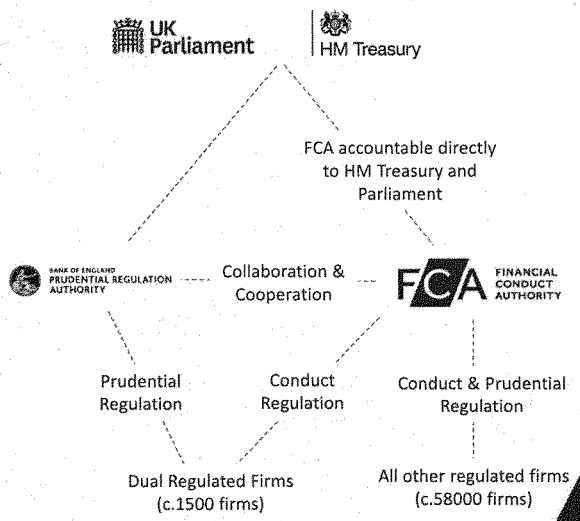
Chair, IOSCO FinTech Network

FCA Statutory Objectives

- Strategic objective of ensuring that the relevant markets function well;
- To secure an appropriate degree of protection for consumers;
- To protect and enhance the integrity of the UK financial system;
- Promote effective competition in the interests of consumers.

UK Regulatory Landscape

- The FCA is an independent public body.
- Work and purpose defined by the Financial Services and Markets Act.
- The FCA:
  - regulate standards of conduct in retail and certain wholesale markets;
  - supervise trading infrastructures that support those markets;
  - prudentially regulate firms not regulated by the Prudential Regulation Authority; and
  - operate the UK Listing regime.



Project Innovate

- From 2 employees in 2014 to a fully fledged Innovation division in 2019.

Aims

- Provide greater regulatory certainty for innovative business cases.
- Improve outcomes for consumers: we want to see innovation at scale.
- Encourage positive innovation to come to market.

Actions

- Provide formal and informal support in all Financial Services markets.
- Provide testing environment in the FCA Innovate Sandbox.
- Produce policy in innovative areas such as DLT and Cryptoassets.
- Encourage the development of RegTech and test potential solutions.

Project Innovate evaluation

- Early steers help firms develop and iterate their innovations.
  - Over 1,500 applications and nearly 700 firms supported.
  - Over 150 informal steers issued to clarify how we regulatory requirements.
- Guide firms through regulatory processes to get to market faster.
  - Over 100 new firms authorised through Project Innovate.
  - 40% reduction in time to be authorised for certain groups of firms.
- Firms supported by Innovate are establishing themselves in the market.
  - Around 80% of firms that completed Sandbox testing are still operating.
  - Start-ups in Sandbox cohort 1 received £135m of equity funding.
  - 13 of 50 firms to receive Direct Support have received over £165m of equity funding.
  - Open to all firms – major firms have tested as well as new FinTechs

Open Banking – the story so far

- The Payment Services Directive (PSD2) was adopted by EU in 2015.
- Implemented in UK law via the Payment Services Regulations in 2017.
- The Competition and Markets Authority (CMA) mandated 9 UK Banks to establish the Open Banking Standard in 2016.
- The Standard is delivered by 'Application Programming Interfaces' (APIs)
  - Secure method of providing access to data.
  - Standardised system aides implementation and innovation.

Outcomes

- Create more competition in retail banking sector for consumers.
- Reduce barriers to entry, increase financial inclusion and engagement.
- Improved visibility of accounts for consumers and clearer alternatives.

Open Banking ➡ Open Finance ➡ Open Everything?

- Success of open banking requires it to expand further.
- Looking to expand Open Banking type access to savings, pensions and mortgages markets.
- Encouraging innovation across financial services through the use of data.
- Moving toward a cross-sector approach with Smart Data consultation by the Department for Business, Energy and Industrial Strategy (BEIS).
- The Smart Data Review is looking at how data access could be carried out across regulated sectors (telecoms, energy and financial services).
- Improved consumer outcomes in all sectors.

International Collaboration

- Promoting collaboration through the Global Financial Innovation Network.
  - Driving cross jurisdictional collaboration on Fintech.
  - 35 international members.
  - Cross border testing pilot established with 8 firms (4 US headquartered).
- 11 cooperation agreements with international regulators.
  - Allowing more efficient information sharing.
  - Improving access to markets for firms.
  - Enhancing protections for consumers.
- Working with international counterparts to develop global standards.
  - Global Anti Money Laundering & Financial Crime TechSprint.
  - IOSCO Fintech Network.

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June 24, 2019

The Honorable Stephen Lynch
Chairman
Task Force on Financial Technology
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

The Honorable French Hill
Ranking Member
Task Force on Financial Technology
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

Re: Tomorrow's Hearing, "Overseeing the Fintech Revolution: Domestic and International Perspectives on Fintech Regulation"

Dear Chairman Lynch and Ranking Member Hill:

I write to you today on behalf of the National Association of Federally-Insured Credit Unions (NAFCU) ahead of tomorrow's hearing on "Overseeing the Fintech Revolution: Domestic and International Perspectives on Fintech Regulation" to share our thoughts regarding the growing role of fintechs in the financial services marketplace. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 117 million consumers with personal and small business financial service products. NAFCU and our members encourage the Task Force to continue to scrutinize the growing fintech sector, and we stand ready to work with you as you examine this important topic.

This emergence of fintech in the financial services marketplace presents new opportunities. However, it can also present new threats and challenges as entities emerge in an environment that can be unregulated or underregulated. As such, NAFCU believes that Congress and regulators must ensure that when fintechs compete with regulated financial institutions, they must do so on a level playing field where smart regulations and consumer protections apply to all actors in that space.

Just recently, we saw another example of the growing role of fintech in the financial services marketplace with Zillow officially entering the mortgage business through their new "Home Loans" division. We urge the Task Force to keep a watchful eye on developments such as this, where fintechs could end up benefitting from regulatory arbitrage and competing with fewer supervisory protections than regulated depository institutions.

It is important to note that credit unions do not view fintech companies in adversarial terms. There is no doubt that the responsible use of financial technology can have positive effects for consumers, and credit unions have always sought to leverage new technologies to make it easier for members to manage their finances, including through the development of new financial literacy tools. Credit unions continue to work with fintech companies to improve efficiency in traditional financial

services, and any future regulatory framework must recognize the value of these partnerships. At the same time, Congress should guard against the risk of unsupervised market disruptors who may be prioritizing time to market over transparency and consumer protection.

Consumers today have come to expect technological developments from their financial institution – from online banking to mobile bill pay. However, credit unions are concerned when unregulated fintech companies exploit supervisory gaps to obtain a competitive advantage in the marketplace. Although non-bank lenders are subject to the enforcement and rulemaking authority of the CFPB, they are not always supervised in the same way as credit unions or banks.

Certain fintech companies can also magnify data security concerns when they collect large quantities of consumer financial data. For example, a fintech company that consolidates or aggregates transactional and account information on a single platform elevates the risk of fraud and may not be subject to regular cybersecurity examination in the same way that credit unions are under the *Gramm-Leach-Bliley Act* (GLBA). The 2017 Equifax data breach exemplifies this risk, but the reality is that poor data security practices exist in virtually all unregulated industries. This is one reason why NAFCU strongly believes that Congress must establish a strong national data security standard akin to the GLBA's requirements for financial institutions that applies to all entities that handle consumer financial data. We hope that this issue will be on the Financial Services Committee's agenda this year as well.

Ultimately, credit unions view advancements in technology in holistic terms, and the adoption of new services, products or features is driven primarily by the not-for-profit, cooperative mission of prioritizing member service. As new companies emerge and compete in this area, it is important that they engage with traditional financial institutions on a level playing field of regulation – from data security to consumer protection. Finally, I would note that it is equally important that laws are modernized to allow credit unions to keep up and compete with technological advances that have altered both consumer expectations and business models.

Thank you for your attention to this important issue. We look forward to continuing to work with the Committee on this and other issues of importance to credit unions. Should you have any questions or require any additional information, please contact me or Janelle Relfe, NAFCU's Associate Director of Legislative Affairs, at 703-842-2237.

Sincerely,

Brad Thaler

Brad Thaler
Vice President of Legislative Affairs

cc: Members of the House Financial Services Committee

STATEMENT OF

the

FEDERAL DEPOSIT INSURANCE CORPORATION

on

"OVERSEEING THE FINTECH REVOLUTION: DOMESTIC AND INTERNATIONAL PERSPECTIVES ON FINTECH"

before the

TASK FORCE ON FINANCIAL TECHNOLOGY

of the

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

June 25, 2019
2129 Rayburn House Office Building

Chairman Lynch, Ranking Member Hill, and members of the Task Force, the FDIC appreciates the opportunity to submit this statement for the record for your hearing, entitled "Overseeing the Fintech Revolution: Domestic and International Perspectives on Fintech Regulation."

Technological changes in financial services are not new. ATMs and mobile banking are just two examples of how innovation and technology have transformed access to banking services and banking itself during our lifetimes. Today, innovation and technology have the potential to change how banks satisfy the needs of their customers by introducing new financial products and services, increasing access to affordable financial services, improving the regulatory and oversight process for banks, and contributing to safety and soundness.

The FDIC supports innovation in the financial services industry. FDIC Chairman Jelena McWilliams has put the agency at the forefront of this movement with last October's announcement of a new organization within the FDIC – the FDIC Tech Lab, or "FDiTech." The FDIC is in the process of recruiting a Chief Innovation Officer and laying the legal and operational foundation for FDiTech.

FDiTech will promote the adoption of innovative and transformative technologies in the financial services sector, help the FDIC better understand how innovation can contribute to the expansion of banking services to the unbanked, underbanked, and individuals in underserved communities as well as promote the adoption of technology that can help community banks compete in the modern financial market place.

Although FDiTech is just getting started, we have already taken steps to increase coordination and cooperation with technology firms, our fellow regulators, and the institutions we oversee. FDiTech will bring a renewed focus to these topics with a mandate to engage banks

and technology providers and to encourage the adoption of technology throughout the sector in a manner that promotes safety and soundness and consumer protections. The FDIC looks forward to continued collaboration with the Committee and this Task Force as FDiTech is established.

Using Technology to Meet Consumers' Needs

Overcoming challenges to economic inclusion is vital to the FDIC's mission to maintain public confidence in the financial system. The FDIC's most recent "Survey of Unbanked and Underbanked Households" shows that more than 8 million households do not have any relationship with the banking system.[1] Another 24.2 million households are underbanked, meaning they have a bank account but go outside of the banking system to satisfy some of their financial service needs.[2] Unbanked and underbanked rates are higher among lower-income households, less-educated households, younger households, black and Hispanic households, working-age disabled households, and households with volatile income. In short, millions of Americans are missing out on the important benefits banks provide, including access to credit, wealth-building opportunities, and the protection provided by deposit insurance.

Innovation and technology have the potential to provide important inroads to reach these consumers. The key customer-centric features of digital banking, such as online banking or mobile financial services applications, are affordability, convenience, and real-time access to information. These features not only enable consumers to understand their financial standing in real time, as well as plan for long-term goals and unexpected emergencies, but they also encourage wider adoption and promote financial access and inclusion.

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[1] *See* Federal Deposit Insurance Corporation, "2017 FDIC National Survey of Unbanked and Underbanked Households," (October 2018), available at https://www.fdic.gov/householdsurvey/2017/2017report.pdf.
[2] *Ibid.*

Using Technology to Improve the Supervisory Process

With the potential for so much change, it is incumbent upon the FDIC to understand how emerging technology can improve the FDIC's approach to supervision. In March, the FDIC held the inaugural meeting of the Subcommittee on Supervision Modernization for the Advisory Committee on Community Banking.[3] This subcommittee was established to support the FDIC's longstanding Advisory Committee on Community Banking and will consider ways in which the FDIC can leverage technology and refine processes to make the examination program more efficient, while managing and training a geographically dispersed workforce. The subcommittee is expected to hold three more meetings in 2019 and utilize conference calls or smaller group briefings to supplement its in-person discussions over the course of the year.

The FDIC is also in the process of developing and implementing updates to its information technology systems to bring much needed improvements to the systems that banks and non-banks use to interface and exchange information with the FDIC. There are multiple projects in various states of development, and over the next 18 to 24 months the FDIC plans to deploy technology improvements to deliver modern features and capabilities to improve the speed, reliability, and overall user experience for FDIC-supervised entities. Feedback on these improvements has been favorable, with bankers commenting that the new systems are "intuitive," "simple," and "night-and-day" improvements over the previous systems.

Technology and the Business of Banking

Technology is transforming not only how consumers access financial services, but the business of banking itself. For example, data analytics and artificial intelligence have the

[3] *See* FDIC Press Release: FDIC's Subcommittee on Supervision Modernization for the Advisory Committee on Community Banking Holds its Inaugural Meeting, PR-16-2019 (March 6, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19016.html

potential to help banks develop new approaches to assess credit risk. Analytical tools are enabling banks to better understand customers' needs and design more affordable, personalized products and services.

Much financial technology has been developed outside of the traditional banking system, driven by venture capital startups and emerging companies. A number of banks, particularly smaller institutions, have begun to embrace technology, and this has required a fundamental rethinking of how they interact with the technology industry.

The FDIC is particularly interested in being a bridge between technology companies and the banking sector to create an environment where innovation can thrive. This can be particularly meaningful for community banks, which may have limited resources to develop technology on their own.

The FDIC's Role in Fostering Innovation

The FDIC can foster innovation, while simultaneously protecting consumers, markets, and the Deposit Insurance Fund.

As the fintech environment has matured, the pace of change has increased. Federal financial regulators have begun to take stock of regulatory impediments to innovation that might ease compliance burden, make supervision more efficient, or give the unbanked and underbanked better access to the banking system. For example, on December 3, 2018, the FDIC, along with the other federal depository institution regulators and the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN), issued a *Joint Statement on*

Innovative Efforts to Combat Money Laundering and Terrorist Financing.[4] This statement encourages banks to consider responsible, innovative approaches to meet their Bank Secrecy Act/anti-money laundering compliance obligations. As this example demonstrates, regulators are mindful that their approach to oversight and regulation can affect the extent and speed of implementing financial innovation, and are striving to be forward-thinking, while maintaining the necessary protections of underlying regulations.

Although the FDIC is still in the process of standing up FDiTech, significant resources have already been dedicated to identify and understand emerging technological developments and their impacts on insured depository institutions, their customers, and the financial system overall. The FDIC approaches innovation with four fundamental questions:

1. How can the FDIC provide a safe regulatory environment to promote the technological innovation that is already occurring?
2. How can the FDIC promote technological development at our community banks with limited research and development funding to support independent efforts?
3. What changes in policy – particularly in the areas of identity management, data quality and integrity, and data usage or analysis – must occur to support innovation while promoting safe and secure financial services and institutions?
4. How can the FDIC transform – in terms of our technology, examination processes, and culture – to enhance the stability of the financial system, protect consumers, and reduce the compliance burden on our regulated institutions?

The FDIC is examining trends in retail financial markets, including marketplace and digital lending, digital payments, machine learning and artificial intelligence, big data, open

[4] *See* "Bank Secrecy Act: Interagency Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing" (FIL-79-2018), (December 2018), available at https://www.fdic.gov/news/news/financial/2018/fil18079.pdf.

banking, consumer-permissioned data sharing, and application programming interfaces. The agency is also monitoring developments in the wholesale financial markets, such as changes to payment systems, distributed ledger technology (e.g., blockchain), smart contracts, and digital assets. Over the last several years, this work has been overseen by the FDIC's Emerging Technology Steering Committee, which is comprised of senior leadership across the FDIC.

To gain a better understanding of these issues, the FDIC has engaged extensively with stakeholders, including financial institutions, consumer groups, trade associations, and technology companies on a variety of innovative, technology-driven products and services. In addition, through our ongoing supervisory processes, the FDIC regularly reviews supervised institutions' uses of technology. This includes innovations developed by FDIC-supervised institutions themselves, as well as activities conducted through their relationships with third parties.

To ensure a coordinated approach, the FDIC regularly engages in collaborative discussions with relevant financial regulators on these topics through venues like the Federal Financial Institutions Examination Council (FFIEC), Financial Stability Oversight Council (FSOC), and Interagency Fintech Discussion Forum.

On the international front, the FDIC is part of the Basel Committee on Banking Supervision's Task Force on Financial Technology. The Task Force's work resulted in the publication of "Sound Practices: Implications of fintech developments for banks and bank supervisors,"[5] which assesses how technology-driven innovation in financial services may affect the banking industry and the activities of supervisors in the near- or medium-term.

[5] Basel Committee on Bank Supervision, "Sound Practices: Implications of fintech developments for banks and bank supervisors," (February 2018), available at https://www.bis.org/bcbs/publ/d431.pdf.

On April 24, 2019, the FDIC, in partnership with Duke University, hosted a research and policy conference on financial technology and the future of banking. Prominent academic experts delivered presentations on technology's impact on lending, financial advice, and competition.[6] Senior leaders in the financial industry and financial policy experts shared their views on these topics as well. The event drew more than 300 representatives of banks, nonbank financial companies, technology service providers, federal regulatory agencies, other government agencies, Congress, nonprofit organizations, and research institutions.

FDIC Tech Lab

As previously noted, the FDIC is launching a new internal office to focus on innovation and technology (i.e., the FDIC Tech Lab, or "FDiTech.")

FDiTech's goals are to engage and collaborate with innovators in the financial and nonfinancial sectors to identify, develop, and promote technology-driven solutions that:

- Improve the safety and soundness of FDIC-insured institutions,
- Support the development and adoption of innovative financial products and services,
- Increase economic inclusion and consumer benefits,
- Promote competition,
- Support the early identification of risk at financial institutions or in the financial system, and
- Facilitate the efficient resolution of failed financial institutions, when that is needed.

To further its mission and within FDIC's authorities under the FDI Act, FDiTech will engage directly with innovators and community banks around the country and sponsor or co-sponsor

[6] *See* Fintech and the Future of Banking, (April 24, 2019), available at https://www.fdic.gov/bank/analytical/fintech/agenda.html.

"tech sprints" to promote innovation and find solutions to challenges facing consumers and the industry. For truly innovative and new technologies, the FDIC may also conduct voluntary pilot programs, in cooperation with our regulatory partners in the states, to help community banks test new products and services within legal and regulatory parameters.

Conclusion

Too often regulatory agencies play "catch up" with technological advancements and their impact on regulated entities and consumers. The FDIC's goal is to reverse that trend through increased collaboration and partnership with the industry. Working together, the FDIC can help increase the velocity of transformation, while ensuring that banks continue to operate in a safe and sound manner and consumers remain protected.