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TESTIMONY OF
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before the
TASK FORCE ON FINANCIAL TECHNOLOGY
COMMITTEE ON FINANCIAL SERVICES
UNITED STATES HOUSE OF REPRESENTATIVES

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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.

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.

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.

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.

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

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 paper¹¹ 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

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.