

# OCC Issues Latest Fintech Interpretive Letters Covering Distributed Ledger Technology in Payments and Limited Purpose Banks

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The Office of the Comptroller of the Currency (the “OCC”) recently issued two interpretive letters that are designed to facilitate the use of financial technology and Fintech charters. The first [interpretive letter](#), issued by the Chief Counsel, determines that national banks and federal savings associations (together, “banks”) may use and issue stablecoins and participate in independent node verification networks (“INVN”) to facilitate payment transactions (the “INVN Letter”). The INVN Letter was followed by an additional [interpretive letter](#) issued by the Chief Counsel addressing the authority of the OCC to charter a bank that limits its operations to those of a trust company and activities related thereto (“national trust banks”), determining that national trust banks may engage in certain activities permissible for a state trust bank or company (“state trust banks”), even if those activities are not necessarily considered fiduciary in nature under 12 USC § 92a and 12 CFR Part 9 (the “National Trust Bank Letter”).

These letters are the latest in a series of interpretations by the OCC under former Acting Comptroller Brian Brooks that evidence the former Acting Comptroller’s encouragement of new technologies and new business models.<sup>1</sup> However, it remains to be seen what the OCC’s position on Fintech will be under the Biden administration.<sup>2</sup>

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<sup>1</sup> Last year, the OCC Chief Council issued letters clarifying that banks can provide cryptocurrency (including stablecoin) custody services for customers and hold deposit “reserves” on behalf of customers that issue certain types of stablecoins. For more information, please see our analysis available [here](#). Brooks also made statements at the 2020 Cato Summit on Financial Regulation asserting that he has authority to charter nondepository banks. Related, there has been recent controversy around the agency’s apparent willingness to grant a national bank charter to Figure Technologies Inc., which would accept only uninsured deposits. That proposal has spurred the Conference of State Bank Supervisors to file a complaint in D.C. federal court against the OCC and Brooks.

<sup>2</sup> Notably, on December 4, 2020, House Financial Services Committee Chairwoman Maxine Waters, sent a [letter](#) to President-Elect Joe Biden recommending that the OCC’s guidance on holding stablecoin reserves and custodying cryptocurrency be rescinded. It is also not yet clear how the work of other federal agencies will impact these OCC initiatives. Senator Sherrod Brown, the incoming chairman of the Senate Banking Committee, has introduced a bill that would provide free bank accounts through digital dollar wallets (see our analysis available [here](#)) and the Federal Reserve’s plan to develop a new round-the-clock real-time payment and settlement service called the FedNow<sup>SM</sup> Service is expected to be available in 2023 or 2024. On the securities front, Gary Gensler, the announced nominee for the next chairman of the U.S. Securities and Exchange Commission (“SEC”), has testified before the House Agriculture Committee on cryptocurrencies and will likely also be focused on these issues during his tenure, if he is confirmed.

Should the INVN Letter remain in effect, it may change the U.S. payment landscape by paving the way for stablecoins to be used as a means of effecting real-time payments. For *de novo* institutions, the National Trust Bank Letter may provide a route to seeking a national bank charter and at the same time help avoid legal challenges associated with the Southern District of New York's decision striking down the OCC's special purpose national bank charter for Fintechs<sup>3</sup> and the new legal action surrounding nondepository bank charters like the one sought by Figure Technologies Inc.<sup>4</sup>

Below, we provide a brief summary of each of these recent letters.

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## INVN Letter

The INVN Letter allows banks to facilitate payment transactions using INVNs and stablecoins, including by: validating transactions by serving as a node on the INVN, facilitating the conversion from U.S. dollars to stablecoin (and vice versa), and issuing stablecoins. According to the letter, the OCC expects that these new technologies will increase the speed and efficiency and lower the cost of payment transactions such as cross-border remittances. As with all other activities, banks must of course participate in such transactions in a manner consistent with safe and sound banking practices and all other applicable laws, and in particular should focus on heightened risks around fraud, liquidity, compliance with the Bank Secrecy Act ("BSA") and other Anti-Money Laundering ("AML") laws, and consumer protection laws and regulations. Banks also should ensure that they have the appropriate technological expertise to conduct such activities and, importantly, under the terms of the letter they are required to consult OCC supervisors prior to engaging in activities covered by the letter.

### Stablecoins and INVNs

Stablecoins are a type of cryptocurrency designed to have a stable value. Fiat-backed stablecoins are backed by, and can typically be exchanged for, the underlying fiat currency. Stablecoins may be used by a bank to facilitate payment transactions if the bank issues a stablecoin<sup>5</sup> and exchanges that stablecoin for fiat currency. Stablecoins transactions are recorded, validated and broadcasted using distributed ledger technologies, which are INVNs or shared electronic databases where copies of the same information are stored on multiple computers.

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<sup>3</sup> Lacewell v. Office of the Comptroller of the Currency, No. 18-cv-8377 (S.D.N.Y. Oct. 21, 2019).

<sup>4</sup> The company would not take FDIC-insured deposits but would originate uninsured deposits.

<sup>5</sup> The letter cautions that certain stablecoins may be securities and that a bank's issuance of a stablecoin must comply with all applicable securities laws and regulations.

When taken together, stablecoins and the INVNs represent a new payment technology that, to some, promises to be safer, faster and more cost-effective than other existing payment systems. To establish the role of banks in this new payment infrastructure and potentially also to encourage participation and competition in this space, the letter provides that:

- a bank may serve as a node on an INVN; and
- a bank may use INVNs and related stablecoins to carry out other permissible payment activities (including by issuing and facilitating the exchange of stablecoins for fiat currency).

The letter also reiterates a point made in a recent statement of the President's Working Group on Financial Markets,<sup>6</sup> noting that stablecoin arrangements should:

- provide for the capability to obtain and verify the identity of all transacting parties, including for those using unhosted wallets;<sup>7</sup> and
- have appropriate systems, controls, and practices in place to manage relevant risks, including strong reserve management practices ensuring a 1:1 reserve ratio and adequate financial resources to absorb losses and meet liquidity needs.

## Commentary

Citing examples from ancient Rome, Mesopotamia and Egypt, the INVN Letter notes that banks have long played a role as financial intermediaries in exchanging payments and securities to settle transactions for other parties and such financial intermediation can take many forms. As a legal matter, the INVN Letter relies on banks' authority to engage in payment-related activities<sup>8</sup> and to use electronic means or facilities to perform any function of an authorized activity<sup>9</sup> as the basis for its conclusions.

Among other things, the letter highlights that the OCC has explicitly permitted banks to adopt new technologies to carry out payment services, for example, engaging in

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<sup>6</sup> President's Working Grp. on Fin. Markets Releases Statement on Key Regulatory and Supervisory Issues Relevant to Certain Stablecoins, Treasury, SM-1223 (Dec. 23, 2020), available [here](#).

<sup>7</sup> See also our analysis on the recent Financial Crimes Enforcement Network ("FinCEN") notice of proposed rulemaking to require banks and money service businesses to submit reports, keep records, and verify the identity of customers in relation to transactions involving certain convertible virtual currencies and digital assets held in unhosted wallets, available [here](#).

<sup>8</sup> See, e.g., IL 1157; IL 1140; OCC Interpretive Letter 1014 (Jan. 10, 2005); OCC Interpretive Letter 929 (Feb. 11, 2002); OCC Interpretive Letter 993 (May 16, 1997) (IL 993); IL 737; OCC Conditional Approval Letter 220.

<sup>9</sup> See 12 CFR § 7.5000 et seq.; 12 CFR § 155.200.

activities related to electronic funds transfer systems,<sup>10</sup> real-time settlement systems,<sup>11</sup> and stored value systems.<sup>12</sup> The letter also analogizes the use of INVNs and related stablecoins to the use of electronically stored value (“ESV”) systems, which are permissible bank activities.<sup>13</sup> While it remains to be seen whether the INVN Letter will be rescinded or modified under the Biden administration, assuming that it remains valid, it could change the landscape of the U.S. payment system.<sup>14</sup> Further, because the letter requires a bank to consult its OCC supervisors before relying on the letter, new leadership at the OCC presumably could avoid the proliferation of activities covered by the letter without rescinding the letter itself (and instead by declining to provide supervisory non-objection to commencement of activities covered by the letter).

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## National Trust Bank Letter

For Fintechs seeking to organize a *de novo* banking organization, charter choice is often one of the first and most critical decisions to be made. If it remains effective, the National Trust Bank Letter may present a viable alternative for Fintechs that seek to engage in only nondepository activities. As described below, the letter recognizes that national trust banks may engage in fiduciary and non-fiduciary activities, including those activities permissible for state trust banks.

The OCC’s authority to charter national trust banks comes from 12 USC § 27(a), which provides that a national bank that limits its activities to *those of a trust company and activities related thereto* is not illegally constituted. According to the National Trust Bank Letter, there is no textual or other statutory guidance on what constitutes a “trust company” and the phrase contained in 12 USC § 27(a) has been interpreted to include the activities of trust departments of banks and the activities of state trust companies and trust banks. The letter confirms that such activities typically include fiduciary activities as defined under federal and state law, as well as activities that are non-fiduciary in nature, such as non-fiduciary custody.

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<sup>10</sup> See, e.g., IL 890; IL 854.

<sup>11</sup> See, e.g., IL 1157; IL 1140.

<sup>12</sup> See, e.g., OCC Conditional Approval Letter 220; OCC Conditional Approval Letter 568; IL 737.

<sup>13</sup> 12 CFR 7.5002(a)(3).

<sup>14</sup> In a recent interview with Politico, Brooks explained that the point of clarifying that banks can act as nodes in blockchain networks is to say to banks, “Hey, listen, you’re not limited in your ability to engage in payments by the Clearing House and the Federal Reserve. There are these other networks for value exchange, and you’re welcome to connect to those and use those networks for real-time payments, if you want to.’ Those are cheaper and faster, so that’s a good thing. And you know, expect that’ll happen. And frankly, if you look at the rate at which stablecoins have started to be adopted by banks as it is, I think that the future on that front is a lot closer than most people think.” Victoria Guida, POLITICO Pro Q&A: Former Acting Comptroller Brian Brooks, POLITICO (1/15/2021, 6:14 PM).

Accordingly, a national trust bank may conduct fiduciary activities as defined by state or federal law and certain non-fiduciary activities (e.g., non-fiduciary custody), as described below. The letter adds that there is no *de minimis* rule regarding national banks' use of trust powers; and there is no requirement that such a bank perform primarily in a fiduciary capacity.

### **Fiduciary Activities Authorized Under State Law**

Twelve USC § 92a provides that a national bank with trust powers may engage in “any other fiduciary capacity in which State banks, trust companies, or other corporations which come into competition with national banks are permitted to act under the laws of the State in which the national bank is located.”<sup>15</sup> This is known as the “bootstrap.” provision of 12 USC § 92a and generally authorizes such national banks to engage in all fiduciary activities of state trust banks located in the same state as the national bank. The letter clarifies that in order to rely on the bootstrap provision, the OCC must determine that the national trust bank is engaging in the relevant activity, role, or function consistent with the parameters provided for in the relevant state law for a state bank.<sup>16</sup>

### **Fiduciary Activities Authorized by the OCC**

In addition to the bootstrap provision, 12 USC § 92a and 12 CFR Part 9 enumerate activities or roles under the definition of “fiduciary capacity,” including trustee, transfer agent, investment adviser (if the bank receives a fee for its investment advice), and any capacity in which the bank possesses investment discretion on behalf of another. Naturally, a bank may conduct any of these fiduciary activities under a national trust bank charter.

Twelve CFR Part 9 also provides that the OCC may authorize similar activities pursuant to 12 USC § 92a. In determining whether an activity falls under this prong, the National Trust Bank Letter states that the OCC will consider whether the substantive conduct of the bank is analogous to the enumerated fiduciary capacities in 12 USC § 92a and 12 CFR Part 9. Specifically, the OCC will consider: (1) whether the activity involves the exercise of discretion on behalf of a client or third party in a manner that would have an economic impact on the client or third party, and (2) whether, in carrying out the discretionary activities, the bank is subject to the duties or standards of behavior that are

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<sup>15</sup> Notably, the letter does not expand this authority beyond the laws of the state in which the national trust bank is located. Thus, different national trust banks may be legally permitted to conduct different activities depending on the states in which its branches are located.

<sup>16</sup> The letter provides that Interpretive Letter No. 265, which concluded that the OCC will only look to state law to determine whether a fiduciary capacity of a national bank is permissible after the activity is determined to be “fiduciary” within the meaning of 12 USC § 92a, is superseded to the extent it conflicts with this decision.

customarily associated with being a fiduciary.<sup>17</sup> Accordingly, the letter provides an additional potential avenue for new financial activities or roles to be conducted under a federal charter that is not dependent on authorization under state law.

### **State Trust Bank Activities That Are Part of the Business of Banking**

The OCC may authorize national banks to engage in specific activities that are part of the business of banking and incidental to the business of banking under 12 USC § 24(Seventh). The National Trust Bank Letter provides that the OCC may use such authority to authorize a national bank to engage in an activity permitted for a state trust bank if the OCC is satisfied that the following factors required to be considered for such an authorization are sufficiently met:

- The activity is the functional equivalent to, or a logical outgrowth of, a recognized banking activity.
- The activity strengthens the bank by benefiting its customers or its business.
- The activity involves risks similar in nature to those already assumed by banks.<sup>18</sup>

Accordingly, the letter appears to contemplate the OCC authorizing national banks to engage in electronic activities that are permitted for state trust banks, including state trust banks located in a state in which the national bank is not located. The National Trust Bank Letter adds that any national bank without fiduciary powers may engage in state trust bank activities under this authority as long as they are not fiduciary for purposes of 12 USC § 92a or 12 CFR Part 9.<sup>19</sup>

### **Commentary**

As noted, the National Trust Bank Letter may help charter applicants and the OCC to avoid the legal challenges associated with the OCC's special purpose national bank

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<sup>17</sup> The letter cites the following as among the common duties of a fiduciary: duty of loyalty (acting in good faith, protecting the interest of the client, and taking no action in favor of the fiduciary that would impair the interest of the client); duty of care or prudence (exercising reasonable care, skill, and caution in performing activities); duty to segregate funds (keeping client assets distinct from other assets, including those of the fiduciary); duty to safeguard (protecting client assets from damage, loss, or destruction); duty to invest (acting as a prudent investor bearing the purpose and interest of the client mind); and duty of accounting (providing full and fair disclosure and keeping records of receipts, expenses, sales, purchases, exchanges and/or distributions to account for the fiduciary's activities on behalf of the client).

<sup>18</sup> See 12 CFR 7.5001(c)(1) (listing, in addition to the three factors above, "[w]hether the activity is authorized by state-chartered banks"). The letter also states that the OCC has discretion to vary the weight given to each factor when considering the factors described in section 7.5001(c)(1).

<sup>19</sup> The letter encourages national banks seeking guidance on whether a new activity would be subject to 12 CFR Part 9 to speak with examination staff, which may seek further guidance from attorneys and others within the OCC.

charter for Fintechs and the new legal action surrounding nondepository bank charters like the one sought by Figure Technologies Inc. Moreover, a national trust bank charter could allow the bank access to the Federal Reserve payment system and its parent and other affiliates to avoid regulation by the Federal Reserve.

There is already evidence that the national trust bank charter is appealing to Fintechs. Two days after the National Trust Bank Letter was issued, the OCC conditionally approved the application of a state trust bank to convert to a national trust bank (Anchorage Digital Bank, National Association) and continue to engage in activities related to digital assets, including custodying digital assets.

However, the National Trust Bank Letter does not appear to be exclusively directed at national trust banks. The letter essentially provides national banks without fiduciary authority something akin to a “wildcard statute” with respect to state trust bank activities, potentially allowing national banks to engage in activities permissible for trust banks chartered in any state.

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