

# Skinny Charters:

## Rebuilding the Banking Regulatory Perimeter

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*One of the most controversial contemporary issues in financial regulation involves who should get access to a federal banking charter. Chartering was how regulators maintained a congressionally mandated separation between banking and commerce. Today, however, the regulatory perimeter barely exists—but it is not because of overweening banks using their balance sheets to manipulate their way into commerce, but the entry of nonbanks into banking.*

*Large commercial firms offer their customers deposit accounts, debit and credit cards, direct deposit for paychecks, and payments processing. Financial technology firms, or fintechs, increasingly offer a suite of some or all of the trinity of banking services—taking deposits, making loans, and processing payments. Other nonbanks now handle much or most of what used to be the core of banking, including mortgage origination and commercial lending. For their part, the big bank evasions of the regulatory perimeter are not new—they offer investment banking, compete with mutual funds, and can market other financial products, but have done so for a while. To be sure, the regulatory perimeter has always been porous—the very traditional trust charter has allowed banks to offer services outside the banking trinity, and nonbanks a way to participate in some services traditionally offered by banks. But those tools had never been interpreted to permit the mixing of commerce and banking allowed today.*

*This Article offers a host of takeaways. It shows how the always porous regulatory perimeter is now being breached by a varied mix of commercial firms taking on banking responsibilities. It proposes that a new, intentionally, rather than haphazardly, permeable regulatory perimeter be rebuilt through the offering of a variety of ‘skinny charters,’ including fintech charters, payments charters, and perhaps also deposit and lending charters. It takes a deep dive into the history and present of the trust charter, one of the oldest ways that banks and nonbanks traversed the regulatory perimeter, and a likely future source of charters for fintechs. Moreover, thinking these policies through provides an opportunity to assess the undertheorized role of licensing in administrative law, which, this article argues, is prone to becoming the sort of common law regime licensing was designed to replace. It makes that case by through a quantitative analysis of federal bank licensing decisions that establishes, through the application of plagiarism software, that licensing decisions look like one another—that parts of them follow precedent. A looser regulatory*

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*perimeter would better reflect the way financial services are offered now, and increase competition in banking services, while maintaining the traditional license for the most dangerous kinds of banks.*

INTRODUCTION.....	700
I. BREACHING THE REGULATORY PERIMETER.....	705
A. <i>The Business of Banking</i> .....	706
B. <i>The Entry of Commercial Firms into Banking</i> .....	708
1. <i>Walmart Returns to Banking</i> .....	709
2. <i>PayPal and Service Tying</i> .....	712
C. <i>Big Commerce Lends Money</i> .....	714
D. <i>Nonbanks As Deposit-Takers</i> .....	718
E. <i>Fintechs Are Entering Finance . . . Sometimes with Banking Licenses</i> .....	720
F. <i>Banks Have Breached the Perimeter as Well, But They Always Have</i> .....	723
1. <i>Banks Rent Out Their Charters to Allow Nonbanks to Breach the Regulatory Perimeter</i> .....	723
2. <i>Banks Now Underwrite Most Securities Offerings</i> .....	725
3. <i>Banks Compete with Mutual Funds</i> .....	726
4. <i>Banks Are Dipping a Toe into Commerce (If It Brings In Customers)</i> .....	729
II. THE TRUST CHARTER AS THE EDGE CASE.....	730
A. <i>Trust Charters for Fintechs: State Efforts</i> .....	732
B. <i>Enter The Feds</i> .....	736
III. THE LICENSE: PUBLIC INTEREST, PUBLIC CHOICE, AND COMMON LAW .....	743
A. <i>Public Interest</i> .....	743
B. <i>Public Choice</i> .....	745
C. <i>Licensing As Common Law</i> .....	746
IV. QUALITATIVE AND QUANTITATIVE ANALYSIS OF CHARTER GRANTS .....	747
V. THE SKINNY CHARTER.....	750
CONCLUSION .....	752

## INTRODUCTION

One of the most important ways to regulate banking is to limit who can do it, but it is time for the old rules to be rethought. Regulators are supposed to maintain a “regulatory

perimeter,”<sup>1</sup> separating banking and commerce, with never the twain to meet.<sup>2</sup> The Bank Holding Company Act reified the separation by prohibiting commercial firms from owning government-insured banks.<sup>3</sup> Saule Omarova has observed that “[t]he separation of banking and commerce is one of the fundamental principles underlying the U.S. system of bank regulation.”<sup>4</sup>

That perimeter has been breached, although not in the way anyone expected. Enormous commercial firms offer almost every kind of banking service—Walmart alone has do-everything MoneyCenters in half of its stores and now holds 18.7% percent of the consumer checking market—and neither banks nor their regulators seem to care.<sup>5</sup> That is a real change from 2006 when the industry fiercely opposed Walmart’s initial tentative entry into financial services.<sup>6</sup>

1. As Howell Jackson has observed, “[d]rawing an effective line between activities that must be brought within the regulatory perimeter for entity regulation and those activities that can remain outside of direct supervisory oversight is a fraught task,” which, as this article will show, is undoubtedly the case. Howell E. Jackson, *The Nature of the Fintech Firm*, 61 WASH. U. J.L. & POL’Y 9, 15 (2020). For more on the challenges of maintaining a clean regulatory perimeter, see Alexandros Vardoulakis et al., *Lessons from the History of the U.S. Regulatory Perimeter*, BD. GOVERNORS OF THE FED. RSRV. SYS. (Oct. 15, 2021), <https://www.federalreserve.gov/econres/notes/feds-notes/lessons-from-the-history-of-the-u-s-regulatory-perimeter-20211015.html> [<https://perma.cc/46DA-H4ZC>] (discussing the perimeter in relation to so-called “stablecoins”).

2. “The United States has had a long tradition of legislative separation of banking and commerce.” Paul A. Volcker, *Statements by Paul A. Volcker, Chairman, Board of Governors of the Federal Reserve System, before the Subcommittee on Commerce, Consumer, and Monetary Affairs of the Committee on Government Operations, U.S. House of Representatives, June 11, 1986.*, 72 FED. RSRV. BULL. 541, 544 (1986); see also *Financial Services Restructuring: Hearings on H.R. 797 Before the Subcomm. on Telecommunications and Finance of the House Comm. on Energy and Commerce*, 102d Cong. 357 (1991) (discussing a potential “reversal of the long-standing U.S. tradition of separating commerce from banking”); Reid B. Stevens & Jeffery Y. Zhang, *The Costs of Banks Engaging in Non-Banking Activities: A Case Study*, 39 YALE J. ON REGUL. 375, 377 (2022) (“The legal separation of banking and commerce goes back almost a century in the United States and many more centuries in Europe.”); S. REP. NO. 100-19, at 2 (1987) (“At the foundation of American financial law is a longstanding tradition of separating banking and commerce. This separation has served to preserve the equal availability of credit in the United States and minimize the concentration of financial and economic power.”).

3. 12 U.S.C. § 1843 (prohibiting bank holding companies from the “direct or indirect ownership or control of any voting shares of any company which is not a bank”). For a discussion of how the act does so, see Arthur E. Wilmarth, Jr., *Wal-Mart and the Separation of Banking and Commerce*, 39 CONN. L. REV. 1539, 1550 (2007).

4. Saule T. Omarova, *The Merchants of Wall Street: Banking, Commerce, and Commodities*, 98 MINN. L. REV. 265, 273 (2013).

5. Kevin Payne, *Walmart Now Offers Banking Services. Here’s What to Expect*, MOTLEY FOOL: THE ASCENT (Jan. 20, 2023), <https://www.fool.com/the-ascent/banks/articles/walmart-now-offers-banking-services-heres-what-to-expect/> [<https://web.archive.org/web/20221207180548/https://www.fool.com/the-ascent/banks/articles/walmart-now-offers-banking-services-heres-what-to-expect/>]; Ray Birch, *Walmart Headed for ‘Dominance’ in Checking*, CUToday (Aug. 02, 2022), <https://www.cutoday.info/site/THE-feature/Walmart-Headed-For-Dominance-In-Checking> [<https://perma.cc/PHZ9-4CYF>].

6. Walmart applied for a so-called industrial loan carter, and obtained one from the state of Utah, but was unable to obtain deposit insurance from the FDIC. For discussions of the contretemps, see Richard E. Gottlieb, Brian Korn & Taylor Steinbacher, *Four-Way Stalemate: Recent Developments in Regulatory Compliance for Fintech Companies and Marketplace Lenders*, 75 BUS. LAW. 1931, 1937 (2020) (“Walmart and Home Depot sought ILC charters in the mid-2000s but withdrew their applications after intense lobbying and public outcry.”); Mehrsa Baradaran, *The ILC and the Reconstruction of U.S. Banking*, 63 SMU L. REV. 1143, 1144 (2010) (“The commotion surrounding the ILC died down shortly after Wal-Mart withdrew its application in 2007, but skepticism of its value and soundness continues to remain high among some lawmakers and regulators.”).

For their part, banks have expanded beyond the traditional regulatory perimeter, but mostly in ways that are old news. They have also shrunk from doing all the possible activities that their perimeter would permit. Banks now own all the large investment banks—something that was banned in the United States for 60 years, but that is met with a shrug today—but that process started in 1999 and finished in 2008.<sup>7</sup> Banks offer products substantially similar to money market funds, which are regulated by the Securities Exchange Commission, rather than the banking agencies; they breached that regulatory perimeter 90 years ago.<sup>8</sup> And many banks are partnering with nonbanks to let the nonbank offer financial services to their clients—a sign that the old regulatory perimeter is being ignored as a functional matter.<sup>9</sup>

What this means is that the old licensing regime for banks increasingly does not do the work that that regime was supposed to do. In this Article, I recommend that the licensing project be rethought. Bank licensing should be expanded to include financial technology firms. Both the Obama and the Trump administrations tried to extend a limited charter to them, this effort could be redoubled; nonbanks also provide useful competition for banks.<sup>10</sup>

Bank regulators should also offer *skinny* banking licenses, such as for payment processors who do not want to hold deposits or lenders who want to finance their lending with private equity or other unconventional sources of capital, as so-called “peer to peer” or private credit lenders do.<sup>11</sup>

A more officially countenanced regulatory perimeter would better reflect the reality of financial engagement today, could increase competition for banking services in a way that would benefit consumers, and would also make for a more nimble financial system.

But this Article offers more than a new account of the modern breakdown of the regulatory perimeter, which mostly reflects commerce entering banking, and has plenty of precedent, given that the perimeter has always been porous. It also offers a definitive account of one of the oldest means of breaching the regulatory perimeter, and one of the most plausible ways that financial technology firms will get a banking charter—the trust bank charter. It takes all the developments as an opportunity to reflect on the license as administrative law. And it finally offers a mildly empirical story about how licensing decisions

7. 12 U.S.C. § 377 (repealed 1999); 12 U.S.C. § 78 (repealed 1999). See Joe Mahon, *Financial Services Modernization Act of 1999 (Gramm-Leach-Bliley)*, FED. RESRV. HIST. (Nov. 22, 1999), <https://www.federalreservehistory.org/essays/gramm-leach-bliley-act> [<https://perma.cc/TF3J-D92Y>] (explaining the aftermath of the repeal).

8. See *infra* Part I.F.3.

9. See *infra* Part I.F.1.

10. It was eventually the first Trump administration that made the change.

While the Obama Administration’s comptroller Thomas Curry is the [OCC] head who began consideration of the special purpose fintech charter, it is the Trump Administration’s Joseph Otting who helmed the Agency when it ‘announced it will begin accepting applications for national bank charters from nondepository financial technology (fintech) companies engaged in the business of banking’ on July 31, 2018.

David Zaring, *Modernizing the Bank Charter*, 61 WM. & MARY L. REV. 1397, 1450–51 (2020).

11. See Kathryn Gaw, *P2P and Private Debt: P2P’s USP*, ALT. CREDIT INV. (Oct. 11, 2023), <https://alternativecreditorinvestor.com/2023/10/11/p2p-and-private-debt-p2ps-usp/> [<https://perma.cc/VF4T-PHNNH>] (explaining how “peer-to-peer” investment functions).

often follow precedent, much like the common law regime that licensing is meant to replace.

Moreover, it would reflect the sort of experimentalism that has long been tolerated by the banking charter, which has always been more of a *they* than an *it*. Bank supervisors charter *normal* banks, but have long extended the charter to trust banks,<sup>12</sup> credit card banks,<sup>13</sup> merchant acquirer businesses,<sup>14</sup> and even, in some cases, to fintech nonbanks.<sup>15</sup>

Trust charters alone have been used to get insurance companies, asset managers, and even a private college into at least the trust business of banking. And, on the other side of the coin, trust charters have been used to allow banks to offer services to pension plans that allow banks to compete with mutual funds.<sup>16</sup> The Presidential Working Group and three law professors have suggested that the trust charter could be used to create a regulatory paradigm for ‘stablecoin’ cryptocurrencies.<sup>17</sup> It could even be a way to get some of the most unstable kinds of banks—cryptocurrency exchanges—into the world of supervision and oversight, although, as we will see, this innovation may be too risky to adopt.<sup>18</sup>

The fact that the breach of the regulatory perimeter is not about banks entering commerce—but commerce entering banking—calls a widely held conventional wisdom into question. Far too many scholars and policymakers have suggested that the regulatory perimeter is necessary because banks keep trying to break through it. Former FTC Chair Lina Khan recommended keeping banks out of commerce because the result might be “large financial-industrial conglomerates” with “concentrate[d] political power,” resulting in “too-big-to-fail” firms.<sup>19</sup> Lev Menand has argued that the regulatory perimeter was meant to “preserve political liberty by checking the power and influence of the people who run banks.”<sup>20</sup> Andrew Tuch has argued that the perimeter was created because “popular mistrust of large accumulations of power led politicians to restrict major financial institutions from controlling industrial enterprises.”<sup>21</sup> These scholars think that the problem with the

12. See *infra* Part II.

13. OCC, CREDIT CARD LENDING VERSION 2.0 170 (2021), <https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-handbook/files/credit-card-lending/pub-ch-credit-card.pdf>.

14. See *Merchant Acquirers*, GA. DEPT. BANKING & FIN., <https://dbf.georgia.gov/merchant-acquirer-limited-purpose-banks-malpb> [ <https://perma.cc/UJ6E-SMTR>] (The law “was created to allow entities engaged in merchant acquiring or settlement activities to directly access payment card networks.”). For a discussion, see Peter T. Luce, *Georgia’s New Merchant Acquirer Bank Charter: ‘Wait and See’*, DAVID WRIGHT TREMAINE (Dec. 12, 2012), <https://www.dwt.com/blogs/financial-services-law-advisor/2012/12/georgias-new-merchant-acquirer-bank-charter--wait> [ <https://perma.cc/ABM6-7VFX>] (“The new law was intended to permit non-bank payment processors to more effectively compete with large financial institutions that also offer payment card processing services to merchants.”). The important banking service provider, Fiserv, has recently applied for the charter. Caitlin Mullen, *Fiserv Seeks Special Purpose Bank Charter*, PAYMENTS DIVE (Jan. 12, 2024), <https://www.paymentsdive.com/news/fiserv-seeks-special-purpose-bank-charter-payments-merchant-acquiring/704520/> [ <https://perma.cc/8GEM-ZC9P>].

15. See *infra* notes 135–36 and accompanying text.

16. See *infra* Part I.F.3.

17. Howell Jackson, Timothy G. Massad & Dan Awrey, *How We Can Regulate Stablecoins Now—Without Congressional Action* 1–2 (Hutchins Ctr., Working Paper No. 76, 2022), <https://www.brookings.edu/research/how-we-can-regulate-stablecoins-now-without-congressional-action>.

18. See *infra* Part II.A.

19. Lina M. Khan, Note, *Amazon’s Antitrust Paradox*, 126 YALE L.J. 710, 795 (2017).

20. Lev Menand, *The Logic and Limits of the Federal Reserve Act*, 40 YALE J. ON REG. 197, 216 (2023).

21. Andrew F. Tuch, *The Remaking of Wall Street*, 7 HARV. BUS. L. REV. 315, 369–70 (2017).

regulatory perimeter is that banks are ignoring it; I will show that the real action lies in commercial firms entering banking.

Nor is the story here consistent with those who exalt the kind of strict perimeter that no longer exists. Lev Menand and Morgan Ricks worried that any relaxation of the regulatory perimeter—and this paper recommends just this sort of relaxation—would mean that banking regulators would essentially federalize corporate law.<sup>22</sup> In their view, the mixing of banking and commerce with a federal charter available to an array of businesses would be a real threat to Delaware-centric corporate law.

The claim here that a relaxed perimeter would be more consistent with the way that financial markets are actually practiced today is more aligned with the views of Joshua Macey and Daniel Awrey.<sup>23</sup> They observed that the “historical rationale for the structural separation of banking and commerce perhaps rings hollow in today’s world in which commercial enterprises can theoretically obtain capital from a wide range of financial markets and institutions—and where no single financial institution enjoys a dominant market position.”<sup>24</sup>

More broadly, the newly blurred borders between commerce and banking allow for an exploration of some of the purposes of a licensing regime, an important part of administrative law that has received little theoretical attention. A charter is nothing more than a license, and a bank charter is a license to engage in the business of banking.

Licensing is undertheorized and often caught in the middle of an unresolvable debate between public interest theorists and public choice theorists. The public interest advocates describe a world where the license is a tool to manage scarcity, to ensure that licensees are qualified to offer a service and to use the licensing condition as an opportunity to enlist licensees in the service of realizing other public values.<sup>25</sup> Public choice views licenses only as tools used to restrict competition and extract rents from the general public.<sup>26</sup> Splitting the difference between these two accounts is not easy. One is very cynical, and the other perhaps naively technocratic—but a presumption that licenses often serve some public purpose—but are capable of being abused—is the right way to think about the practice. Perhaps less obvious is the way that licensing regimes often come to look like the common law regimes they replaced, where precedent is important, and there is a tendency to decide like applications in similar ways.

Finally, in addition to the legal analysis, some modest quantitative research on how tailored chartering decisions are at the federal level can serve as an exercise with practical implications for those interested in thinking about how a well-run licensing regime could be operated, and an opportunity to run the rule over a federal regulator—do all their licenses look the same, or do they reflect bespoke examinations of the quality of the licensee? I will show, through content analysis, that recent chartering decisions by the Office of the Comptroller of the Currency (OCC) can look similar, which is some evidence that adherence to precedent and *stare decisis* is being practiced at that agency.

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22. Lev Menand & Morgan Ricks, *Federal Corporate Law and the Business of Banking*, 88 U. CHI. L. REV. 1361, 1417 (2021) (worrying that a fintech charter would invite “an enormous range of business enterprises into a federal charter”).

23. Dan Awrey & Joshua Macey, *The Promise & Perils of Open Finance*, 40 YALE J. ON REG. 1, 57 (2023).

24. *Id.*

25. *See infra* Part III.A.

26. *See infra* Part III.B.

In Part I, I establish the breakdown of the barriers between banking and commerce. In Part II, I analyze the trust charter—in particular, the fintech trust charter and put it in the context of the history of the ever-changing borders of trust banking; this shows how the license has been used to manage the regulatory perimeter. In Part III, I review the two perspectives on licensing: one that posits it is serving the public interest, and another that posits that licenses are generally bad for the public—a so-called public choice perspective. I then, in Part IV, analyze the current status of this regime with a quantitative and qualitative analysis of recent national banking and trust charter grants. The Article culminates in Part V with a recommendation that chartering be expanded through skinny charters that can re-establish a sensible regulatory perimeter and expand the remit of the federal banking regulators while also increasing competition in banking. A brief conclusion follows.

### I. BREACHING THE REGULATORY PERIMETER

There are four ways into the banking system that are particularly relevant to breaking down the barrier between banking and commerce:

(1) A nonbank offering banking services with a bank partnership. These firms contract around the regulatory perimeter, enter into agreements often called Banking as a Service (BaaS), and could be thought of either entirely traditional customer acquisition models, or as pure regulatory arbitrage. Chime, CashApp, and Revolut are examples—they are fintechs offering banking services in conjunction with a partnership with a small community bank.<sup>27</sup>

(2) Nonbanks doing things that banks used to do without getting a banking license. Rocket Mortgage and other mortgage servicers now underwrite over half of the home mortgages in the United States, and mortgage underwriting used to be a core function of banks.<sup>28</sup> The retail money market fund industry now manages \$2.76 trillion; it was started as a competitor to banks.<sup>29</sup>

(3) A large business trying to offer financial services to existing customers, such as Walmart and PayPal.<sup>30</sup> Their relationship with banking law is similar to the financial technology firm relationship, but the goal of the nonbank is to offer banking services to their commercial clients. These efforts have been tolerated but are the most serious encroachments by commercial firms inside the regulatory perimeter separating banking and commerce.

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27. See Gloria Methri, *Stride Bank Extends Partnership with FinTech Chime*, IBS INTEL. (Jan. 12, 2023), <https://ibsintelligence.com/ibsi-news/stride-bank-extends-partnership-with-fintech-chime> [<https://perma.cc/4X3N-VG42>] (stating that non-bank Chime was founded “on the premise that basic banking services should be helpful, easy, and free”); Tom Wilson & Sinead Cruise, *Revolut Gets UK Banking Licence, Ending Three-Year Wait*, REUTERS (July 25, 2024), <https://www.reuters.com/technology/revolut-gets-uk-banking-licence-2024-07-25/> (on file with the *Journal of Corporation Law*) (describing how Revolut operated for years without a banking license).

28. Bonnie Sinnock, *Nonbanks Made the Majority of Purchase Mortgages in 2021*, NAT’L MORTG. NEWS (June 17, 2022), <https://www.nationalmortgagenews.com/news/nonbanks-made-the-majority-of-purchase-mortgages-in-2021> [<https://perma.cc/EY6C-S3A9>].

29. *Money Market Fund Assets*, INV. CO. INST. (Jan. 30, 2025), <https://www.ici.org/research/stats/mmf/> [<https://perma.cc/S8QP-KFU8>].

30. Baradaran, *supra* note 6, at 1144; *What Bank Does PayPal Use?*, PayCEC (Jan. 2, 2023), <https://www.paycec.com/faq/what-bank-does-paypal-use> [<https://perma.cc/UEV3-WQ5H>].

(4) A fintech that wants the benefits of banking regulation and accordingly obtains an actual banking charter or a stripped-down banking charter. LendingClub, a peer-to-peer lender, merged with a tiny bank in order to get a banking license.<sup>31</sup> SoFi, another such lender, did the same thing.<sup>32</sup> And some fintechs are nothing more than online-only banks—Varo is an example of this.<sup>33</sup>

These four disparate challenges for what counts as banking and what does not nicely illustrate some of the tensions of any licensing regime, which Part III of this Article takes up. The advantages of permitting nonbanks to offer banking services concern access and competition—the root of the public choice critique of any licensing regime, which assumes that the license can restrict such competition. The concerns are twofold. First is that unlicensed banking means that banking services will be offered by unqualified vendors, and because banking is an abnormally dangerous activity, the consequences could be serious. Second, licensing regimes are often established to further other public policy interests, and one of the purposes of the licensing regime in banking is to limit the power of banks.

### A. The Business of Banking

Deposit-taking has long been defined as a critical part of the business of banking. This term was initially defined in the United States under the charter of the Commercial Bank of Albany in 1825.<sup>34</sup> The old New York charter authorized the bank “to carry on the business by . . . receiving deposits.”<sup>35</sup> In 1873, the U.S. Supreme Court defined the term “bank” as one that was “a place for the deposit of money, as that is the most obvious purpose of such an institution.”<sup>36</sup> The definition stuck. In 1963, the Supreme Court noted that a unique feature of banks was that “they alone are permitted by law to accept demand deposits.”<sup>37</sup>

But if deposits make banks distinctive, they would not require much legal attention. It is what banks do with the deposits that make them distinctive, useful, and risky and, therefore, candidates for regulation and activity limitation. Banks take the deposits, promise depositors that they can have the deposits back at any time, and use them to make loans, which frequently can remain outstanding for decades—one of the most common loans in the United States is the 30-year fixed mortgage.<sup>38</sup> As Jonathan Macey has observed, “Economists have found that maturity mismatch causes self-fulfilling panics among bank depos-

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31. Press Release, LendingClub, LendingClub Closes Acquisition of Radius Bancorp (Feb. 1, 2021), <https://ir.lendingclub.com/news/news-details/2021/LendingClub-Closes-Acquisition-of-Radius-Bancorp> [<https://perma.cc/WF8R-3N9V>].

32. Press Release, SoFi Technologies, Inc., SoFi Completes Acquisition of Golden Pacific Bancorp, Inc. (Feb. 2, 2022), <https://www.sofi.com/press/sofi-completes-acquisition-of-gpb> [<https://perma.cc/8W3T-NCGA>].

33. Zaring, *supra* note 10, at 1434–39.

34. 1 KENNETH M. LAPINE ET AL., BANKING LAW § 1.03 (Matthew Bender & Co. ed., 2024).

35. *Id.* (“[T]o carry on the business by discounting bills, notes and other evidences of debt, by receiving deposits; by buying and selling gold and silver bullion and foreign coins; by buying and selling bills of exchange and by issuing bills, notes and other evidences of debt.”).

36. *Oulton v. Savs. Inst.*, 84 U.S. 109, 118–19 (1872).

37. *U.S. v. Phila. Nat’l Bank*, 374 U.S. 321, 326 (1963).

38. Nestor M. Davidson, *Property and Relative Status*, 107 MICH. L. REV. 757, 807 (2009) (noting that “most homeowners tak[e] out standard thirty-year fixed mortgages”).



itors. This happens in the banking context because of the very nature of banks, which engage in maturity transformation, turning short-term liabilities into longer term assets.”<sup>39</sup> That is why the OCC has posited a trinity of bank functions, as opposed to only focusing on deposit-taking: they take deposits, use those deposits to make loans, and facilitate payments between clients.<sup>40</sup>

On the banking side, starting in the 1980s, banks have tried to emerge from the limitations of the Glass-Steagall Act to become more comprehensive entities that combine banking, capital markets services, and other financial services that mirror the so-called “universal banks” of Europe and Japan.<sup>41</sup> Those foreign firms offer their clients banking, fundraising, insurance, and other services, offering the financial “one-stop shopping” that American businesses are increasingly emulating.<sup>42</sup> Financial institutions in the United States do not sell widgets or socks yet (although some sell coffee), but many now offer the full suite of financial services to their clients, ranging from banking to investment advice to insurance—or, at least, insurance products.<sup>43</sup> Some banks have even rebranded themselves as technology companies.<sup>44</sup>

These functional changes have been matched with legal innovations that have upended the definition of what a bank can do. For over a century, banks have been chartered

39. Jonathan Macey, *Error and Regulatory Risk in Financial Institution Regulation*, 25 SUP. CT. ECON. REV. 155, 179 (2017).

40. 12 C.F.R. § 5.20(e)(i) (2020); see OCC, CONSIDERING CHARTER APPLICATIONS FROM FINANCIAL TECHNOLOGY COMPANIES 2 (2018), <https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-licensing-manual/files/pub-considering-charter-apps-from-fin-tech-co.pdf> [<https://perma.cc/CK45-YXQQ>] (stating that special purpose national banks must engage in at least one of the “core banking functions of taking deposits, paying checks, or lending money”).

41. See Charles W. Calomiris, *Universal Banking ‘American-Style’*, 154 J. INSTITUTIONAL & THEORETICAL ECON. 44, 44 (1998) (“American corporate banking has undergone enormous change over the past two decades. That change . . . that led US banks and their regulators to a new American version of global universal banking. From the perspective of the scale and scope of banks, these changes represent a convergence of US banks to international norms in banking.”).

42. See Editorial, *Chase, J.P. Morgan Deal Represents A Step Toward One-Stop Shopping*, WALL ST. J. (Sept. 14, 2000), <https://www.wsj.com/articles/SB968882980680349481> (on file with the *Journal of Corporation Law*) (discussing the trend that more and more American financial institutions evolved into “the financial equivalent of a Wal-Mart store” and provided “one-stop shopping”); see, e.g., Michael Siconolfi, *Travelers and Citicorp to Merge in Megadeal Valued at \$83 Billion*, WALL ST. J. (Apr. 7, 1998), <https://www.wsj.com/articles/SB891818705198998500> (on file with the *Journal of Corporation Law*) (“This merger could also trigger the formal end of legislation that prevents full-fledged unions among insurance companies, banks and brokerage firms. Indeed, the plan is based on the assumption that Congress will dismantle the Depression-era law that separated the banking and brokerage industries.”).

43. Banks have found the offering of insurance products to be more attractive than the purchase of insurance firms. Brian Ambrosia, *Why Banks Are Divesting Insurance Brokerages*, BANK DIR. (Aug. 18, 2023), <https://www.bankdirector.com/article/why-banks-are-divesting-insurance-brokerages/> [<https://perma.cc/P4MS-3WSN>] (“For the first time in nearly two decades, announced divestitures of bank-owned insurance brokerages have outpaced announced acquisitions.” (emphasis omitted)).

44. See, e.g., Emily McCormick, *BofA CEO on Future of Banking: ‘We’re Clearly a Technology Company’*, YAHOO FIN. (Oct. 26, 2021), <https://finance.yahoo.com/news/bof-a-ceo-on-future-of-banking-were-clearly-a-technology-company-144208908.html> (on file with the *Journal of Corporation Law*) (“We’re clearly a technology company, [Bank of America CEO] Moynihan said.” (internal quotations omitted)).

either by the federal government or the states, and limited, at least in theory, to the “business of banking,” understood to be a combination of taking deposits, making loans, and processing payments.<sup>45</sup>

But now, both the states and the federal government are exploring new sorts of charters. The federal government has offered a special charter to financial technology firms.<sup>46</sup> New York and Wyoming have rushed to do something similar.<sup>47</sup> The cryptocurrency industry has asked for a special charter for so-called “stablecoins,” cryptocurrencies whose value is tethered to the value of a dollar, gold, or some other underlying asset.<sup>48</sup> One of the most recent heads of the OCC, the regulator of national banks, has mused about splitting up the banking charter still further, into slimmed-down licenses for payments processors, lenders, and, if necessary, deposit takers.<sup>49</sup>

All of this might suggest a dynamic where powerful and risky banks are straining at the limits that modern regulators are increasingly finding hard to maintain. But when it comes to the separation of banking and commerce, the proverbial call is coming from outside, rather than inside, the house.

### B. The Entry of Commercial Firms into Banking

Our first tour into the blurring of the regulatory perimeter takes us to the increasing number of commercial firms that are offering their clients banking services. This Article starts with Walmart, the nonbank, which is becoming one of the largest providers of financial services in the country.<sup>50</sup> Then it considers the example of PayPal—a financial firm and established fintech that has become one of the largest providers of payment services to consumers in the world.<sup>51</sup> Both firms are increasingly close to offering the full suite of

45. 12 C.F.R. § 5.20 (2020).

46. See News Release, OCC, OCC Begins Accepting National Bank Charter Applications from Financial Technology Companies (July 31, 2018), <https://www.occ.gov/news-issuances/news-releases/2018/nr-occ-2018-74.html> [<https://perma.cc/R2J5-U52R>] (The “OCC today announced it will begin accepting applications for national bank charters from nondepository financial technology (fintech) companies engaged in the business of banking.”).

47. See William E. Stern & Alexander J. Callen, *ILCs Are Back on the Table for Fintechs Seeking Banking Charters*, GOODWIN (May 7, 2020), [https://www.goodwinlaw.com/publications/2020/05/05\\_07-fintech-flash\\_ils-are-back-on-the-table](https://www.goodwinlaw.com/publications/2020/05/05_07-fintech-flash_ils-are-back-on-the-table) [<https://perma.cc/RX4V-Y7TQ>] (stating that states like Utah are granting industrial loan company (ILC) charters to fintech companies to allow them make loans, accept certain types of deposits, and therefore operate like banks).

48. See John Adams, *Crypto Firm Circle Eyes Bank Charter to Bolster Stablecoin Venture*, AM. BANKER (Aug. 9, 2021), <https://www.americanbanker.com/news/crypto-firm-circle-eyes-bank-charter-to-bolster-stablecoin-venture> (on file with Author) (stating that crypto firm Circle, which “is best known for its U.S. Dollar Coin, or USDC,” intends to become a “national digital currency bank”).

49. See Jason Brett, *hCC Chief Brian Brooks Says Payments Charter Is Ready, More Crypto Banks Coming Soon*, FORBES (Nov. 17, 2020), <https://www.forbes.com/sites/jasonbrett/2020/11/17/exclusive-occ-chief-brian-brooks-says-payments-charter-is-ready-more-crypto-banks-coming-soon/?sh=5470cb0b2626> (on file with the *Journal of Corporation Law*) (discussing rationales of pushing for new charters like “Payment Charter”); see also Victoria Guida, *Top Regulator Pushes Ahead With Plan To Reshape Banking, Sparking Clash With States*, POLITICO (Aug. 31, 2020), <https://www.politico.com/news/2020/08/31/currency-comptroller-reshape-banking-406393> [<https://perma.cc/9MCK-VYRF>] (“A federal regulator is moving to offer national charters to companies that provide payments services, escalating a battle with states over whether businesses that don’t take deposits should be given national bank status.”).

50. Birch, *supra* note 5.

51. *What Bank Does PayPal Use?*, *supra* note 30.

financial services to their customers—Walmart is about to develop a loan program, which is usually the last of the three core banking services offered by a nonbank.<sup>52</sup>

In both of these cases, the question of legality—nonbanks are not permitted to operate as banks without a license from the banking regulators<sup>53</sup>—turns on the relationship between the commercial business and the financial institution that touches the money. If the relationship is one of customer acquisition—the commercial firm brings clients to the financial institution—then the separation of banking and commerce has been preserved to a degree. If the relationship is something different from that, however, then the question becomes more fraught.

But regardless of the contractual nature of the relationship, there is no question that the business of banking is now being facilitated by nonbanks. Firms that epitomize commerce, like Amazon and Walmart, offer their customers credit cards, take deposits, and make payments—the sort of activities that banks, and only banks, were permitted to do.<sup>54</sup> Technology firms have been particularly aggressive offerors of financial services, creating wallets for their customers, building out payment systems, and making loans or holding assets in custody, often for an interest payment.<sup>55</sup> Apple’s and Google’s payment services exemplify the development.

### 1. Walmart Returns to Banking

Only 15 years after Walmart’s effort to charter its own financial institution failed in high-profile controversy and strong opposition from the banking industry, the retailer has hired executives away from Goldman Sachs’s consumer bank, and put MoneyCenters in most of its stores, which it describes as “your one-stop shop for financial services.”<sup>56</sup> The everything store, a nonbank, holds 18.7% of the market of consumer checking accounts.<sup>57</sup>

Walmart tried to offer banking services before. It tried to open its own quasi-bank, an industrial loan company.<sup>58</sup> It was not permitted to do so (it withdrew its application for deposit insurance for an industrial loan corporation it had created as a subsidiary in 2007), but since then has become one of the leading providers of financial services to American

52. *Buy Now, Pay Over Time*, WALMART, walmart.com/cp/one-loans/6982710 [https://perma.cc/73N2-BQ8F].

53. *How Can I Start a Bank?*, BD. GOVERNORS FED. RSRV. SYS., https://www.federalreserve.gov/faqs/banking\_12779.htm [https://perma.cc/VE2Z-AW26].

54. See Anna Irrera & Iain Withers, *Focus: Banks Beware, Amazon and Walmart are Cracking the Code for Finance*, REUTERS (Sept. 17, 2021), https://www.reuters.com/business/finance/banks-beware-outsiders-are-cracking-code-finance-2021-09-17/ (on file with the *Journal of Corporation Law*) (“Global brands from Mercedes and Amazon [] to IKEA and Walmart [] are cutting out the traditional financial middleman and plugging in software from tech startups to offer customers everything from banking and credit to insurance.”).

55. Gregory Barber, *Every Tech Company Wants to Be a Bank—Someday, at Least*, WIRED (Nov. 16, 2019), https://www.wired.com/story/tech-companies-banks/ [https://perma.cc/94QK-QAYM] (quoting Gerard du Toit, a Bain banking consultant, that tech companies “clearly intend for world domination, and there’s no doubt financial services are a part of that”).

56. *Walmart Money Services*, WALMART, https://www.walmart.com/cp/walmart-moneycenter/5433 (on file with the *Journal of Corporation Law*).

57. Birch, *supra* note 5.

58. Baradaran, *supra* note 6, at 1144.

consumers.<sup>59</sup> This curious development—15 years after being told it could not enter the business of banking it now provides banking services to over 100 million people—calls for an inquiry about how the regulatory perimeter works, or if it does at all. Although Walmart does not report revenue from financial services, except to report in its 2018 Form 10K that it amounted to less than 1% of its revenue—something it no longer says on those forms.<sup>60</sup> The company’s 10Ks mentioned financial service 15 times in 2023<sup>61</sup> and 12 times in 2022,<sup>62</sup> up from 1 in 2012.<sup>63</sup>

Walmart’s entry has been facilitated by bank partnerships—it borrows various financial institution charters to offer financial services through contracts with financial firms.<sup>64</sup> The question with these rent-a-bank relationships between banking and commerce is whether the commerce parent is a customer acquisition channel for the bank, in which case it is little different from a branded credit card, like one for the Philadelphia Eagles or Nordstrom.<sup>65</sup> Alternatively, the bank could be covering for its much bigger commercial partner’s entry into finance—Walmart is one of the largest companies in the world, and the financial firms it partners with are tiny. Its largest position in the market in consumer checking accounts<sup>66</sup> amounts to over 108 million active accounts.<sup>67</sup> This success in the financial sector is made possible through partnerships with ‘neobanks,’ the term I will use to deal with startups and new partnerships with community banks, and the use of rent-a-banking. One interesting feature of Walmart’s entry into financial services is that it is quite a bit more traditional than the online-only services offered by other commercial firms. Shoe leather banking is on offer at Walmart, through its in-store MoneyCenters, placed in over 4600 Walmarts across the country,<sup>68</sup> customers are able to access many of the basic services provided by standard banks.

Of the three major functions of banks—taking deposits, facilitating payments, and making loans—Walmart currently does the first two and has plans to begin offering loans in the near future through its partnership with One. It is through One that Walmart hopes

59. For a discussion, see Saule T. Omarova & Margaret E. Tahyar, *That Which We Call a Bank: Revisiting the History of Bank Holding Company Regulation in the United States*, 31 REV. BANKING & FIN. L. 113, 168 (2011).

60. Walmart Inc., Annual Report (Form 10-K) 9 (Mar. 3, 2018).

61. Walmart Inc., Annual Report (Form 10-K) (Mar. 17, 2023).

62. Walmart Inc., Annual Report (Form 10-K) (Mar. 18, 2022).

63. Walmart Inc., Annual Report (Form 10-K) (Mar. 27, 2012).

64. See, e.g., Dee-Ann Durbin, *Walmart has Ended its Partnership with Capital One. Here’s What it Means for Cardholders*, AP NEWS (Mar. 25, 2024), <https://apnews.com/article/walmart-capital-one-credit-cards-ca5b7fd458da902b7c6ccf96e74a8605> [<https://perma.cc/EFU5-WL7Q>] (detailing consequences for the ending of one of these relationships).

65. Although many sports teams offer branded credit cards to fans, the most common such card are those affiliated with retailers—the largest branded credit card is offered by Costco. See CO-BRANDED CREDIT CARDS IN THE US, FREEDONIA GRP. (10th ed. 2025).

66. Birch, *supra* note 5 (Walmart holds 18.7% of the market share of consumer checking accounts).

67. Ray Birch, *Walmart Approaching 109 Million Checking Accounts*, CU TODAY (Jan. 16, 2023), <https://www.cutoday.info/site/THE-feature/Walmart-Approaching-109-Million-Checking-Accounts> [<https://perma.cc/N55C-LKGA>] (“Members of the Big Checking fraternity range from Walmart at no. 1 in transaction accounts.” These 108 million accounts account for 19% of the national market.)

68. Penelope Wang, *Is Banking at Walmart Worth It?*, CONSUMER REPS. (Aug. 2, 2022), <https://www.consumerreports.org/banks/is-banking-at-walmart-worth-it-a3165612052/> [<https://perma.cc/YPN6-SVQK>] (discussing Walmart’s more than 4600 in-store MoneyCenters).

to realize its goal to help its customers “[s]ave, spend, & grow your money—all in one place.”<sup>69</sup>

Deposits at Walmart are made possible through its partnerships with Green Dot Bank, the world’s largest prepaid debit card company (which does not make it very large), and a successful fintech startup.<sup>70</sup> These partnerships are often called Banking as a Service (BaaS). BaaS is a business model where traditional banks or licensed financial institutions provide their infrastructure, regulatory compliance, and services—such as payment processing, account management, or lending—through APIs to non-bank businesses. It enables companies like fintechs, retailers, or other enterprises to integrate financial products into their platforms, offering banking services under their own brand without needing a banking license.

Customers are able to open an account with Green Dot at any Walmart MoneyCenter, and can do so online.<sup>71</sup> Walmart and Green Dot have offered to convert the prepaid debit cards to demand deposit accounts—one of the core features of banks.<sup>72</sup> The partnership was very important to Green Dot; it provided 21% of the revenue of Green Dot, \$304.4 million, in 2022.<sup>73</sup> GreenDot, moreover, is one of the larger BaaS banks; many are tiny community banks with little sophistication.

Prepaid debit cards—an important entry point into the financial system for a working-class customer population that sometimes struggles with credit scores—can also be obtained at any MoneyCenter through Green Dot, and Walmart offers other services for those who partake, including cashback on Walmart products, early direct deposit up to two days early, free family debit accounts, and optional overdraft protection.<sup>74</sup>

But prepaid debit cards largely help customers make payments. The next step in banking services, particularly for underbanked working-class consumers, is access to credit, and Walmart, once again, is there to help its customers. Credit cards are now available to Walmart customers through a partnership with Capital One.<sup>75</sup> With the Capital One Rewards Mastercard, Walmart customers received 2% back on in-store purchases, and 5% back online.<sup>76</sup>

69. See *Walmart Money Services*, *supra* note 56.

70. Gabrielle Saulsbery, *Green Dot Execs Mised Shareholders About Declining Business, Lawsuit Says*, YAHOO FIN. (July 17, 2024), <https://finance.yahoo.com/news/green-dot-execs-mised-shareholders-165236080.html?guccounter=1> [<https://perma.cc/MP5B-4RVX>].

71. *How Do I Get a Walmart MoneyCard Account?*, WALMART MONEYCARD, <https://www.walmart-moneycard.com/helpcenter/getting-started/how-to-get-a-card/how-do-i-get-a-walmart-moneycard-account> [<https://perma.cc/WS9V-VLMU>] (“You can order a Walmart MoneyCard online for free here.”).

72. Tatiana Walk-Morris, *Walmart, Green Dot Switch MoneyCard to Demand Deposit Account*, BANKING DIVE (June 28, 2021), <https://www.bankingdive.com/news/walmart-green-dot-switch-moneycard-to-demand-deposit-account/602516/> [<https://perma.cc/WEJ7-CJ5R>] (“Walmart and the fintech Green Dot said Thursday the retailer’s MoneyCard is now offered as a demand deposit account, according to a press release.”).

73. Green Dot Corp., Annual Report (Form 10-K) 3 (Feb. 27, 2023).

74. Payne, *supra* note 5 (“Other features include early direct deposit up to two days early, free family debit accounts, and optional overdraft protection.”).

75. Press Release, Capital One, Capital One and Walmart Reimagine the Retail Credit Card Program (Sept. 18, 2019), <https://investor.capitalone.com/news-releases/news-release-details/capital-one-and-walmart-reimagine-retail-credit-card-program> [<https://perma.cc/6W36-JQY5>].

76. *Id.*; but see *Capital One Walmart Rewards® Card*, CAPITAL ONE, <https://www.capitalone.com/credit-cards/walmart-rewards/> [<https://perma.cc/H93Z-6XCG>] (discussing the end of the partnership).

Other banking services can also be obtained at MoneyCenters, including international and domestic money transfers, and bill payments through partnerships with Western Union, MoneyGram, and Ria.<sup>77</sup> During tax season, Walmart has also offered in-store popup tax preparation centers, supported by tax preparer Jackson Hewitt.<sup>78</sup> It has made noises about offering investment services to its customers as well—again, the goal is to make the MoneyCenter a financial supermarket.<sup>79</sup>

As extensive as they are, Walmart’s CEO characterized its current financial service offerings as mostly analog, saying, “the opportunity to make it digital is right there in front of us.”<sup>80</sup> To make this transition possible, Walmart has created One, a fintech start-up; here the supporting ‘rent-a-bank’ is the relatively new startup Coastal Community Bank.<sup>81</sup> One will offer debit cards and deposit accounts.<sup>82</sup> Eventually, Walmart hopes to expand One’s services and offer customers loans, fulfilling all three of the major functions of a bank.<sup>83</sup> The company has hired two senior bankers with Goldman Sachs to oversee the rollout of its suite of financial services.<sup>84</sup> America’s most commercial firm is providing almost all the main services you might expect a bank to provide.

## 2. PayPal and Service Tying

Financial technology firms, or fintechs, have also made inroads into the banking franchise. In many cases, fintechs integrate a traditional commercial bank’s infrastructure with the technology of a neobank through the BaaS model.<sup>85</sup> Through such a model, banks effectively license their charters, offering regulated infrastructure and, depending on the structure of the relationship, even deposit insurance, to a neobank that is looking to offer novel financial products—or reach a novel consumer base.<sup>86</sup>

77. *Money Transfers*, WALMART, [https://www.walmart.com/cp/online-money-transfers/1089406?povid=OMNISRV\\_D\\_Cp\\_MS\\_CheckCashing\\_632047\\_MS\\_1089406\\_TileCardsIcon\\_RelatedFinancialServices\\_MoneyTransfers\\_1332399668](https://www.walmart.com/cp/online-money-transfers/1089406?povid=OMNISRV_D_Cp_MS_CheckCashing_632047_MS_1089406_TileCardsIcon_RelatedFinancialServices_MoneyTransfers_1332399668) [https://perma.cc/XP3H-CUTV] (listing them as “[o]ur partners”).

78. *Tax Time Made Easy at Walmart*, WALMART, <https://www.walmart.com/cp/tax-prep-services/1091305> [https://perma.cc/NN5S-JADN].

79. *Walmart Money Services*, *supra* note 56 and accompanying text.

80. Jennifer Surane & Brendan Case, *Milk, Diapers and Checking Accounts: Banking Comes to Walmart*, BLOOMBERG (Sept. 14, 2022), <https://www.bloomberg.com/news/articles/2022-09-14/walmart-backed-startup-one-to-offer-bank-accounts-to-shoppers-workers#xj4y7vzkg> (on file with the *Journal of Corporation Law*) (“We’ve got a pretty big financial services business, but I would characterize it as being analog, and the opportunity to make it digital is right there in front of us, Walmart Chief Executive Officer Doug McMillon said last year at an investor conference.” (internal quotations omitted)).

81. *Id.*

82. *Id.*

83. *Id.*

84. Sridhar Natarajan, *Walmart Lures Goldman Bankers in Bid to Fight Wall Street*, BLOOMBERG (Feb. 28, 2021), <https://www.bloomberg.com/news/articles/2021-02-28/goldman-s-consumer-chief-ismail-makes-surprise-exit-for-fintech> (on file with the *Journal of Corporation Law*).

85. CCG CATALYST, *BANKING-AS-A-SERVICE: NAVIGATING A NEW FRONTIER* 3 (2021), <https://www.ccg-catalyst.com/thought-leadership/research/banking-as-a-service-navigating-a-new-frontier/> [https://perma.cc/M6CD-ZLM6] (“BaaS, [which] centers on this kind of partnership, by which a regulated bank provides its charter to a nonregulated brand, enabling the latter to offer financial services to their customers.”).

86. *Id.* at 5.

When a traditional commercial bank partners with any nonbank entity to enhance or outsource bank activities and functions, the bank opens itself up to additional risks.<sup>87</sup> Neobanks lack federal or state bank charters, oversight, and supervision to take customer deposits and originate loans, among other activities.<sup>88</sup> Traditional commercial banks, in contrast, may collect deposits and issue loans because of their licensure under state or federal charters.<sup>89</sup> How then can neobanks, such as Chime and Cash App, advertise savings and checking accounts to customers?<sup>90</sup> The answer lies in BaaS and their silent partners: regional commercial banks and community banks that facilitate the provision of financial services on behalf of a neobank. For example, Chime has partnered with Bancorp Bank and Stride Bank to provide banking services like consumer deposits and small loans to its customers.<sup>91</sup>

PayPal is another company that makes use of the modern rent-a-banking scheme. Through partnerships with two banks—Bancorp Bank and Synchrony Bank—PayPal offers debit cards, prepaid cards, credit cards, and lines of credit.<sup>92</sup> PayPal itself has a number of state money transmitter licenses and works with rent-a-banks to offer the other services, but the idea is pretty clear—it wants to offer all the services of a bank (and more, like investing and trading in crypto), without actually being a bank.<sup>93</sup>

PayPal is big, too. It processed \$936 billion in payments in FY2020, and earned \$21.45 billion, and it is growing, with 72.7 million new active accounts.<sup>94</sup>

PayPal, as a matter of first impression, is a payment company. But through its payments channel, it has induced a large customer base to leave money with the firm through PayPal Balance (Formerly PayPal Cash and Cash Plus Accounts).<sup>95</sup> These two cash balance (i.e., prepaid debit) accounts let you send money from your PayPal balance or hold money; PayPal Cash Plus gets you a MasterCard and lets you direct deposit your paycheck

87. *Id.* at 3.

88. Stephanie Walden, *What is a Neobank?*, FORBES ADVISOR (June 24, 2021), <https://www.forbes.com/advisor/banking/what-is-a-neobank/> [<https://perma.cc/P56J-5YE3>].

89. *Id.*

90. *Id.*; *Save For Your Goals, Your Way*, CASH APP, <https://cash.app/savings> [<https://perma.cc/LUD8-9SF2>].

91. Gloria Methri, *Stride Bank Extends Partnership with FinTech Chime*, IBS INTEL. (Jan. 12, 2023), <https://ibsintelligence.com/ibsi-news/stride-bank-extends-partnership-with-fintech-chime> [<https://perma.cc/EAR6-VBZW>] (explaining that the partnership enables Chime to offer its members innovative, easy-to-use, and fully regulated products with the same important consumer protections that are in place for traditional bank customers, including FDIC insurance).

92. *What Bank Does PayPal Use?*, *supra* note 30 (detailing that although PayPal is not a bank, it collaborates with banks such as The Bancorp Bank and Synchrony Bank to provide products such as debit cards, prepaid cards, credit cards, and lines of credit).

93. *State Licenses*, PAYPAL, <https://www.paypal.com/us/webapps/mpp/licenses> [<https://perma.cc/32PH-Y674>].

94. Press Release, PayPal, *PayPal Fourth Quarter and Full Year 2020 Results* (Feb. 3, 2021), <https://investor.pypl.com/news-and-events/news-details/2021/PayPal-Reports-Fourth-Quarter-and-Full-Year-2020-Results/default.aspx> (on file with the *Journal of Corporation Law*).

95. Kate Rooney, *PayPal is Exploring a Stock-Trading Platform for U.S. Customers*, CNBC (Aug. 30, 2021), <https://www.cnbc.com/2021/08/30/paypal-is-looking-to-launch-a-stock-trading-platform-for-its-customers.html> [<https://perma.cc/8BKX-MCXP>]; Adam Rozsa, *PayPal Balance Account (Formerly PayPal Cash & Cash Plus Account) – Fees and Features*, WISE (Mar. 27, 2023), <https://wise.com/us/blog/paypal-cash-account> [<https://perma.cc/W7XU-YH3X>].

in the Cash Plus account.<sup>96</sup> PayPal also offers a buy now pay later service called “Pay in 4,” where you use PayPal to pay for a purchase in four installments with one payment every two weeks.<sup>97</sup> These installment payments are interest-free and do not affect your credit score.

You cannot do all your banking at PayPal—it doesn’t offer paper checks, auto loans, home mortgages, home equity lines of credit, or wealth management, but it does offer stock trading and cryptocurrency services.<sup>98</sup>

PayPal and Walmart are just two of the many non-financial institutions that are taking advantage of rent-a-banking to offer financial services to customers. It is estimated that there are around 42 current banks that do rent-a-banking, with this number projected to rise to above 100 by 2030, according to CCG Consulting.<sup>99</sup> These banks exist to work with commercial firms to offer financial services; once again, if the commercial firm is simply scouting customers for the bank, then the separation of banking and commerce has been preserved, for good or ill. But if the rent-a-banks are allowing for entryism not banking by large nonbanks partnering with tiny community banks, then the question is whether we should simply want the separation between banking and commerce to go away.

### C. Big Commerce Lends Money

In addition, financially motivated nonbanks, such as mortgage service providers and money market funds occupy an increasingly prominent role in the national banking system. Half of the deposits of the banks that failed during the 2023 banking crisis ended up in money market funds.<sup>100</sup> Non-bank mortgage providers account for over half the mortgages now issued in the United States.<sup>101</sup> These institutions are increasingly doing what banks used to do, and yet they are not regulated like banks. There has been a great deal of controversy over whether they should be similarly regulated, and whether they serve as a useful competitive source of discipline to the banking industry.<sup>102</sup>

96. Rozsa, *supra* note 95.

97. *Buy Now, Pay Later With PayPal*, PAYPAL, <https://www.paypal.com/us/digital-wallet/ways-to-pay/buy-now-pay-later> [<https://perma.cc/MJ8F-5VTH>].

98. Rooney, *supra* note 95 (detailing after rolling out the ability to trade cryptocurrencies last year, the payments giant has been exploring ways to let users trade individual stocks).

99. Lisa Joyce, *More Banks Eye Rent-a-Charter Business Model for Fintechs & Neobanks*, THE FIN. BRAND (2023), <https://thefinancialbrand.com/news/banking-as-a-service/banks-eye-rent-a-charter-baas-model-for-fintechs-neobanks-120576/> [<https://perma.cc/8H49-G53N>] (“CCG Consulting predicts that the number of financial institutions partnering with nonbanks will more than double by 2030.”).

100. Filip De Mott, *People Have Moved \$500 Billion into Money-Market Funds and Major Banks Since SVB Imploded. JPMorgan Offers 3 Reasons Why the Shift will Continue*, YAHOO! FIN. (Mar. 22, 2023), <https://ca.finance.yahoo.com/news/people-moved-500-billion-money-174601489.html> [<https://perma.cc/ZE8K-2AN5>] (“Vulnerable US lenders have lost around \$500 billion since Silicon Valley Bank collapsed, as depositors took their money out in search of safer havens, such as money-market funds and bigger banks.”).

101. Orla McCaffrey, *Nonbank Lenders Are Dominating the Mortgage Market*, WALL ST. J. (June 22, 2021), <https://www.wsj.com/articles/nonbank-lenders-are-dominating-the-mortgage-market-11624367460> (on file with the *Journal of Corporation Law*) (stating that nonbanks issued more than two-thirds of mortgages in 2020, their highest market share on record).

102. *See, e.g.*, FIN. STABILITY OVERSIGHT COUNCIL, REPORT ON NONBANK MORTGAGE SERVICING 43 (2024), <https://home.treasury.gov/system/files/261/FSOC-2024-Nonbank-Mortgage-Servicing-Report.pdf> [<https://perma.cc/DZ44-M2KS>] (discussing proposed regulations for the industry).



Nonbanks have also begun to outcompete banks for market share in other traditional banking services like asset management and mortgage underwriting that have traditionally been performed by large banks.<sup>103</sup> Consider money market funds, nonbank home mortgage originators and servicers, and private lenders. Money market funds, which were started as competitors to banks,<sup>104</sup> is a problematic but enormous alternative to them. Home mortgage lending—such a traditional service of banks that the most famous film about (among other things) banks, *It's a Wonderful Life*, stars a banker who makes home loans—is now mostly done by nonbanks.<sup>105</sup> And something similar is beginning to happen in commercial lending.<sup>106</sup>

The oldest—though not too old—form of these nonbanks displacing core banking functions—is the money market mutual fund industry. That industry was created out of regulatory arbitrage—banks at the time were obligated to pay fixed interest rates on their deposits, and money market funds, because they did not hold banking charters, were not.<sup>107</sup> They nonetheless offered most of the services of banks to their customers.<sup>108</sup> As with bank deposits, money market deposits could be withdrawn at any time—“on demand.”<sup>109</sup> Money market funds offered their customers checking-like services called NOW accounts.<sup>110</sup>

As banks do, money market funds would use these deposits to lend out to others—mostly very short-duration loans, like commercial paper and short-term sovereign debt.<sup>111</sup> The idea was that these investments would be safe because they were so short-term—a corporation large enough to issue commercial paper would probably be around in 3 months

103. See Courtney Degen, *Asset Managers Worried About Increased Federal Oversight of Nonbanks*, PENSIONS & INVS. (Nov. 23, 2023), <https://www.pionline.com/regulation/asset-managers-worried-about-increased-federal-oversight-nonbanks> [<https://perma.cc/S5BW-HCQV>] (discussing nonbank industry reaction to proposed regulation); Ian Walsh, *Two Types of Underwriting*, SCOTSMAN GUIDE (Oct. 2019), <https://www.scotsmanguide.com/residential/two-types-of-underwriting/> [<https://perma.cc/VY76-TE25>] (discussing difference in approach between bank and nonbank underwriters).

104. John H. Cochrane, *Challenges for Cost-Benefit Analysis of Financial Regulation*, 43 J. LEGAL STUD. S63, S83 (2014).

105. For a very in-depth discussion, see Jay Y. Rubin, *It's A Wonderful Life—or Used to Be*, PA. LAW., Dec. 18, 1996, at 28 (discussing life in small town America).

106. McCaffrey, *supra* note 101.

107. Money market funds were an invention of regulatory arbitrage. Regulation Q of the now nostalgically remembered Glass-Steagall regulatory system limited the interest rates that banks could pay, with the explicitly stated goal of maintaining the profitability of banks and reducing competition for deposits. When inflation demanded higher interest rates, money market funds developed to evade the interest rate restriction. Cochrane, *supra* note 104, at S83.

108. *Taking a Look at Money Market Funds*, FINRA (Apr. 9, 2024), <https://www.finra.org/investors/insights/money-market-funds> [<https://perma.cc/3UQ9-8LF8>].

109. *Id.*

110. For a discussion, see William P. Rogers & James N. Benedict, *Money Market Fund Management Fees: How Much is Too Much?*, 57 N.Y.U. L. REV. 1059, 1121 (1982) (discussing money market funds and NOW accounts).

111. Jonathan Macey, *Reducing Systemic Risk: The Role of Money Market Mutual Funds as Substitutes for Federally Insured Bank Deposits*, 17 STAN. J.L. BUS. & FIN. 131, 135 (2011) (noting that money market funds maintain their value “by keeping their risk exposures low and by buying short-term debt securities from issuers whose financial strength makes them highly unlikely to default prior to the date on which the securities mature”).

when that commercial paper became due.<sup>112</sup> The United States has, famously, never defaulted on its debt.<sup>113</sup> The industry, started in the United States in 1972, now has over \$5 trillion of assets under management.<sup>114</sup> This greatly exceeds the amount of mutual funds and deposits under bank management, although, as we will see, banks now have their own version of money market funds that can compete with the industry.<sup>115</sup> These funds directly compete with bank deposits, and consumers often shift their money away from bank deposits and towards money market funds as a safe haven when the banking industry is in crisis.<sup>116</sup>

Money market funds have thus entered the business of banking, albeit in a rather problematic way—they have been bailed out twice by the government in the last fifteen years, and still haven't been adequately regulated by the SEC.<sup>117</sup> Sometimes it is good to introduce competition in financial services, and the development of money market funds has certainly done so—they are a specialized kind of bank that offers demand deposits and invests those deposits in pretty liquid loans.<sup>118</sup>

Since the financial crisis, non-banks have also increasingly outcompeted banks in performing mortgage underwriting services, once a core function of traditional banks.<sup>119</sup>

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112. *See id.* (discussing how this safety makes the investment attractive to long-term investors).

113. CARMEN M. REINHART & KENNETH S. ROGOFF, *THIS TIME IS DIFFERENT: EIGHT CENTURIES OF FINANCIAL FOLLY* 44 (2009) (noting that the United States is a “default virgin at least in the narrow sense that they have never outright failed to meet their external debt repayment obligations or rescheduled on even one occasion” (internal quotations omitted)).

114. *See* ANTOINE BOUVERET, ANTOINE MARTIN & PATRICK E. MCCABE, *MONEY MARKET FUND VULNERABILITIES: A GLOBAL PERSPECTIVE* 2–4 (2022), [https://www.newyorkfed.org/medialibrary/media/research/staff\\_reports/sr1009.pdf?sc\\_lang=en](https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr1009.pdf?sc_lang=en) [<https://perma.cc/W7H7-6A2C>] (discussing the origins of money market funds in the United States).

115. *See id.* at 3.

116. *See* John Mccrank, *U.S. Money Market Fund Assets Hit Record Highs Despite Debt-Ceiling Fears*, *REUTERS* (May 23, 2023), <https://www.reuters.com/markets/us/us-money-market-fund-assets-hit-record-highs-despite-debt-ceiling-fears-2023-05-24/> (on file with the *Journal of Corporation Law*) (noting that “[a]lthough money market funds are considered safe havens, they have experienced runs during previous crises and government officials and ratings agencies have warned they may continue to be vulnerable to rapid redemptions in times of stress”).

117. *Id.*

118. Macey, *supra* note 111, at 135.

119. *See* Kathryn Fritzdixon, *Bank and Nonbank Lending over the Past 70 Years*, 13 *FDIC Q.*, no. 4, 2019, at 31, 32, <https://www.fdic.gov/system/files/2024-07/fdic-v13n4-3q2019.pdf> [<https://perma.cc/89WX-UKNS>] (“The shifts in bank lending also reflect the growth of nonbank loan holders, primarily in the mortgage market. GSEs hold an increasing share of residential mortgages.”).

Rocket Mortgage and other mortgage servicers now underwrite over half of the home mortgages in the United States.<sup>120</sup> These nonbanks, regulated by the CFPB,<sup>121</sup> face less stringent capital requirements than traditional banks, which has prompted criticism from the banking industry as well as lawmakers.<sup>122</sup>

Is the turn away from bank-led mortgage origination good? It certainly increases competition for financial services, and one can always hope that competition will lead to lower prices and more innovation, as new entrants try to distinguish themselves to win market share. As with neobanks (this Article’s term for fintechs or novel partnerships pursued by large commercial firms), mortgage lenders have been able to use their lighter regulatory touch to try out some customer-facing innovations that have certainly been popular. Some have argued the non-bank boom has been driven largely by technological innovations by non-banks in the mortgage industry and has had a positive impact on consumers.<sup>123</sup> Others contend that the non-bank boom is a result of the financial crisis prompting banks to begin refusing to extend mortgage credit to borrowers with poor credit scores,<sup>124</sup> as well as non-banks evading regulations and engaging in risky behavior.<sup>125</sup> But the larger point is that this most traditional area of bank lending is largely being done by someone else now—again, raising questions about the regulatory perimeter, and even the point of the idea of the separation of banking and commerce.

Finally, private lending has also increased exponentially. In its April 2023 Global Financial Stability Report, the IMF devoted a chapter to nonbanks engaged in finance.<sup>126</sup> It observed that “private credit has grown rapidly over the last decade, surpassing the size of

120. Sinnock, *supra* note 28; see Brad Finkelstein, *Nonbanks Dominate Top 2021 Mortgage Lender List*, NAT’L MORTG. NEWS (Mar. 28, 2022), <https://www.nationalmortgagenews.com/list/nonbanks-dominate-top-2021-mortgage-lender-list> [<https://perma.cc/8Q6G-9T5G>] (noting that non-bank mortgage loan provider Rocket Mortgage was the largest lender of home mortgage loans in 2021).

121. See Marshall Lux & Robert Greene, *What’s Behind the Non-Bank Mortgage Boom?* 1, 9 (Harv. Mossavar-Rahmani Ctr. for Bus. & Gov’t, Working Paper No. 42, 2015), [https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/working\\_papers/42\\_Nonbank\\_Boom\\_Lux\\_Greene.pdf](https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/working_papers/42_Nonbank_Boom_Lux_Greene.pdf) [<https://perma.cc/L5ML-PK4D>] (“Dodd-Frank authorized the CFPB to supervise, examine, and regulate all non-banks engaged in the mortgage market.”).

122. See Caitlin Reilly, *Bank Executives Warn Lawmakers of Lending Risk Among Nonbanks*, ROLL CALL (Sept. 21, 2022), <https://rollcall.com/2022/09/21/bank-executives-warn-lawmakers-of-lending-risk-among-non-banks/> [<https://perma.cc/9FP4-NYM6>] (noting that non-bank mortgage lenders are not required to hold a minimum amount of capital like banks).

123. See You Suk Kim et al., *Nonbanks and Mortgage Securitization*, 14 ANN. REV. FIN. ECON. 137, 143 (2022) (“Non-banks can be more nimble than banks in entering new markets, adapting to changing market conditions, and adopting new technologies.”); Lux & Greene, *supra* note 121, at 26–29 (discussing how non-banks have successfully used technology and innovation to revolutionize the mortgage underwriting market).

124. See You Suk Kim et al., *Mapping the Boom in Nonbank Mortgage Lending—and Understanding the Risks*, BROOKINGS (Sept. 10, 2018), [https://www.brookings.edu/articles/mapping-the-boom-in-nonbank-mortgage-lending-and-understanding-the-risks/#\\_ftn1](https://www.brookings.edu/articles/mapping-the-boom-in-nonbank-mortgage-lending-and-understanding-the-risks/#_ftn1) [<https://perma.cc/Z8HS-54GU>] (“The share of mortgages issued by nonbanks grew, in part, because banks pulled back from extending mortgage credit to borrowers with lower credit scores in the aftermath of the financial crisis.”).

125. See Zsuzsa R. Huszár & Wei Yu, *Mortgage Lending Regulatory Arbitrage: A Cross-Sectional Analyses of Nonbank Lenders*, 41 J. REAL ESTATE RSCH. 219, 223–24 (2019) (arguing that opportunistic nonbank lenders may have entered via less regulated states and engaged in large scale risky loan originations).

126. See generally IMF, GLOBAL FINANCIAL STABILITY REPORT SAFEGUARDING FINANCIAL STABILITY AND HIGH INFLATION AND GEOPOLITICAL RISKS (2023) (on file with *The Journal of Corporation Law*) (discussing vulnerabilities of nonbank financial intermediaries in great detail in Chapter 2).

the US institutional leveraged loan market[,] . . . a sector in which pension funds and insurance companies are significant investors. . . .”<sup>127</sup> Worldwide, “private credit market rivals the institutional leveraged loan market, which is driven by large bank syndications. Both markets had approximately \$1.4 trillion outstanding in 2022.”<sup>128</sup>

Some of the biggest PE and investment management firms, including Ares Management Corp, Brookfield Asset Management, and KKR are lending in areas traditionally dominated by banks.<sup>129</sup> Investors providing private credit comprise 12% of the \$6.3 trillion U.S. commercial credit market, according to Fitch Ratings.<sup>130</sup> That is smaller than, but not incomparable with, regional banks, which account for \$4.5 trillion in loans.<sup>131</sup>

One might expect banks to respond to these incursions onto their turf with protests and defenses of their industries, but that has not been the case. Banks appear to mostly think that the mortgage origination market is not worth the regulatory hassles, to say nothing of their new appreciation for the riskiness of mortgage loans in the wake of the financial crisis. The nonbanks who are doing most of the mortgage origination these days have not been met with much handwringing at all. Worries about private equity’s entry into real estate lending have also generated little more than a shrug. And money market funds, which have received plenty of criticism, appear to be here to stay.

#### D. Nonbanks As Deposit-Takers

You can even tell a story that nonbanks are intruding on the holiest of functions of banks—taking deposits. To be sure, the story requires a modest suspension of disbelief, or at least a willingness to think creatively about the meaning of the word deposit. But if companies hold money or other stores of value for millions of customers, redeemable on demand, they are not *not* engaging in the business of banking. Consider two examples: gift cards and frequent flyer programs.

Starbucks has over \$1.6 billion in stored value on its customers’ Starbucks cards and over 24 million members in its reward program.<sup>132</sup> Those cards are redeemable at Starbucks whenever the customer wants—just as money in checking accounts is at banks. Moreover, it is real money—the money stored on Starbucks cards exceeds the total value of deposits held by many chartered banks.<sup>133</sup> The great thing about deposits is that they are a cheap form of financing—banks pay low interest on checking and savings accounts,

127. *Id.* at 16.

128. *Id.* at 72.

129. Tatiana Bautzer & Saeed Azhar, *Private Equity Steps Up Lending as U.S. Banks Pull Back*, REUTERS (May 22, 2023), <https://www.reuters.com/business/finance/private-equity-steps-up-lending-us-banks-pull-back-2023-05-22/> (on file with the *Journal of Corporation Law*).

130. *Id.*

131. *Id.*

132. Abhinav Paliwal, *The Neo Bank that Grew its Deposits to \$1.6B*, FINEXTRA (Apr. 4, 2022), <https://www.finextra.com/blogposting/22084/the-neo-bank-that-grew-its-deposits-to-16b> [<https://perma.cc/6KJA-CQMU>].

133. Tonya Garcia, *Starbucks has More Customer Money on Cards than Many Banks Have in Deposits*, MARKETWATCH (June 11, 2016), <https://www.marketwatch.com/story/starbucks-has-more-customer-money-on-cards-than-many-banks-have-in-deposits-2016-06-09> [<https://perma.cc/3T33-H7XM>].

much lower than the current rate of inflation, as many people have observed.<sup>134</sup> But bank deposit interest rates are much better than the 0% that Starbucks pays its card-holding customers. In all, Starbucks' card program gives it a seven-figure interest-free line of credit to reinvest in its business—or at least take all the upside on the float.<sup>135</sup> To be sure, Starbucks does not treat these deposits precisely the way a bank would—it does not lend against them, and it is the taking of deposits (with low interest rates) to lend them out (at higher interest rates) that makes banks useful, usually profitable, and occasionally dangerous (because the deposits can be taken out at any time, but the loans cannot be liquidated as easily). This Article is not calling for Starbucks to be subject to bank regulation; it is only observing that a creative but completely plausible interpretation of *deposits* shows that a commercial firm like Starbucks is, like a bank, a deposit-taking institution. And of course, something similar can be said about all the other firms with similar card offerings.

As for frequent flyer programs, some people have observed that the miles and credit card business that every airline offers are usually worth more than the move-people-through-the-air business.<sup>136</sup> One sometimes hears that these companies should get out of the transportation business and focus on their more valuable commercial operations. For example, over half of American Airlines' profits are from selling frequent flier miles to big banks and other companies.<sup>137</sup> This has led some commentators to describe these large airline companies as “central banks” because airlines can adjust the supply of frequent flier miles based on consumer demand, similar to how central banks adjust interest rates to affect economic conditions.<sup>138</sup> Once again, this does not mean that federal banking regulators should charge the airlines with unlicensed banking operations. But the analogy between

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134. See, e.g., Taylor Tepper, *History of Savings Account Interest Rates*, FORBES (Feb. 4, 2025), <https://www.forbes.com/advisor/banking/savings/history-of-savings-account-interest-rates/> (on file with the *Journal of Corporation Law*) (describing typical U.S. savings account rates in the 2010s as being, at most, one-tenth of the inflation rate of the same time period).

135. See Justin Bariso, *Starbucks Devised a Brilliant Plan to Borrow Money from Customers (Without Getting Anybody Angry)*, INC. (Oct. 21, 2020), <https://www.inc.com/justin-bariso/starbucks-devised-a-brilliant-plan-to-borrow-money-from-customers-without-getting-anybody-angry.html> [<https://perma.cc/YL7D-LUB6>] (citing Neil Patel that Starbucks had \$1.4 billion in unused prepaid balances as of March 29, 2020); see also Yashna Nathwani & Ishwari Hartalkar, *Starbucks: Coffee Shop or Unregulated Bank?*, INT'L J. RSCH. ENG'G, SCI. & MGMT., no. 11, 2021, at 89, 90 (“Starbucks’ strategy is genius because it gives the company access to cash flow and produces extra revenue.”).

136. Jon Sindreu, *Are Frequent-Flier Programs Really Worth More Than Airlines?*, WALL ST. J. (Mar. 15, 2021), <https://www.wsj.com/articles/are-frequent-flier-programs-really-worth-more-than-airlines-11615810430> (on file with the *Journal of Corporation Law*); see also Justin Bachman, *Airlines Make More Money Selling Miles Than Seats*, BLOOMBERG (Mar. 31, 2017), <https://www.bloomberg.com/news/articles/2017-03-31/airlines-make-more-money-selling-miles-than-seats#xj4y7vzkg> (on file with the *Journal of Corporation Law*) (stating that loyalty programs have “expanded so much that it accounts for more than half of all profits for some airlines”).

137. *Major U.S. Airlines have Played Their Cards Right, Making Banks a Vital Co-Pilot*, DALL. MORNING NEWS (Mar. 31, 2017), <https://www.dallasnews.com/business/airlines/2017/03/31/major-u-s-airlines-have-played-their-cards-right-making-banks-a-vital-co-pilot/> [<https://perma.cc/82PV-4H8L>].

138. See Elliot Locke, *The Strange Way Airlines are Actually Central Banks*, WTF IS GOING ON WITH THE ECON.?! (June 23, 2020), <https://abroaden.substack.com/p/the-strange-way-airlines-are-actually> [<https://perma.cc/ABW3-DF36>] (“For airlines, frequent flyer points are like having and controlling an in-house currency — just like a central bank. And just like central banks, airlines can manage their own economy to weather turbulent markets and boost growth on their terms.”).

dollars and frequent flyer miles has been drawn before—both are stores of value and fungible units of account. Customers talk about banking their frequent flyer miles.<sup>139</sup> Airlines also make money from their credit card programs via rent-a-banks, and so are important financial institutions, as well as transportation firms.<sup>140</sup>

*E. Fintechs Are Entering Finance . . . Sometimes with Banking Licenses*

Increasingly, nonbanks offering banking services are successfully contracting around the regulatory perimeter to offer a full suite of banking services to customers.<sup>141</sup> Since 2020, megabanks such as Bank of America, JPMorgan Chase, and Wells Fargo, have seen decreases in primary customer checking account assignments among the Millennial, Gen Z, and Gen X demographics—and Gen Xers can be over fifty at this point—although 2023 crises at some midsized banks led to deposit in-flows back into some of the biggest banks.<sup>142</sup>

These digitally native consumers are increasingly turning towards digital banks such as Chime, PayPal, or Cash App for banking services.<sup>143</sup> These fintech companies, many of which are fully digital, are able to offer nearly identical banking services as a traditional brick-and-mortar bank by contracting with and entering into partnerships with banks that do have the necessary regulatory approvals to offer the services that banks do.<sup>144</sup> In some cases like Revolut, these partnerships may only be temporary as fintech companies seek regulatory approval to become a traditional bank.<sup>145</sup> But in other cases, these partnerships

139. David Crook, *I'm Following Congress' Example and Skipping My Credit Bill*, KIPLINGER (May 17, 2023), <https://www.kiplinger.com/politics/im-following-congress-example-and-skipping-my-credit-bill-crook-note> [https://perma.cc/L9R3-JSKW].

140. Locke, *supra* note 138.

141. See, e.g., Serge Beck, *What Factors Affect The Development of Neobanks?*, FORBES (Oct 4, 2022), <https://www.forbes.com/sites/forbestechcouncil/2022/10/04/what-factors-affect-the-development-of-neobanks/?sh=1d5654eb4f81> (on file with the *Journal of Corporation Law*) (discussing the main growth factors affecting neobanks and noting the high expected compound annual growth rate of neobanks).

142. See Ron Shevlin, *How Fintechs Are Dominating New Checking Account Openings*, FORBES (July 5, 2023), <https://www.forbes.com/sites/ronshevlin/2023/07/05/the-checking-account-war-is-over-and-the-fintechs-have-won/?sh=6a4e1d5e3a31> (on file with the *Journal of Corporation Law*) (examining why this generational shift is occurring).

143. See Ron Shevlin, *The Growing Domination of Chime, Cash App, and PayPal in Banking*, FORBES (Mar. 1, 2022), <https://www.forbes.com/sites/ronshevlin/2022/03/01/the-growing-domination-of-chime-square-cash-app-and-paypal-in-checking-accounts/?sh=17da06cb565c> [https://perma.cc/57CT-97A2] (describing the trend as “skyrocketing”).

144. See Julie Verhage, *No Banking Charter? No Problem. Fintech Companies Team Up with Small-Town Banks*, L.A. TIMES (Sept. 27, 2019), <https://www.latimes.com/business/story/2019-09-26/no-banking-charter-no-problem-fintechs-team-up-with-small-town-banks> (on file with the *Journal of Corporation Law*) (“Partnerships between high-flying tech companies and traditional banks, many of them tiny by comparison, are a key force behind the financial technology boom. Because virtually no tech companies have the license required to perform banking services, many of them partner with existing banks to offer a suite of services including checking accounts, credit cards and the back-end and regulatory work the tech companies aren’t equipped—or allowed—to handle.”).

145. See Laura Noonan & Siddarth Venkataramakrishnan, *Revolut's Growing Pains: Is the Fintech Ready to Become a Bank*, FIN. TIMES (Nov. 17, 2022), <https://www.ft.com/content/4c02367e-7549-4502-9455-fcb9dc31dfe0> (on file with the *Journal of Corporation Law*) (noting that the CEO of Revolut believes a banking license is “key to the company’s broader ambitions”).

are often a part of a neobanks' long-term strategy who have no interest in pursuing a charter.<sup>146</sup>

Neobanks have been learning as they have been doing, and have had to worry about payment hiccups, cybersecurity, and even fraud banks loath to see,<sup>147</sup> as well as marketing themselves as banks despite not having the necessary regulatory approvals.<sup>148</sup> Fintech companies have defended their entry into banking on the grounds that neobanks are better able to serve mainstream consumers whose trust in large banks has waned.<sup>149</sup>

Nor is this the only advantage that the digital neobanks claim to offer. They also posit, with at least some justification, that they can solve the problem of unbanked and underbanked Americans. The idea is that having a bank account is not just useful, but almost necessary in this modern world, and those without often have trouble cashing their paychecks, taking advantage of credit and debit cards, and simply saving for the future.<sup>150</sup>

Can the Chimes of the world help? The Philadelphia Federal Reserve has conducted a study suggesting individuals are more likely to begin first-time savings or significantly increase their savings after engaging with a fintech.<sup>151</sup> Moreover, these fintechs can use

146. See Ryan Deffenbaugh, *Upstart Has a New Plan to Sell Wall Street on its Loans*, PROTOCOL (Aug. 18, 2022), <https://www.protocol.com/fintech/upstart-loans-balance-sheet> [https://web.archive.org/web/20220818124034/https://www.protocol.com/fintech/upstart-loans-balance-sheet] (explaining that, despite non-bank Upstart's short-term decline in revenue, it has "no plans" to apply for a banking charter).

147. See Siddarth Venkataramakrishnan & Akila Quinio, *Revolut's US Payment Flaws Allowed Thieves to Steal \$20mn*, FIN. TIMES (July 9, 2023), <https://www.ft.com/content/0025347f-6e0c-4dbd-9762-e4ecc0431050> (on file with the *Journal of Corporation Law*) (discussing how organized criminal groups used Revolut's payment system to perpetuate a fraud against the company); see also Carson Kessler, *A Banking App Has Been Suddenly Closing Accounts, Sometimes Not Returning Customers' Money*, PROPUBLICA (July 6, 2021), <https://www.propublica.org/article/chime> [https://perma.cc/6BKV-F5KS] (noting that hundreds of Chime consumer accounts were reported as having been erroneously closed as a part of Chime's effort to crack down on fraud); see Press Release, Senator Sherrod Brown, Brown Presses CFPB To Address Risks to Consumers From Fintechs Like Chime (July 27, 2021), <https://www.brown.senate.gov/newsroom/press/release/presses-cfpb-address-risks-fintechs-chime> [https://perma.cc/YFD9-2M5E] (urging the Acting Director of the CFPB to investigate consumer risks involving non-banks, including "privacy concerns, fraud, data breaches, and proper disclosure that these companies are not actually banks").

148. See Lydia Beyoud, *California Prohibits Fintech Chime From Calling Itself a Bank*, BLOOMBERG L. (May 5, 2021), <https://news.bloomberglaw.com/banking-law/california-prohibits-fintech-chime-from-calling-itself-a-bank> (on file with the *Journal of Corporation Law*) (discussing a settlement between Chime and California's financial regulators whereby Chime must refrain from "calling itself a 'bank' or using the term 'banking' in its marketing materials."); Settlement Agreement, Comm'n of Fin. Prot. and Innovation v. Chime Fin., Inc., 2021 WL 1536229, at \*2 (Cal. Dept. Corp. Mar. 29, 2021) (ordering Chime to "cease and desist from using the name 'chimebank.com' in its business unless and until it becomes licensed or otherwise authorized to engage in the business of banking under the laws of California, another state or of the United States").

149. See Ian Thomas, *Fintech CEO Chris Britt of Chime on Reasons Americans Don't Trust Banks*, CNBC: DISRUPTOR 50 (May 9, 2023), <https://www.cnbc.com/2023/05/09/chime-ceo-chris-britt-on-the-reasons-americans-dont-trust-banks.html> [https://perma.cc/8RW9-HKM2] (quoting Chime CEO Chris Britt that "[i]t's very difficult for the big banks structurally to compete for the segment that we aim to serve, which is sort of mainstream middle and more lower income consumers").

150. See generally MEHRSA BARADARAN, *HOW THE OTHER HALF BANKS: EXCLUSION, EXPLOITATION, AND THE THREAT TO DEMOCRACY* (2015) (discussing the paradoxical high cost of being too poor to use traditional financial institutions).

151. Gregor Becker, *Does FinTech Affect Household Savings Behavior?: Findings From a Natural Field Experiment 3* (June 12, 2017) (unpublished manuscript) (on file with Fed. Rsrv. Bank of Phila.), <https://www.philadelphiafed.org/-/media/frbp/assets/events/2017/consumer-finance/fintech-2017/day-2/does-fintech-affect-household-saving-behavior.pdf> [https://perma.cc/6H4X-NP4H].

their data on their customers and design their apps to help their consumers save more.<sup>152</sup> One of the reasons they can do so is precisely because they are not regulated like traditional banks, which face more regulatory scrutiny, meaning that the digital experience of these fintechs is different from banks and often more appealing to the underbanked.<sup>153</sup> Neobanks thus often tout their ability to win customers from underbanked groups like hourly wage workers, students, small startup businesses, and even affinity groups who have been left behind by traditional banking.<sup>154</sup>

Many nonbank fintechs, wanting the benefits of banking regulations, have either applied for or been granted an actual or stripped-down banking charter.<sup>155</sup> Varo Bank, a digital fintech company, was the first neobank to be granted a stand-alone application for a national bank charter by the OCC in 2018.<sup>156</sup> Other fintech nonbanks have obtained banking charters by merging with smaller banks with pre-existing banking licenses, oftentimes at a premium price.<sup>157</sup> For example, LendingClub, a peer-to-peer lender, gained a bank

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152. Antoine Gara, Nathan Vardi & Jeff Kauflin, *The Forbes Investigation: Inside the Secret Bank Behind the Fintech Boom*, FORBES (Dec. 17, 2019), <https://www.forbes.com/sites/antoinegara/2019/12/17/the-forbes-investigation-inside-the-secret-bank-behind-the-fintech-boom/?sh=1ed2cabb3c10> (on file with the *Journal of Corporation Law*); Cara Daly, *How Betterment's Tech Helps You Manage Your Money*, BETTERMENT (Sept. 1, 2022), <https://www.betterment.com/resources/how-betterment-technology-manages-money> [<https://perma.cc/6LQW-EHZ7>].

153. See Christopher K. Odinet, *Predatory Fintech and the Politics of Banking*, 106 IOWA L. REV. 1739, 1754 (2021) (reporting that Neobanks create a user experience that is more appealing to the modern day consumer); see Anne Field, *Fighting Systemic Barriers With a Neobank for Native Americans*, FORBES (Nov. 22, 2022), <https://www.forbes.com/sites/annefield/2022/11/22/fighting-systemic-barriers-with-a-neobank-for-native-americans/?sh=7324a394573f> (on file with the *Journal of Corporation Law*) (for example, the neobank To-tem is aimed at Native Americans “living on remote rural reservations” that features spotty mail delivery).

154. See Terri Bradford, *Neobanks: Banks by Any Other Name?*, FED. RSRV. BANK KANSAS CITY (Aug. 11, 2020), <https://www.kansascityfed.org/research/payments-system-research-briefings/neobanks-banks-any-other-name/> [<https://perma.cc/8XNQ-VMDT>] (noting that Neobanks differentiate themselves from traditional banks to target specific consumer groups by offering a strong digital interface).

155. See Allison Bennett & Nathaniel Melican, *SoFi's National Bank Charter Widens Door for Fintechs*, S&P GLOBAL (Feb. 8, 2022), <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/sofi-s-national-bank-charter-widens-door-for-fintechs-68729830> [<https://perma.cc/P77M-EDHB>] (“Some large fintechs want to become banks because it gives them access to more customers and allows them to provide the same broad range of services that national banks do.”); see also Sara Khairi, *Rebundling Banking Services: Are Fintechs Trying to be More Like Banks?*, TEARSHEET (Jan. 9, 2023), <https://tearsheet.co/new-banks/rebundling-banking-services-are-fintechs-trying-to-be-more-like-banks/> [<https://perma.cc/V66S-ABJY>] (discussing why fintech companies are seeking banking licenses).

156. See Letter from Stephen A. Lybarger, Deputy Comptroller for Licensing, OCC, to Mitchell S. Eitel, Sullivan & Cromwell LLP, Conditional Approval #1205: Preliminary Conditional Approval of the De Novo Charter Application for the Proposed Varo Bank (Aug. 31, 2018), <https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2018/ca1205.pdf> [<https://perma.cc/3JBG-MWEV>]; see also Zaring, *supra* note 10, at 1434–39 (discussing in-depth Varo’s application for a banking charter).

157. See Naomi Synder, *Fintechs Are Starting to Buy Banks, But Why?*, BANK DIR. (Nov. 22, 2021), <https://www.bankdirector.com/issues/bank-ma/fintechs-are-starting-to-buy-banks-but-why/> [<https://perma.cc/6HSB-4HRN>] (“Fintechs may also be willing to pay more for a small bank than another bank will. For a large fintech company, getting access to a bank charter may be critical for their business plan going forward; paying an extra \$1 million or \$2 million may not be a lot of money for the fintech, but might be meaningful for the small bank.”).



charter by acquiring Radius Bank in 2020,<sup>158</sup> and SoFi, another lender, did the same through its acquisition of Golden Pacific Bank in 2022.<sup>159</sup> The overall success of fintechs acquiring bank charters with the OCC, however, has been mixed, with most recent applications either being withdrawn or pending under the Biden administration.<sup>160</sup>

#### F. Banks Have Breached the Perimeter as Well, But They Always Have

Banks have made fewer efforts to run commercial firms in the past decade, but they also have gone beyond their perimeter in one controversial way and two long-permitted ways. The newer development is that banks sometimes open customer-friendly businesses like coffee shops.<sup>161</sup> As we have seen, more banks are partnering with nonbanks to let the nonbank offer financial services to their clients which, as we have seen, has created a real set of challenges to the regulatory perimeter.<sup>162</sup> Finally, there have been a few modest efforts to actually pursue commercial ventures; because one of these efforts is both amusing and illustrative, we analyze it here. The Trump administration, of course, may be more sympathetic to breaches of the regulatory barrier between banking and commerce.

##### 1. Banks Rent Out Their Charters to Allow Nonbanks to Breach the Regulatory Perimeter

The most recent and controversial way that banks are breaching the regulatory perimeter is by partnering with nonbanks to let them participate in the business of banking. There is no need here to recount the particulars of the BaaS model that we have seen exemplified by the work of Walmart, PayPal, Revolut, and Chime, with their banking partners in Part I.<sup>163</sup> But it is worth noting that BaaS is a function of regulatory arbitrage. It allows fintechs and large commercial firms to use toe-touches through very small banks to offer banking

158. See Letter from Stephen A. Lybarger, Deputy Comptroller for Licensing, OCC, to Sara Lenet, Couns., Hogan Lovells US LLP & Tim Bogan, Chief Banking Integration Off., LendingClub Corp., Conditional Approval #1258: Application by Radius Bank to Convert to a National Banking Association and to Charter LendingClub Bank (Dec. 30, 2020), <https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2021/ca1258.pdf> [<https://perma.cc/B5CA-K7C8>] (approving the application by Radius Bank to convert to a National Banking Association); see also Hugh Son, *LendingClub Buys Radius Bank for \$185 Million in First Fintech Takeover of a U.S. Regulated Bank*, CNBC (Feb. 18, 2020), <https://www.cnbc.com/2020/02/18/lendingclub-buys-radius-bank-in-first-fintech-takeover-of-a-bank.html> [<https://perma.cc/J8GN-CER9>] (reporting that LendingClub acquired Radius Bank to access cheaper funding).

159. See Letter from Stephen A. Lybarger, Deputy Comptroller for Licensing, OCC, to Richard K. Kim, Partner, Wachtell, Lipton, Rosen & Katz, Conditional Approval #1252: Conditional Approval to charter SoFi Interim Bank (Jan. 18, 2020), <https://www.occ.treas.gov/news-issuances/news-releases/2022/nr-occ-2022-4a.pdf> [<https://perma.cc/8GZF-UZQF>]; see also Bennett & Melican, *supra* note 155 (discussing how this approval was “largely” accomplished through the acquisition of a small bank).

160. See Alison Bennet & Nathaniel Melican, *National Bank Charter Applications Plummet Under Biden Administration*, S&P GLOBAL (Nov. 5, 2021), <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/national-bank-charter-applications-plummet-under-biden-administration-67460466> [<https://perma.cc/WA3M-6GC8>] (“In addition to the lack of applications in the Biden administration, there have been several withdrawals of requests filed under Trump.”).

161. Kate Fitzgerald, *The Bank-Branch Café is Still Booming*, YAHOO FINANCE (Aug. 23, 2023), <https://finance.yahoo.com/news/bank-branch-caf-still-booming-161921551.html> [<https://perma.cc/8EM4-ST7S>].

162. See *supra* Part I.B.

163. *Id.*

services to their customers. The BaaS banks are compensated, either with a fee or with a share of the lending or deposits that the nonbanks bring in.<sup>164</sup>

Regulators do not appear to care about this straightforward breach of the regulatory perimeter—and maybe it is good to have nonbanks competing to offer banking services with banks.<sup>165</sup> But there is more than a touch of hypocrisy here. As Matt Levine has observed, the bases for BaaS arrangements “are essentially regulatory: US law prefers personal loans made by banks and disfavors personal loans made by other companies and is mostly pretty flexible about what happens a second before and second after the loan is made.”<sup>166</sup>

Through BaaS partnerships, fintech firms interested in doing the business of banking can create a website that markets loans to consumers, briefly connects those interested to banks to get the loans, and then buys the loans from the banks immediately.<sup>167</sup> Of course banking as a service banks can provide other kinds of banking services that do not seem particularly worrisome—“white label” credit cards mean that department stores or sports teams can extend credit to their customers or fans, other commercial firms can use banks to process payments, and so on.<sup>168</sup>

But the BaaS version of split-second lending makes it look like neither regulators nor banks really care about maintaining the regulatory perimeter and are happy to let nonbanks pretend that they are working with banks to offer banking services to their customers. Nonbanks do not have to worry about capital requirements, bank runs, or the other things that regulators and banks obsess over.<sup>169</sup> And yet the nonbanks are, economically, exactly in the same place as lending banks.

It is unlikely that, if a nonbank’s customer acquisition practices got a bank in trouble, the trouble would introduce too much risk into the system now—BaaS banks are generally small ones, and the market is new, although some expect it to grow in the United States at a 14.3% rate annually for the rest of the decade.<sup>170</sup> But currently, it is not clear that these partners are subject to much oversight.

164. As the consultant Elizabeth Gujral put it, “[t]he fintech company takes on most of the costs around customer acquisition and banks get a portion of the interchange or fee income generated by those customers.” Elizabeth Gujral, *BaaS Banks Are In Time Out, And Here’s Why It’s a Big Deal*, CORNERSTONE ADVISORS (June 14, 2023), <https://gonzobanker.com/2023/06/baas-banks-are-in-time-out-and-heres-why-its-a-big-deal/> [<https://perma.cc/8SKZ-AEX7>].

165. Braeden Hodges, *Banking-As-A-Service: Fintechs Walking the Regulatory Perimeter*, 17 BROOK. J. CORP., FIN. & COM. L. 127, 139 (2023) (“OCC Says Bank-FinTech Partnerships Are Here to Stay.” (internal quotations omitted)).

166. Matt Levine, *The Fintechs Are Banks Now*, BLOOMBERG (Feb. 19, 2020), <https://www.bloomberg.com/opinion/articles/2020-02-19/the-fintechs-are-banks-now> (on file with the *Journal of Corporation Law*).

167. *Id.*

168. For an analysis, see Matthew Adam Bruckner, *The Promise and Perils of Algorithmic Lenders’ Use of Big Data*, 93 CHI.-KENT L. REV. 3, 22 n.132 (2018).

169. Raj Bhala, *Applying Equilibrium Theory and the FICAS Model: A Case Study of Capital Adequacy and Currency Trading*, 41 ST. LOUIS U. L.J. 125, 130 n.17 (1996).

170. *Banking-as-a-Service Market Size, Share & Trends Analysis Report By Product Type (API-, Cloud-based BaaS), By Component (Platform, Services), By Enterprise Size (Large, SME), By End-Use (Banks, NBFC), And Segment Forecasts, 2022 – 2030*, GRANDVIEW RSCH. (2022), <https://www.grandviewresearch.com/industry-analysis/banking-as-a-service-market-report> [<https://perma.cc/K4VZ-PF5V>] (“The global banking-as-a-service market size was valued at USD 19.65 billion in 2021 and is expected to expand at a Compound Annual Growth Rate (CAGR) of 16.2% from 2022 to 2030.”).

Federal banking regulators have claimed that the Bank Service Company Act gives them the authority to supervise these third-party relationships and have brought some enforcement actions against BaaS providers and third parties.<sup>171</sup> But that statute—passed in 1962 to deal with third-party contractors who offered services such as “check and deposit sorting and posting, computation and posting of interest and other credits and charges, preparation and mailing of checks, statements, notices, and similar items, or any other clerical, bookkeeping, accounting, statistical, or similar functions performed for a depository institution,” is not clearly fit for a supervisory purpose.<sup>172</sup>

As we will see, directly chartering fintechs would much more directly bring them inside the regulatory perimeter and obviate the need for the most hypocritical forms of BaaS.

## 2. Banks Now Underwrite Most Securities Offerings

The most important long-permitted form of banks entering nonbanking was driven by the repeal of the separation between banking and investment banks occasioned by the 1999 Gramm-Leach-Bliley Act’s repeal of the portion of the Depression Era Glass-Steagall Act separating banking from investment banking,<sup>173</sup> and finalized by the collapse of all of the five major investment banks during the financial crisis of 2007–08.<sup>174</sup>

Gramm-Leach Bliley repealed section 20 of the Glass-Steagall Act, which forbade banks from affiliating with firms that underwrote securities.<sup>175</sup> Under the statute, commercial banks were permitted to affiliate with insurance companies, investment banks, and other financial companies, though all such financial supermarkets would need to be organized as bank holding companies supervised by the Fed.<sup>176</sup>

The combination of banking and insurance has been halting, if not unheard of,<sup>177</sup> but the financial crisis rescue of four of the five largest investment banks, and the failure of the fifth, means that American banks now own all the large investment banks.<sup>178</sup> The SEC had a disastrous time during the financial crisis supervising the capital adequacy standards of large investment banks, over which it then had jurisdiction, and, as a condition of rescuing

171. See, e.g., Cross River Bank, FDIC 17-0123b, FDIC 17-0121b, FDIC 17-0122k (2018) (“Consent Order, Order for Restitution, and Order to Pay Civil Money Penalty”); Freedom Fin. Asset Mgmt., LLC, FDIC 17-0126b, FDIC 17-0125b, FDIC 17-0124k (2018) (“Consent Order, Order for Restitution, and Order to Pay Civil Money Penalty”). For a more sanguine view of the authority of regulators than mine, see Marc P. Franson, *Collisions at the Intersection of State Usury Laws and Federal Preemption*, 39 REV. BANKING & FIN. L. 949, 1002 (2020).

172. 12 U.S.C. § 1863.

173. Banking Act of 1933, 12 U.S.C. §§ 78, 227; James R. Barth, R. Dan Brumbaugh & James A. Wilcox, *Policy Watch: The Repeal of Glass-Steagall and the Advent of Broad Banking*, 14 J. ECON. PERSPS. 191 (2000).

174. John Weinberg, *The Great Recession and Its Aftermath*, FED. RSRV. HIST. (Nov. 22, 2013), <https://www.federalreservehistory.org/essays/great-recession-and-its-aftermath> [<https://perma.cc/X5NE-7ZCZ>].

175. Despina Chouliara, *The Financial Services Modernization Act of 1999*, AM. PREDATORY LENDING (Apr. 25, 2020), <https://predatorylending.duke.edu/policy/legislative-memos/the-financial-services-modernization-act-of-1999/> [<https://perma.cc/WV4V-8B69>].

176. Bank Holding Company Act of 1956, 12 U.S.C. § 1843(c)(8).

177. Allissa Kline, *Why Lots of Banks Are Saying Goodbye to Their Insurance Agencies*, AM. BANKER (Dec. 22, 2023), <https://www.americanbanker.com/list/why-lots-of-banks-are-saying-goodbye-to-their-insurance-agencies> [<https://perma.cc/4944-EPBS>].

178. Manoj Singh, *The 2008 Financial Crisis Explained*, INVESTOPEDIA (Aug. 25, 2024), <https://www.investopedia.com/articles/economics/09/financial-crisis-review.asp> [<https://perma.cc/6AUP-VMBF>].

the investment banks, banking regulators either merged them with banks or required them to become bank holding companies overseen by the Fed.<sup>179</sup> The combination of banking and investment banking has been momentous, but has also been the subject of a large legal literature—recounting it again is perhaps unnecessary. The point is to further destabilize the regulatory perimeter by recognizing a very intentional dismantling of part of it by the regulators themselves.

### 3. Banks Compete with Mutual Funds

Banks offer products substantially similar to money market funds, which are regulated by the SEC, rather than the banking agencies.<sup>180</sup> This is banks doing nonbanking, but the industry has breached this perimeter for a very long time—the first such bank-administered funds were created in 1927.<sup>181</sup>

The trust charter has allowed banks to get out of banking alone and offer other services to investors for almost a century, an important example of the fuzzy boundaries between banks and financial commerce that have been tolerated by regulators.

Trusts have been used to create a set of competitors to money market mutual funds and money managers like Vanguard, Fidelity, and State Street. Trust bank charters are often used to house Collective Investment Funds (CIFs) and Short Term Investment Funds (STIFs). CIFs are tax-exempt pooled investment vehicles.<sup>182</sup> The funds look like mutual funds—they co-mingle investor funds that provide their investors with a pro-rata return on their funds—just as mutual funds do. Like, mutual funds, CIFs and STIFs enable their sponsors to avoid holding a large number of small investment accounts and offer the possibility of scale to both investors and sponsors.<sup>183</sup>

179. See Daniel M. Gallagher, Comm’r, SEC, Speech on The Philosophies of Capital Requirements (Jan. 15, 2024), <https://www.sec.gov/newsroom/speeches-statements/2014-spch011514dmg> [<https://perma.cc/JY65-M5VB>] (discussing SEC’s view of capital requirements in the wake of the financial crisis).

180. SEC, MUTUAL FUNDS AND ETFs: A GUIDE FOR INVESTORS 13–14 (2016), <https://www.sec.gov/investor/pubs/sec-guide-to-mutual-funds.pdf> [<https://perma.cc/H9TJ-2PC9>].

181. Troy Segal, *Collective Investment Fund (CIF): History, Pros & Cons, Example*, INVESTOPEDIA (May 25, 2020), <https://www.investopedia.com/terms/c/collective-investment-fund.asp> [<https://perma.cc/MJ5Y-Q22A>]. (“The first collective investment fund was created in 1927. A victim of bad timing, when the stock market crashed two years later, the perceived contribution of these pooled funds to the ensuing financial hardships led to severe limitations on them. Banks were restricted to only offering CIFs to trust clients and through employee benefit plans.”).

182. CIFs are only available for investment by some institutional retirement plans including, most importantly, 401(k) plans, and defined contribution (DC) or defined benefit (DB) retirement plans that are qualified under Internal Revenue Code Section 401(a). In some cases, “Taft-Hartley” retirement plans, and government 457(b) plans, as well as self-employed plans, church plans, and Puerto Rico plans, will also be eligible. For articles on CIFs, see MICHAEL NELLIGAN, COLLECTIVE INVESTMENT TRUSTS LOWER COSTS AND GREATER FLEXIBILITY 1 (2018), <https://www.ssga.com/dc/2019/Collective-Investment-Trusts-vs-Mutual-Funds.pdf> [<https://web.archive.org/web/20220720181814/https://www.ssga.com/dc/2019/Collective-Investment-Trusts-vs-Mutual-Funds.pdf>]; *Collective Investment Funds*, OCC, <https://www.occ.treas.gov/topics/supervision-and-examination/capital-markets/asset-management/collective-investment-funds/index-collective-investment-funds.html> [<https://perma.cc/8U7P-JDUL>]; THE COALITION OF COLLECTIVE INV. TRUSTS, COLLECTIVE INVESTMENT TRUSTS 3 (2022), <https://www.seic.com/sites/default/files/2022-05/SEI-STC-CCIT-WhitePaper.pdf> [<https://perma.cc/FB9F-SVBX>].

183. See Segal, *supra* note 181 (discussing mechanics of CIF); James Chen, *Short-Term Investment Fund (STIF): What It Is, How It Works*, INVESTOPEDIA (July 7, 2022), <https://www.investopedia.com/terms/s/stif.asp> [<https://perma.cc/8PKQ-UFE8>] (discussing mechanism of STIF).

STIFs are special CIFs that invest in short-term money market investments, thought to be less risky because they will be paid back so quickly.<sup>184</sup> In this way, STIFs closely resemble money market mutual funds, which also invest in short-term instruments.<sup>185</sup> In addition to selling the opportunity to participate in STIFs to pension funds, banks also use STIFs in connection with sweep and securities lending programs.<sup>186</sup>

In 2019, CIF assets totaled \$3.78 trillion and made up 30.1% of all assets held in 401(k) accounts, including most large plan sponsors.<sup>187</sup> When the OCC revised the requirements imposed on national banks regarding STIFs in 2012, the STIF market included \$118 billion in investments.<sup>188</sup>

The difference between these sorts of funds and mutual funds lies in who the sponsor can be, who can take advantage of the funds, and who regulates the fund. A bank or trust company holds the legal title to the fund's assets, acting as the fiduciary of the CIF's beneficial owners.<sup>189</sup> Those owners in turn own an undivided interest in the aggregate assets of a CIF.<sup>190</sup> The bank is constrained by its Declaration of Trust, which lays out the structure of the funds and the role of the trustee as well as a Supplemental Declaration of Trust that outlines the investment objective and guidelines for the fund.<sup>191</sup> CIFs are group trusts,<sup>192</sup> and so are exempt from income taxation—a feature that simplifies the pooling of assets, IRS reporting requirements, and goesos returns for investors.<sup>193</sup> However, CIFs are not open to any individual investors—instead, they can be offered by institutional investors like pension funds and other collective investment vehicles—a distinction, and one that

184. See Chen, *supra* note 183 (stating that STIFs are viewed as “the most conservative investments in the financial industry”).

185. See *What are Money Market Funds and How Do They Work?*, VANGUARD (Feb. 4, 2024), <https://investor.vanguard.com/investor-resources-education/mutual-funds/what-are-money-market-funds> [<https://perma.cc/5QJN-AJRD>] (“They’re designed to offer a safe, stable investment option for money you may need to access in the short term.”).

186. See *STIF: Fund Overview: Objective, Strategy and Holdings*, WESPATH (Feb. 4, 2024), <https://www.wespath.org/Fund-Performance/STIF> [<https://perma.cc/5MQV-B6US>] (stating that Wespath’s STIF “[i]nvests exclusively in units of the sweep account”).

187. ROB BARNETT, JESSICA SCLAFANI & JASON ROBERTS, *COLLECTIVE INVESTMENT TRUSTS: AN IMPORTANT PIECE IN THE RETIREMENT PLANNING PUZZLE 1* (2021), [www.sparkinstitute.org/wp-content/uploads/2021/10/RICS-CIT-White-Paper.pdf](http://www.sparkinstitute.org/wp-content/uploads/2021/10/RICS-CIT-White-Paper.pdf) [<https://perma.cc/72VA-78WV>]; Jana Steele, *A Year Out of Time: Our Survey Tracks How DC Plans Operated in 2020*, CALLAN (Feb. 16, 2021), <https://www.callan.com/blog-archive/2021-dc-survey/> [<https://perma.cc/N6KL-VFHE>] (reporting that 78% of large-plan sponsors used CIFs in their plans); JOHN ALSHEFSKI, *ASSET MANAGERS CAPITALIZE ON GROWTH OF CITS TO ACCESS \$35 TRILLION U.S. RETIREMENT MARKET 1* (2021), <https://www.seic.com/sites/default/files/2022-05/SEI-IMS-Asset-Managers-Capitalize-CIT-Growth-Alshefski.pdf> [<https://perma.cc/JU28-MC5C>]; Kristin O’Donnell, Ryan Mullaney & Tom Peattie, *Why Collective Investment Trusts Are Gaining Traction Within DC Plans*, WELLINGTON MGMT. (Aug. 2022), <https://www.wellington.com/en/insights/collective-investment-trusts-dc-retirement-plans> [<https://perma.cc/ZHW2-PBBJ>].

188. Short Term Investment Funds, 77 Fed. Reg. 61229, 61230 (Oct. 9, 2012) (to be codified at 12 C.F.R. pt. 9).

189. Segal, *supra* note 181.

190. *Id.*

191. See Naomi Wilkes, *Declaration of Trust – Everything You Need to Know*, MOORE BARLOW (May 4, 2022), <https://www.moorebarlow.com/guides/declaration-of-trust-everything-you-need-to-know/> [<https://perma.cc/C6SG-ZCNN>] (discussing declarations of trusts generally).

192. 26 U.S.C. § 401(a).

193. 26 U.S.C. § 501(a).

narrows the market for CIFs compared to mutual funds, which can be offered to any investor, though that makes for larger advertising expenses.<sup>194</sup> The funds have existed since 1927.<sup>195</sup>

Governance, and the possibility of regulatory arbitrage, is perhaps the most notable difference between CIFs and mutual funds. Trust funds are not regulated by the SEC, but, because of the retirement goal, and the trust charter wrapper, are not unregulated—the Department of Labor regulates 401(k)s pursuant to ERISA, while, of course, federal bank regulators regulate the trusts that house them.<sup>196</sup> The different overseers make for a different regulatory experience, however. CIF and STIF investors receive fewer disclosures than do the mutual funds registered with the SEC, which prioritizes disclosure in much of what it does.<sup>197</sup> CIFs can also charge more variable fees than can mutual funds.<sup>198</sup>

The lighter touch regulation of CIFs, along with their limited potential audience, means that CIFs generally cost less to run than do mutual funds, which must advertise for clients, and must make regular disclosures to their investors.<sup>199</sup>

But the different regulatory regimes pose at least theoretical, and possibly real, problems for regulators who might be played off against one another. Consider the Vanguard Trust.<sup>200</sup> Vanguard can thus sponsor SEC-registered investment funds through funds sponsored by the parent and/or CIFs and STIFs through its trust bank. If the regulations favored trust structures, Vanguard could move money funds from the SEC-regulated funds to the lighter touch trust bank regime. We see some evidence that regulators are worried about this kind of wall-crossing. In 2020, the SEC brought an action against a state-chartered trust company alleging that the “[t]rust [f]unds failed to satisfy the ‘maintained’ by a bank requirement”, thus disqualifying the trust funds from reliance on the relevant investment Company Act and Securities Act exemptions.<sup>201</sup> The action suggested that the SEC is willing to insist that CIFS and STIFs be “bank maintained.”<sup>202</sup>

194. Segal, *supra* note 181; *What are Money Market Funds And How Do They Work?*, *supra* note 185.

195. Segal, *supra* note 181.

196. *Retirement Plans Benefits and Savings*, DEP’T. OF LAB., <https://www.dol.gov/general/topic/retirement> [<https://perma.cc/HQ3Z-E6Q3>]; see also, e.g., *Bank Examination Manual: Section 1 – Management*, FDIC (Apr. 19, 2024), <https://www.fdic.gov/bank-examinations/section-1-management> [<https://perma.cc/2ME4-KPZH>] (one of many examples of the FDIC regulating trusts).

197. *Mutual Fund Fee Disclosure: Frequently Asked Questions*, INV. CO. INST. (Feb. 28, 2019), [https://www.ici.org/faqs/faq/expenses/faqs\\_fee\\_disclosure](https://www.ici.org/faqs/faq/expenses/faqs_fee_disclosure) [<https://perma.cc/7SCN-4NYP>].

198. BAILLIE GIFFORD, *A GUIDE TO COLLECTIVE INVESTMENT TRUSTS* 5 (2022), <https://www.bailliegifford.com/literature-library/miscellaneous/baillie-gifford-collective-investment-trust-summary/> [<https://perma.cc/Y8AR-ZGJQ>].

199. BARNETT, SCLAFANI & ROBERTS, *supra* note 187, at 3–4.

200. Vanguard got a 23A exemption in 2021, to allow its trust bank to support a MMF affiliate. Under 23A, banks are generally limited to how large their nonbank affiliates can become. Letter from Ann E. Misback, Sec’y, Bd. of Governors of the Fed. Rsrv. Sys., to Blake Paulson, Acting Comptroller, OCC (Jan. 29, 2021), <https://www.federalreserve.gov/supervisionreg/legalinterpretations/fedreserseactint20210129.pdf> [<https://perma.cc/7WBD-2BSK>].

201. Great Plains Tr. Co., Inc., Exchange Act Release No. 33-10869, 2020 WL 5820419, at \*5 (Sept. 30, 2020). For a discussion, see Marla J. Kreindler et al., *Common and Collective Investment Funds: SEC Action Warrants Attention but Offers Limited Guidance*, MORGAN LEWIS (Dec. 9, 2020), <https://www.morganlewis.com/pubs/2020/12/common-and-collective-investment-funds-sec-action-warrants-attention-but-offers-limited-guidance> [<https://perma.cc/4Z4W-LWWP>].

202. Kreindler et al., *supra* note 201.

#### 4. *Banks Are Dipping a Toe into Commerce (If It Brings In Customers)*

These interventions are largely financial, they are not opening up factories, or retail outlets—with one, somewhat amusing exception. Some banks, in an effort to reach younger clients, are getting into the coffee business.

Over the past several years, multiple large banks traditionally engaged in brick-and-mortar banking services, including Capital One, Chase, and Santander, have opened coffee shops to stay relevant in the face of an increase in the popularity of digital banking and to promote their banking services, especially amongst millennials.<sup>203</sup> These bank-owned coffee shops can fly under the regulatory radar because they do not offer the full suite of typical banking services and offer services that are related to banking (i.e., promoting banking services through selling coffee and merchandise).<sup>204</sup> As a result, these coffee shops are often not deemed “branches” of a bank under 12 U.S.C. § 36 and are therefore not subject to the same regulatory requirements.<sup>205</sup> For example, at a Capital One Café, a consumer can only engage in limited banking services, such as using an ATM and meeting with an on-site banker to open a bank account or credit card, which does not meet the definition of a branch as set forth in section 36(j).<sup>206</sup> Furthermore, national banks are permitted to sell promotional items for marketing, advertising, and promotional purposes as this is considered incidental to the business of banking, so long as the activities do not constitute impermissible merchandising.<sup>207</sup> The factors distinguishing a permissible promotional program from an impermissible merchandising include “the items being sold are small, low-priced items that possess the bank’s logo, the items are sold on a small scale, the items are sold at a nominal mark-up to cover the expense of the promotion, and the items are sold only or mainly to bank customers without any attempt to distribute items on a large scale.”<sup>208</sup> These factors would suggest that a Capital One Café, where only small items such as coffee, tea, and snacks are sold, and discounts are given to Capital One credit and debit cardholders, is permissible under federal banking regulations.

203. Fitzgerald, *supra* note 161; Julie Muhn, *Six Banks Giving their Branches a Shot of Espresso*, FINOVATE (Mar. 18, 2020), <https://finovate.com/six-banks-giving-their-branches-a-shot-of-espresso/> [<https://perma.cc/XL5S-AJ9Y>].

204. Muhn, *supra* note 203.

205. 12 U.S.C. § 36(j) defines the term “branch” as “any branch bank, branch office, branch agency, additional office, or any branch place of business . . . at which deposits are received, or checks paid, or money lent. The term ‘branch’, as used in this section, does not include an automated teller machine or a remote service unit.”

206. *See 9 Things You Can Do at a Capital One Café*, CAPITAL ONE (Oct. 24, 2019), <https://www.capitalone.com/learn-grow/money-management/explore-capital-one-cafes/> [<https://perma.cc/88RV-ZKXU>]; Dan Rafter, *A Bank? A Café? Capital One Asks, How About Both?* RE JOURNALS (Apr. 1, 2017), <https://rejournal.com/a-bank-a-cafe-capital-one-asks-how-about-both/> [<https://perma.cc/RTE4-3ANG>].

207. *See* 12 U.S.C. § 24 (“Upon duly making and filing articles of association and an organization certificate a national banking association shall become, as from the date of the execution of its organization certificate, a body corporate, and as such, and in the name designated in the organization certificate, it shall have power. . . . (Seventh) To exercise by its board of directors or duly authorized officers or agents, subject to law, *all such incidental powers as shall be necessary to carry on the business of banking.* . . .” (emphasis added)); *see also* Letter from Stephen A. Lybarger, Deputy Comptroller for Licensing, OCC, to Lisa Goodglick, Assoc. Gen. Couns., Capital One Fin. Corp., CRA Decision #153: Application to merge ING Bank into Capital One (Aug. 31, 2018), <https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2012/crad153.pdf> [<https://perma.cc/CT2V-AXKA>].

208. *See* Letter from Stephen A. Lybarger, *supra* note 207 (citing OCC, Interpretive Letter No. 690 (Oct. 2, 1995), as reprinted in [1995-1996 Transfer Binder] Fed. Banking L. Rep. (CCH) ¶ 81005).

To be sure, there is a long tradition of banks trying to offer services related to their banking competencies, sometimes over the objections of commercial competitors. Banks had to fight to offer safety deposit boxes to clients.<sup>209</sup> The Supreme Court heard a dispute over whether banks could offer data processing services to their clients.<sup>210</sup> It turned down their request to offer mutual funds to their clients (though we have discussed how their trust subsidiaries can offer CIFs and STIFs).<sup>211</sup> And banks lost a fight against travel agents to sell travel services to their clients.<sup>212</sup> When it comes to commerce, it is fair to say that banks have been cautious—at least since their 1970s efforts to sell plane tickets and investment opportunities to their depositors.<sup>213</sup>

## II. THE TRUST CHARTER AS THE EDGE CASE

Because trust bank charters are one of the oldest breaches of the regulatory perimeter, and one of the most likely vehicles for fintech entryism in the future, this section offers a hornbook-like account of the evolution of the trust charter over time. This exploration of the trust charter's history and current application highlights the evolution of regulatory tools, demonstrates the fluidity of the regulatory boundaries, and underscores the reality of the dual banking system—both state and federal regulators are leveraging the trust charter to address new potential entrants into the banking sector.

In trust banking, financial regulation has a liminal case when it comes to what licensing permits, and what it forbids. Banks have used trust subsidiaries to expand their operations into holding assets owned by their clients and, thereby, take on fiduciary duties—to provide services, in other words, that are different from taking deposits, making loans, and processing payments.<sup>214</sup> But trust banks also have a long tradition of being used to get nonbanks into the business of banking. Trust banks did a great deal of this before the passage of the Federal Reserve Act, and this tradition has continued to today, where trust bank charters have been the vehicle that three fintechs have used to access some of the privileges that bank charter holders enjoy.

Fintech trust charters have revitalized a rather old, and usually quite sleepy, charter that has been extended exclusively to trust banks. Trust banks were always understood to

209. See Michael Waters, *The Quiet Disappearance of the Safe Deposit Box*, THEHUSTLE (Dec. 3, 2022), <https://thehustle.co/the-quiet-disappearance-of-the-safe-deposit-box> [<https://perma.cc/P6PV-L35N>] (noting that competition from home security made it difficult to successfully offer bank boxes to customers).

210. *Ass'n Data Processing Serv. Orgs., Inc. v. Camp*, 397 U.S. 150, 151 (1970).

211. *Inv. Co. Inst. v. Camp*, 401 U.S. 617, 620 (1971).

212. *Arnold Tours, Inc. v. Camp*, 400 U.S. 45, 46 (1970).

213. See Ronald Grzywinski, *The New Old-Fashioned Banking*, HARV. BUS. REV. (May–June 1991), <https://hbr.org/1991/05/the-new-old-fashioned-banking> [<https://perma.cc/8GLQ-W8QG>] (noting that banks began “very cautiously making multifamily loans in the mid-1970s,” and explaining that there was not enough reward for banks to take extra risk in investments).

214. See 12 U.S.C. § 92(a) (“The Comptroller of the Currency shall be authorized and empowered to grant by special permit to national banks applying therefor . . . the right to act as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, or in any other fiduciary capacity . . .”); see, e.g., *Custody Services*, J.P. MORGAN PRIV. BANK, <https://privatebank.jpmorgan.com/gl/en/services/banking/custody-services> [<https://perma.cc/Q9DK-3PED>] (introducing J.P. Morgan’s custody services); *Fiduciary Services*, BNY MELLON WEALTH MGMT., <https://www.bny.com/wealth/global/en/solutions/fiduciary-services.html> (on file with the *Journal of Corporation Law*) (introducing the world’s largest custodian bank and asset servicing company, BNY Mellon’s fiduciary services).



be banks, but they did not engage in the classic bank business of taking deposits, making loans, and processing payments.<sup>215</sup> Instead, trust banks provided fiduciary services to their clients, usually custodial services.<sup>216</sup> Rather than taking a deposit and using that deposit to make a loan, trust banks took collateral, and held onto it for a fee.<sup>217</sup> That means they did not do the conventional banking “maturity mismatch” trade of using the collateral as an asset that could be lent out.<sup>218</sup> Whereas regular banks engage with their clients at arms-length, pursuing a profit in their dealing with them, trust banks are obliged to put the interests of their clients ahead of their own interests, and make money by charging for this commitment.<sup>219</sup>

Custodial services have long been a part of the common law, with some of the earliest English property cases being about bailments and bailees.<sup>220</sup> Moreover, finding a safe place to keep financial assets has long been one of the yearned for offerings of modern business.<sup>221</sup> Trust banks theoretically offer this sort of safe storage.

This trust charter is a flexible mechanism meant to alleviate some of the problems posed by a strict separation of banking and commerce. The OCC in 2020–21 gave three cryptocurrency brokers trust bank charters that they could use to reassure their clients on custody and perhaps even more importantly, to access the payment rails over which banks enjoy a regulatory monopoly.<sup>222</sup>

This sort of disruption is all but a tradition of the trust banks. Trust charters granted by the OCC have been one of the principal ways that nonbanks have gotten involved in the

215. OCC, COMPTROLLER’S LICENSING MANUAL: CHARTERS 56 (2021), <https://www.occ.gov/publications-and-resources/publications/comptrollers-licensing-manual/files/charters.pdf> [<https://perma.cc/QL5T-BTHT>].

216. *Id.*; see Jonathan Macey, *Reputation the Way It Used to Be*, 87 BUS. HIST. REV. 634, 635 (2013) (“Bankers Trust’s initial business was serving as trustee and managing investments held by clients in trust.”).

217. Macey, *supra* note 216, at 635.

218. As Jonathan Macey has explained, “[m]aturity mismatch refers to the fact that banks’ liabilities are very short term, again in the form of CDs, savings accounts, and demand deposits, whereas their assets are long term in duration.” Jonathan Macey, *Error and Regulatory Risk in Financial Institution Regulation*, 25 SUP. CT. ECON. REV. 155, 179 (2017).

219. The National Banking Act provides that:

The Comptroller of the Currency shall be authorized and empowered to grant by special permit to national banks applying therefor, when not in contravention of State or local law, the right to act as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, or 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.

12 U.S.C. § 92(a).

220. Samuel Stoljar, *The Early History of Bailment*, 1 AM. J. LEGAL HIST. 5, 5 (1957) (“The classic and central problem in medieval law was the bailee’s liability to his bailor for a chattel delivered to his care and his possession.”).

221. Gary Gorton, *The History and Economics of Safe Assets*, 9 ANN. REV. ECON. 547, 547 (2017) (“Much of human history can be written in terms of the search for and production of safe assets.”).

222. See Nikhilesh De, *Paxos Becomes Third Federally Regulated Crypto ‘Bank’*, COINDESK (Sept. 14, 2021), <https://www.coindesk.com/markets/2021/04/23/paxos-becomes-third-federally-regulated-crypto-bank/> [<https://perma.cc/KWG2-YCFG>] (“The national bank regulator announced Friday it has granted Paxos a preliminary charter, letting the firm bring its new Paxos National Trust entity online as a federally regulated entity offering custody services, stablecoin management, payment, exchange and other services.”).

business of banking. The OCC has given trust charters to asset managers, payroll processors, and even to a small college.<sup>223</sup> In this way, the trust charter sits on the very margin of the separation of banking and commerce and is a conduit for banks to expand their business beyond the traditional forms of banking, and for commercial firms to dip a toe in waters otherwise forbidden to them. The trust charter accordingly makes for an excellent case study on the increasingly important question of what licenses in the modern administrative state should do as a matter of both law and policy.

#### A. Trust Charters for Fintechs: State Efforts

Wyoming and New York have led the way in chartering financial technology firms as trusts. Wyoming has developed a special-purpose depository institution (SPDI) charter for cryptocurrency custodial banks.<sup>224</sup> These trusts cannot make loans with customer deposits, and must at all times maintain reserves of high-quality liquid assets against 100% or more of their depository liabilities.<sup>225</sup> This both makes the Wyoming SPDI different from a typical bank, which finances lending with customer deposits—“borrow[] short to lend[] long” is almost a definition of conventional banking—and different from depository institutions that must protect their deposits with insurance.<sup>226</sup>

Wyoming has taken the view that the 100% reserve requirement means that its institutions should not be obligated to obtain deposit insurance from the FDIC, because there is no risk of a shortfall in asset values that would imperil the ability of an SPDI to immediately return any and all deposits to its clients.<sup>227</sup> “Wyoming’s SPDIs are subject to a straightjacket: They cannot rehypothecate customer assets, even if a customer wants them to, said Caitlin Long, founder and CEO of Custodia, a Wyoming SPDI.<sup>228</sup> She claimed that “Wyoming’s charter is hyperfocused on solvency and is the polar opposite of Wall Street’s highly leveraged, highly rehypothecated regime.”<sup>229</sup>

In the fall of 2020, the state awarded SPDI charters to Kraken Financial, a crypto trading venue, and Avanti Financial (now Custodia), a similar kind of firm.<sup>230</sup> Those firms

223. See *infra* Part II.B.

224. *Special Purpose Depository Institutions*, WYO. DIV. BANKING, <https://wyomingbankingdivision.wyo.gov/banks-and-trust-companies/special-purpose-depository-institutions> [<https://perma.cc/93DG-HFYQ>].

225. *Id.*

226. Banks “borrow[] short, and lend[] long.” Franklin R. Edwards & Frederic S. Mishkin, *The Decline of Traditional Banking: Implications for Financial Stability and Regulatory Policy*, 1 FED. RSRV. BANK N.Y. ECON. POL’Y REV., no. 2, July 1995, at 27, 27.

227. *Special Purpose Depository Institutions*, *supra* note 224.

228. Penny Crosman, *States Take Lead on Crypto Bank Charters and Digital Asset Rules*, AM. BANKER (Oct. 18, 2021), <https://www.americanbanker.com/news/states-take-lead-on-crypto-bank-charters-and-digital-asset-rules> [<https://perma.cc/9R2T-WT85>].

229. *Id.*

230. Nate DiCamillo, *Avanti Financial Joins Kraken as a Wyoming-Approved Crypto Bank*, COINDESK (Oct 28, 2020), <https://www.coindesk.com/business/2020/10/28/avanti-financial-joins-kraken-as-a-wyoming-approved-crypto-bank/> [<https://perma.cc/266W-DBAA>] (“Avanti Financial’s banking charter was approved unanimously by the Wyoming State Banking Board on Wednesday, becoming the second newly chartered bank in the state in 2020 after Kraken Financial earned approval last month.”).

have, in turn, sought access to the Fed’s payment system, as state-chartered financial institutions, on the basis that, unconventional though they were, they posed no risk to their counterparties.<sup>231</sup>

Custodia applied for an account at the Kansas City Federal Reserve Bank that would have entitled it to join the banking payment system overseen by that agency.<sup>232</sup> It sued the Fed and its Kansas City affiliate on the basis that its two-year-old application for the account was unreasonably delayed.<sup>233</sup> The Fed then announced new guidance on how it would create master account applications—it created three categories of financial institutions: banks regulated by the national banking regulators, presumptively entitled to charters, bank-like entities like Fannie Mae, who would receive more scrutiny, and all others, who received the most scrutiny.<sup>234</sup> Custodia, which fit into that last category was ultimately denied access to a master account.<sup>235</sup> The denial meant more litigation for the Fed and a blow to Custodia’s business model.<sup>236</sup>

New York has used its own trust charter regime, along with a special money transmitter license for online ventures, to encourage fintechs to charter in the state. The fintechs are taking advantage of a law of some tenure, as well as a new one. Limited purpose trust company charters were first instituted in New York State in 1971.<sup>237</sup> These charters are similar to bank charters except that the minimum capitalization threshold is higher and that there is no requirement of FDIC insurance.<sup>238</sup> In return such companies may not hold deposits nor make loans “except as incidental to the exercise of fiduciary powers.”<sup>239</sup>

The capitalization requirements as articulated by the New York Department of Financial Services are light. They require only that, “[t]he initial capitalization must be in an amount deemed satisfactory to the Superintendent of Financial Services but in no event shall such amount be less than \$2 million in Tier 1 capital.”<sup>240</sup>

231. Andrew Ackerman, *Crypto Firms Want Fed Payment Systems Access—and Banks Are Resisting*, WALL ST. J. (Aug. 28, 2021), <https://www.wsj.com/articles/crypto-firms-want-fed-payment-systems-accessand-banks-are-resisting-11630143002> (on file with the *Journal of Corporation Law*) (“Avanti and Kraken, which both have ‘special purpose’ bank charters in Wyoming, say they have all the same compliance, controls and supervisory requirements of traditional banks.”).

232. Crystal Kim, *Fed Pushback Won’t Stop Custodia’s Lawsuit Over Master Account*, AXIOS (Jan. 27, 2023), <https://www.axios.com/2023/01/27/fed-pushback-custodia-bank-lawsuit-master-account> [<https://perma.cc/G559-3TF2>] (“The U.S. Federal Reserve denied Wyoming-chartered Custodia Bank’s application to be a member of the Federal Reserve System . . .”).

233. *Custodia Bank Inc. v. Fed. Rsrv. Bd. of Governors*, 640 F.Supp. 3d 1169, 1177 (D. Wyo. 2022).

234. Guidelines for Evaluating Account and Services Requests, 87 Fed. Reg. 51099, 51100–01 (Aug. 19, 2022), <https://www.federalreserve.gov/newsevents/pressreleases/files/other20220815a1.pdf> [<https://perma.cc/SB6X-EZEK>].

235. *Custodia Bank, Inc.*, FRB Order No. 2023-02 (Fed. Rsrv. Sys. Jan. 27, 2023), <https://www.federalreserve.gov/newsevents/pressreleases/files/orders20230324a1.pdf> [<https://perma.cc/Q3EV-BEWT>] (order denying application for membership).

236. For a discussion of the Custodia application, see Julie Andersen Hill, *Opening A Federal Reserve Account*, 40 YALE J. ON REG. 453, 481 (2023).

237. *Organization of a Limited Purpose Trust Company*, N.Y. DEPT. OF FIN. SERVS., [https://www.dfs.ny.gov/apps\\_and\\_licensing/banks\\_and\\_trusts/procedure\\_certificate\\_merit\\_trust\\_comp](https://www.dfs.ny.gov/apps_and_licensing/banks_and_trusts/procedure_certificate_merit_trust_comp) [[https://web.archive.org/web/20200803125220/https://www.dfs.ny.gov/apps\\_and\\_licensing/banks\\_and\\_trusts/procedure\\_certificate\\_merit\\_trust\\_comp](https://web.archive.org/web/20200803125220/https://www.dfs.ny.gov/apps_and_licensing/banks_and_trusts/procedure_certificate_merit_trust_comp)].

238. *Id.*

239. *Id.*

240. *Id.*

The nexus of this limited purpose trust charter and fintechs, in particular virtual currency holders, is that New York State offers two routes for virtual currency holders to obtain the license required from NYDFS in order to engage in “Virtual Currency Business Activity.”<sup>241</sup> Such activities are defined as:

Receiving Virtual Currency for Transmission or Transmitting Virtual Currency, except where the transaction is undertaken for non-financial purposes and does not involve the transfer of more than a nominal amount of Virtual Currency; (2) storing, holding, or maintaining custody or control of Virtual Currency on behalf of others; (3) buying and selling Virtual Currency as a customer business; (4) performing Exchange Services as a customer business; or (5) controlling, administering, or issuing a Virtual Currency. The development and dissemination of software in and of itself does not constitute Virtual Currency Business Activity.<sup>242</sup>

One is to obtain a so-called BitLicense and the other is through having a limited-purpose trust charter.<sup>243</sup> There are differences between the rights and requirements of these two regimes. Companies with limited-purpose charters have additional regulatory requirements.<sup>244</sup> However, such companies also have fiduciary powers that allow them to manage their clients’ assets.<sup>245</sup> Moreover, a trust company does not need a separate money transmitter license as it has the authority conferred by such license automatically as a trust company.<sup>246</sup> As of December 2024, there were 34 NYDFS-chartered virtual currency companies and of those, 12 have limited purpose trust company charters.<sup>247</sup> These include some notable companies, such as Coinbase, PayPal, Fidelity, Robinhood Crypto, and Paxos Trust Company.<sup>248</sup>

The so-called BitLicense has accordingly represented an expansion of New York’s licensing regime. BitLicense holders are nonbanks providing financial services over the internet, and New York’s regime is hosting the kind of companies that otherwise might choose to apply for a fintech charter offered by the OCC.<sup>249</sup>

The ability of these firms to access the payment system has become controversial. The payment rails used to be only the province of banks, but the Fed has recently dipped its toes into offering some nonbanks access to those rails.<sup>250</sup> It had already granted access to

241. N.Y. COMP. CODES R. & REGS. tit. 23 § 200.3 (2024).

242. *Id.* § 200.2(q).

243. *Id.* § 200.3(c)(1).

244. *Virtual Currency Businesses – Licensing and Resources*, N.Y. DEPT. OF FIN. SERV., [https://www.dfs.ny.gov/virtual\\_currency\\_businesses](https://www.dfs.ny.gov/virtual_currency_businesses) [<https://perma.cc/MCX3-9WHS>].

245. *Id.*

246. *Id.*

247. *Id.*

248. *Id.*

249. For a discussion of the New York regime, see *Organization of a Limited Purpose Trust Company*, *supra* note 237.

250. Pete Schroeder, *U.S. Fed Proposes Tiered System to Review Master Account Applications*, REUTERS (Mar. 1, 2022), <https://www.reuters.com/business/finance/us-fed-proposes-tiered-system-reviewing-master-account-applications-2022-03-01/> (on file with the *Journal of Corporation Law*).

the government-owned mortgage giants Fannie Mae and Freddie Mac.<sup>251</sup> One fintech has also obtained access to the system.<sup>252</sup>

Prior to the Federal Reserve Act, states and territories had exclusive power to authorize banks to engage in trust activities.<sup>253</sup> The story of the state trusts is a story of consistent efforts to take on more financial activities than a business offering custody of assets would permit. States first granted trust powers to insurance companies, and for some time, the trust and insurance businesses were “regarded as the same class of operations.”<sup>254</sup> Insurance companies have always been expected to offer policyholders fiduciary assurances.<sup>255</sup> They must segregate premiums they receive from those policyholders into separate accounts and invest the proceeds from those accounts in the best interest of their policyholders, rather than in the interest of the insurer.<sup>256</sup> They may be described, then, not as the owners of policy premium funds, but rather as the custodians or trustees of those funds.<sup>257</sup>

In 1822, New York granted the first trust charter to Farmers’ Fire Insurance and Loan Company, empowering it to execute all lawful trusts.<sup>258</sup> New York also granted trust powers to the New York Life Insurance and Trust Company in 1830; Pennsylvania first granted trust powers to the Pennsylvania Company for Insurance on Lives and Granting Annuities in 1836; and Massachusetts first granted trust powers to the New England Trust Company in 1869.<sup>259</sup> In 1887, New York passed the Trust Companies Act, providing a general law, as opposed to a special charter, for trust formation; the law moved trust chartering out of the legislature and towards something like a licensing regime per the modern corporate form.<sup>260</sup> The law resulted in a proliferation of incorporations, with subsequent amendments placing banks and trusts on an even playing field, creating, for example, equal tax rates for both institutions, allowing trusts to engage in banking, *i.e.*, accept deposits, and removing any restrictions regarding investments or reserve deposits.<sup>261</sup>

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251. *Id.*

252. Editorial Bd., *Sarah Bloom Raskin’s Revolving Door*, WALL ST. J. (Feb. 9, 2022), <https://www.wsj.com/articles/sarah-bloom-raskins-revolving-door-reserve-trust-company-federal-reserve-11644339172> (on file with the *Journal of Corporation Law*) (“Reserve Trust engages in payment processing and other services for business-to-business payment companies. Its website boasts that in 2018 it ‘became the first state chartered trust company to obtain a Federal Reserve master account, granting direct access to Federal Reserve clearing, payment, and settlement services.’ It also appears to be the only nonbank fintech company to have received access to the Fed payment system.”).

253. GEORGE E. BARNETT, STATE BANKS AND TRUST COMPANIES SINCE THE PASSAGE OF THE NATIONAL-BANK ACT, NAT’L MONETARY COMM’N, S. Doc. No. 659, at 12 (61st Cong., 3d Sess. 1911).

254. GEORGE CATOR, TRUST COMPANIES IN THE UNITED STATES 12 (1902).

255. Comment, *The Relationship Between a Life Insurance Company and a Policy Holder*, 48 YALE L.J. 839, 844 (1939) (“Under a trust analysis, the company as the fiduciary of the insured would . . . be . . . bound to act in the insured’s best interest.”).

256. M. T. Van Hecke, *Insurance Trusts—The Insurer as Trustee*, 7 N.C. L. REV. 21, 23 (1928).

257. BARNETT, *supra* note 253, at 12.

258. *Id.* at 14; Frederick Kilburn, *The Government in its Relation to Industry*, 24 ANNALS AM. ACAD. POL. & SOC. SCI. 29, 30 (1904).

259. BARNETT, *supra* note 253, at 14–18; Sharon Ann Murphy, *Selecting Risks in an Anonymous World: The Agency System for Life Insurance in Antebellum America*, 82 BUS. HIST. REV. 1, 1 (2008).

260. BARNETT, *supra* note 253, at 15; H. Peers Brewer, *The Emergence of the Trust Company in New York City: 1870–1900*, 3 PROC. BUS. HIST. CONF. 193, 195 (1975).

261. Brewer, *supra* note 260, at 196; *see generally* BARNETT, *supra* note 253 at 15 (describing general direction of state banking law after the National Bank Act).

The pressure to move trusts into banking activities apart from custody has a lengthy tenure. Although state legislatures initially chartered trusts for the single purpose of acting as trustees, trusts, “in some states, developed their banking departments outside of their recognized powers under the law.”<sup>262</sup> Many trusts began to engage in activities whose legality under its charter and the law was subject to different interpretations.<sup>263</sup> Moreover, trusts could, “by some change in the method of doing the kind of banking business in question . . . bring it within the powers actually conferred.”<sup>264</sup>

Under the New York trust statute, for example, trust banks could accept “any and all such trusts and powers of whatever nature or description as may be conferred upon or entrusted or committed to it by any person or persons.”<sup>265</sup> Trusts argued that such sweeping language allowed them to receive and loan deposits, encroaching on ordinary deposit banks’ business.<sup>266</sup>

By 1899, in New York, trust companies held as deposits in trust \$261 million while holding as general deposits \$332 million.<sup>267</sup> In Missouri, after the state’s Supreme Court held that trusts could not accept deposits payable by check on which no interest was paid, trusts began accepting demand deposits, paying a nominal rate to circumvent regulation.<sup>268</sup> In Pennsylvania, the state legislature recognized trusts’ banking powers gradually—giving title insurance companies with at least \$250,000 in capital trust and fidelity-insurance powers in 1881, the power to receive deposits of every description for safe-keeping in 1885, and finally “the power to ‘receive deposits of money and any other personal property and to issue their obligations therefore . . . and to loan money on real and personal securities’” in 1895.<sup>269</sup>

The growth of state trust banks was not an unmitigated good, however. Trust banks have triggered larger runs in the banking sector. The 1907 financial crisis began with the Knickerbocker Trust, expanded to other New York trust banks, and rippled into the larger banking sector.<sup>270</sup> The panic was only stopped once the epitome of a traditional banker, J.P. Morgan, arranged a rescue for the trusts, and the close-run nature of the crisis led, many believe, to the creation of the Federal Reserve System.<sup>271</sup>

### B. Enter The Feds

Prior to the Federal Reserve Act’s ratification in 1913, national banks could not offer fiduciary services to their clients.<sup>272</sup> Trust companies arose to address this need. The turn

262. CATOR, *supra* note 254, at 40.

263. *Id.* at 40–41.

264. BARNETT, *supra* note 253, at 16.

265. Alexander D. Noyes, *The Trust Companies: Is There Danger in the System?*, 16 POL. SCI. Q. 248, 252 (1901).

266. *Id.*

267. *Id.*

268. CATOR, *supra* note 254, at 40.

269. BARNETT, *supra* note 253, at 17.

270. O.M.W. SPRAGUE, HISTORY OF CRISES UNDER THE NATIONAL BANKING SYSTEM, S. Doc. No. 538, at 230–35 (61st Cong. 2d Sess. 1910). Jon R. Moen & Ellis W. Tallman, *The Panic of 1907*, FED. RSRV. HIST. (Dec. 15, 2015), <https://www.federalreservehistory.org/essays/panic-of-1907> [<https://perma.cc/2PFG-8Y3L>].

271. Moen & Tallman, *supra* note 270; Jenny Wahl, *Give Lincoln Credit: How Paying for the Civil War Transformed the United States Financial System*, 3 ALB. GOV’T L. REV. 700, 740 (2010).

272. Albert Léviitt, *The Trust Powers of National Banks*, 77 U. PA. L. REV. 835, 835 (1929).

of the century commentator George Cator distinguished them from the industrial and commodities trusts that the federal government was beginning to break up: “[a] trust or combine conducts business solely on its own account, whereas a trust company . . . manages the property of others.”<sup>273</sup>

Under the National Bank Act of 1864, national banks could not engage in trust activities or securities underwriting.<sup>274</sup> The model was a modest narrow banking idea, designed not to unsettle already existing quasi-bank services offered by the state banking sector.<sup>275</sup> Under the leadership of Senator Nelson Aldrich, the National Monetary Commission, established in 1908 in response to the Panic of 1907, proposed several new classes of national banks.<sup>276</sup> Among them was the national trust company, which was to exercise “all the functions and have all the privileges, including length of charter, which are given to trust companies by the laws of the states.”<sup>277</sup>

Getting a national trust charter requires an application to the OCC. The agency divides its chartering process into four stages; the most important stage is the prefiling stage.<sup>278</sup> During that part of the process applicants can interact with the agency’s licensing officials.<sup>279</sup> By the end of the prefiling review, applicants should be well informed about whether their application will be granted if filed and will have had a chance to correct deficiencies that would prevent the grant from being realized. The filing, review, and evaluation phases then lead to a final decision about the charter application.<sup>280</sup>

The agency announced in 2018 that it would be willing to provide a special charter for financial technology firms that did not take deposits.<sup>281</sup> Controversy and litigation has surrounded this step, meaning that the agency, despite apparent interest from financial technology firms, has not yet received an application for fintech charter.<sup>282</sup> Its legal authority to offer the fintech charter, however, has been challenged.<sup>283</sup> Instead, financial technology firms have either obtained conventional banking charters, either through a so-called *de novo* application, by merging with a charter-holding national bank, or through the trust charter.<sup>284</sup> The firms that have obtained trust charters through one of these means represent a real assortment of businesses. Some can be categorized as asset managers, others as national banks that want to create a trust affiliate, and still others as nonbanks that want to

273. CATOR, *supra* note 254, at 10.

274. National Bank Act of 1864, 12 U.S.C. § 24.

275. Off. of the Comptroller of the Currency, Interpretive Letter No. 525 Concerning Certain of the Trust Interpretations by the OCC Relating to Investments by National Bank Trustees of Trust Assets in Mutual Funds for Which the Same Bank Serves as Investment Advisor (Aug. 8, 1990) (observing that “national banks did not acquire trust powers until” the passage of the Federal Reserve Act).

276. See SUGGESTED PLAN FOR MONETARY LEGISLATION, S. Doc. No. 61-784, at 17 (1911) (“Another class of national banks shall be authorized, which shall be in effect national trust companies, to be designated by some appropriate name and to exercise all the functions and have all the privileges, including length of charter, which are given to trust companies by the laws of the various States.”).

277. *Id.*

278. OCC, *supra* note 215, at 33–37.

279. *Id.* at 33.

280. *Id.* at 41.

281. *Lacewell v. OCC*, 999 F.3d 130, 137 (2d Cir. 2021).

282. See *id.* at 139 (discussing the lack of such charters for the purposes of standing analysis).

283. *Id.* at 134.

284. See *supra* Part I.E.

hold custody of assets.<sup>285</sup> The latter group includes payroll processors and even a college.<sup>286</sup> The nonbank asset managers are largely investment banks or investment advisors who wish to provide fiduciary services to their clients. The national banks that have obtained national trust charters for their affiliates tend to be small.

These diverse projects indicated how trusts can be a way for nonbanks to enter into some portions of the business of banking—payroll managers, wealth managers, and colleges would never be able to comply with the capital requirements faced by ordinary banks; as trust banks, they do not have to do so. Trust subsidiaries of the nonbank businesses were constrained from taking deposits, and the one trust bank that did seek to create two deposit sweep programs, one for retirement accounts and one from non-retirement accounts, that would sweep any cash balances in an affiliated securities brokerage into a wealth manager was required to apply for deposit insurance with the FDIC.<sup>287</sup>

Although trust operations of national banks and nonbanks might be relatively small as a general matter, the thin requirement of tier 1 capital is remarkable. The trust affiliate of Goldman Sachs, for example only needed to hold \$3 million in tier 1 capital; the parent company needs to hold, as of 2020, \$94.3 billion of tier 1 capital.<sup>288</sup> The number of full-service national banks with less than \$10 million of tier 1 capital in the United States is tiny.<sup>289</sup> The modest capital requirements are due to the fact that trusts do not lend out their deposits.

In January 2021, the agency announced that it would expand the powers of the trusts in Interpretive Letter 1176.<sup>290</sup> Specifically, it indicated that the agency would interpret the definition of fiduciary capacity under 12 U.S.C. § 92a to include activities performed in a fiduciary capacity according to state law.<sup>291</sup> The OCC may charter a national bank that limits its operations “to those of a trust company and activities related thereto.”<sup>292</sup> According to the letter, a trust’s activities include fiduciary activities under either federal or state law, superseding OCC’s previous interpretation, which first looked to 92(a) to determine

285. See Grant F. Butler & Robert M. Tammero, Jr., *The Trust Company — An Old Tool For A New Age*, REUTERS (July 22, 2022), <https://www.reuters.com/legal/transactional/trust-company-an-old-tool-new-age-2022-07-22/> (on file with the *Journal of Corporation Law*) (discussing “renewed interest in the trust company charter among financial institutions, asset managers, and fintechs”).

286. *Wheaton College Trust Company*, WHEATON COLL., <https://www.wheaton.edu/giving/gift-planning/wheaton-college-trust-company/> [<https://perma.cc/9869-FBZL>] (discussing how the college uses its trust charter to process and hold on to donations).

287. Letter from Sandya Reddy, Acting Director for District Licensing, OCC, to Zachary A. Abeles, General Counsel, Stifel Trust Company, Conditional Approval #1235: Application by Stifel Trust Company for a Substantial Asset Change (Feb. 14, 2020) (requiring that the wealth manager “shall not begin engaging in the Deposit Sweep Programs until [it] obtains deposit insurance from the FDIC”).

288. GOLDMAN SACHS GRP., INC., PILLAR 3 DISCLOSURES FOR THE PERIOD ENDED MARCH 31, 2021 5 (2021), <https://www.goldmansachs.com/investor-relations/financials/other-information/2021/1q-pillar3-2021.pdf> [<https://perma.cc/73AL-URXY>].

289. *Banks Ranked by Tier 1 (Core) Risk-Based Capital*, US BANK LOCATIONS (June 30, 2021), <https://www.usbanklocations.com/bank-rank/tier-1-core-risk-based-capital.html?d=2021-06-30> [<https://perma.cc/BH26-HA8B>].

290. OCC, Interpretive Letter No. 1176 OCC Chief Counsel’s Interpretation on National Trust Banks 1 (Jan. 11, 2021) [hereinafter Interpretive Letter No. 1176].

291. *Id.*

292. *Id.* (citing 12 U.S.C. § 27(a)).



whether an activity was fiduciary.<sup>293</sup> The critical development was that under state law, trusts often can offer non-fiduciary activities, “such as non-fiduciary custody,” a service of real interest to holders of cryptocurrency.<sup>294</sup>

The Interpretive Letter also confirmed that banks may engage in activities incidental to the business of banking under 12 U.S.C. § 24 (Seventh).<sup>295</sup> The OCC looks at whether the activity is a functional equivalent to, or a logical outgrowth of, a recognized banking activity; whether the activity strengthens the bank by benefiting its customers or its business; whether the activity involves risks similar in nature to those already assumed by banks; and whether the activity is authorized by state-chartered banks.<sup>296</sup> One law firm has suggested that the letter means that a national trust bank acting in a fiduciary capacity may engage in traditional banking activities such as lending.<sup>297</sup>

The letter thus establishes that the OCC may charter a national bank that limits its activities to (1) those permitted under 12 U.S.C. §§ 92(a), 12 C.F.R. § 9.2(e), and 24 (Seventh) and (2) to those permitted under state law for a state trust bank.<sup>298</sup>

On January 13, 2021, in accordance with Interpretive Letter 1176 and under 12 U.S.C. § 35, the OCC granted the fintech Anchorage Trust’s conversion from a South Dakota trust company to a national trust, citing the fact that Anchorage would continue to perform its activities as prescribed by South Dakota law.<sup>299</sup> Other trust bank applications from fintechs followed, including Protego Trust Company’s conversion from a state bank charter to a national trust,<sup>300</sup> and Paxos National Trust—which received approval for a de novo trust from the Office of the Comptroller of the Currency.<sup>301</sup>

All three companies proposed to serve as custodians for cryptocurrency wallet holders and are affiliated with—or at least hope to be affiliated with—cryptocurrency trading venues.<sup>302</sup> Paxos is the most established one, with 184 employees, and sponsors including

293. Compare *id.*, with OCC, Interpretive Letter No. 265 Certain Real Estate Activities of Bank Trust Department Exceeds Bank’s Authority to Act as Fiduciary (1983) as reprinted in [1983-1984 Transfer Binder] Fed. Banking L. Rep. (CCP) ¶ 85429 (overturning the prior interpretive letter that concluded that the OCC will look to state law to determine whether a fiduciary capacity is permissible only after it is deemed permissible under 12 U.S.C. § 92(a)).

294. Interpretive Letter No. 1176, *supra* note 290, at 2.

295. *Id.* at 5.

296. *Id.* at 5–6 (citing 12 C.F.R. § 7.5001(c)(1)).

297. *Virtual Currency/Fintech Update: OCC Approves Anchorage Trust’s Charter Conversion and Expands the General Fiduciary Powers of National Banks*, GIBSON DUNN (Jan. 25, 2021), <https://www.gibsondunn.com/virtual-currency-fintech-update-occ-approves-anchorage-trusts-charter-conversion-and-expands-the-general-fiduciary-powers-of-national-banks/> [<https://perma.cc/JH5N-JHZ5>].

298. *Id.*

299. News Release, OCC, OCC Conditionally Approves Conversion of Anchorage Digital Bank (Jan. 13, 2021), <https://www.occ.gov/news-issuances/news-releases/2021/nr-occ-2021-6.html> [<https://perma.cc/A2NY-PYJS>].

300. News Release, OCC, OCC Conditionally Approves Conversion of Protego Trust Bank (Feb. 5, 2021), <https://www.occ.gov/news-issuances/news-releases/2021/nr-occ-2021-19.html> [<https://perma.cc/76K7-LQFJ>].

301. News Release, OCC, OCC Conditionally Approves Chartering of Paxos National Trust (Apr. 23, 2021), <https://www.occ.gov/news-issuances/news-releases/2021/nr-occ-2021-49.html> [<https://perma.cc/T8XS-ZLJU>].

302. See *Citadel, Schwab Backed EDX Markets Selects Anchorage for Digital Asset Custody*, LEDGER INSIGHTS (Aug. 22, 2023), <https://www.ledgerinsights.com/edx-markets-anchorage-digital-asset-custody/> [<https://perma.cc/4H37-8LRP>] (discussing Anchorage Digital’s role as a custodian for cryptocurrency trading platforms); Nick Robnett, *Crypto 101: What is Crypto Custody?*, PAXOS BLOG (Nov. 17, 2021),

PayPal.<sup>303</sup> The latter firm serves as a partner to Paxos by offering the firm as a place for PayPal clients to keep their crypto assets.<sup>304</sup> Paxos has introduced a virtual currency backed by gold and two stablecoins meant to track the dollar.<sup>305</sup> The result has benefited one of Paxos's most important projects—its “stablecoins” that make it easier for crypto holders to trade with one another.<sup>306</sup> Paxos has partnered with the well-established cryptocurrency exchange Binance to create BUSD, another stablecoin tracking the US dollar and also meant to make it easier for clients to make cryptocurrency trades.<sup>307</sup> One of Paxos' most volatile stablecoins smoothed out once its charter was conditionally approved, as Figure 1, below, taken from CoinMarketCap, shows.<sup>308</sup> As of April 29, 2021, the firm was valued at \$2.4 billion and raised \$300 million in a series D funding round.<sup>309</sup>

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<https://paxos.com/2021/11/17/crypto-101-what-is-crypto-custody/> [<https://perma.cc/LR4C-KT9M>] (explaining how Paxos provides custody solutions for crypto assets using cold and hot wallets and works with trading platforms, such as PayPal's stablecoin project); Will Gottsegen, *Crypto Firm Protego Gets Approval for Federal Bank Charter*, DECRYPT (Feb. 5, 2021), <https://decrypt.co/56766/protego-federal-charter-crypto-bank> [<https://perma.cc/2BVC-XAWS>] (discussing Protego's approval for a federal bank charter by the OCC, enabling it to serve as a custodian for digital assets and offer cryptocurrency-related services).

303. Charles Cascarilla, *PayPal & Paxos Bring Crypto to Millions of Users*, PAXOS BLOG (Oct. 21, 2020), <https://paxos.com/2020/10/21/paypal-paxos-bring-crypto-to-millions-of-users/> [<https://perma.cc/P23S-HFBY>].

304. *Id.*

305. See Walter Hessert, *PAX Gold: The First Gold Token with More Than \$100 Million in Market Cap*, PAXOS BLOG (Jan. 21, 2021), <https://paxos.com/2021/01/21/pax-gold-the-first-gold-token-with-more-than-100-million-in-market-cap/> [<https://perma.cc/XD7B-2CPP>] (discussing PAX Gold as the first regulated digital asset backed by physical gold); *What Stablecoins Does Paxos Power?*, PAXOS, <https://paxos.com/2023/08/07/what-stablecoins-does-paxos-power/> [<https://perma.cc/4T42-UQC7>] (“Paxos powers industry-leading stablecoins: Pax Dollar (USDP) and PayPal USD (PYUSD). Each token is backed 1:1 by the US dollar and Paxos custodies all of the dollar reserves backing each of these tokens in US Treasury bills and FDIC-insured US banks.”).

306. *Rise in Stablecoin Use Inspires Greater Financial Connectivity*, PAXOS BLOG (Sept. 23, 2022), <https://paxos.com/2022/09/23/rise-in-stablecoin-use-inspires-greater-financial-connectivity/> [<https://perma.cc/Q2AT-6Q6B>] (discussing stablecoins as a bridge between traditional finance and cryptocurrency, their use in peer-to-peer transactions and the benefits of regulated stablecoins for enhancing global financial connectivity).

307. Press Release, Paxos, *Binance Partners with Paxos to Launch USD-Backed Stablecoin ‘BUSD’* (Sept. 4, 2019), <https://paxos.com/2019/09/04/binance-partners-with-paxos-to-launch-usd-backed-stablecoin-busd/> [<https://perma.cc/TU2E-Z7UW>] (announcing the partnership between Paxos and Binance to launch Binance USD (BUSD), a stablecoin fully backed by U.S. dollar reserves and approved by the New York State Department of Financial Services, aimed at making cryptocurrency trades easier by providing a stable, regulated digital asset).

308. *Paxos Standard (PAX)*, COINMARKETCAP, <https://coinmarketcap.com/currencies/paxos-standard/> [<https://web.archive.org/web/20210421062350/https://coinmarketcap.com/currencies/paxos-standard/>].

309. Press Release, Paxos, *Paxos Raises \$300 Million in Series D Funding at \$2.4 Billion Valuation* (Apr. 29, 2021), <https://paxos.com/2021/04/29/paxos-raises-300-million-in-series-d-funding-at-2-4-billion-valuation/> [<https://perma.cc/QKD7-NZG4>].



Anchorage, the first trust fintech chartered by the OCC,<sup>310</sup> also has blue-chip investors, including Visa, Singapore’s sovereign wealth fund, and the well-known Silicon Valley venture capital firm Andreessen Horowitz.<sup>311</sup> It has 145 employees and raised \$80 million in its series C funding round.<sup>312</sup> Anchorage, both through its trust subsidiary and through its brokerage, caters to accredited investors who want crypto exposure.<sup>313</sup>

Protego is the least established of the three trusts, but, like the others, is affiliated with a non-bank holding company that deals in crypto, and that also targets accredited investors.<sup>314</sup> The firm is far less operational than Paxos; it raised \$2 million in seed funding, but raised \$70 million in a first round and targeted a \$2 billion valuation in 2022.<sup>315</sup> *New York Magazine* recently used the company as an example of the difficulties crypto has had with managing regulations.<sup>316</sup> *New York Magazine* summed up the company’s founding:

Protego Trust, founded by a lawyer turned venture capitalist, was betting big that it could be the squeaky-clean, bona fide bank that crypto needed to win Wall

310. Will Gottsegen, *Anchorage Becomes First Federally Chartered Digital Asset Bank*, DECRYPT (Jan. 13, 2021), <https://decrypt.co/54074/anchorage-first-federal-charter-digital-asset-bank> [<https://perma.cc/Q2XE-Y5NV>].

311. Diogo Mónica & Nathan McCauley, *Anchorage Raises \$40 Million Series B Led by Blockchain Capital, Visa*, ANCHORAGE DIGIT. (July 10, 2019), <https://www.anchorage.com/insights/anchorage-raises-40-million-series-b-led-by-blockchain-capital-visa> [<https://perma.cc/2K34-N3DR>].

312. *Anchorage Funding Rounds*, CRUNCHBASE, [https://www.crunchbase.com/search/funding\\_rounds/field/organizations/last\\_funding\\_type/Paxos](https://www.crunchbase.com/search/funding_rounds/field/organizations/last_funding_type/Paxos) (on file with the *Journal of Corporation Law*); Diogo Mónica & Nathan McCauley, *Anchorage Raises \$80 Million Series C to Expand Digital Bank Services*, ANCHORAGE DIGIT. (Feb. 25, 2021), <https://www.anchorage.com/insights/anchorage-raises-80-million-series-c-to-expand-digital-bank-services> [<https://perma.cc/5RQV-69VS>].

313. *Our Story*, ANCHORAGE DIGIT., <https://www.anchorage.com/about> [<https://perma.cc/XZP6-Z9TN>] (“Anchorage Digital is a crypto platform that enables institutions to participate in digital assets through custody, staking, trading, governance, settlement, and the industry’s leading security infrastructure.”).

314. Gottsegen, *supra* note 310.

315. Ryan Weeks, *Protego Trust Bank Targets \$2 Billion Valuation After Quietly Raising \$70 Million*, THE BLOCK (May 23, 2022), <https://www.theblock.co/post/148226/protego-trust-bank-fundraise> [<https://perma.cc/MX99-6BAF>].

316. Jen Wiczner, *Is the Federal Government Trying to Kill Off Crypto?*, N.Y. MAG. (May 1, 2023), <https://nymag.com/intelligencer/2023/05/is-the-federal-government-trying-to-kill-off-crypto.html> [<https://perma.cc/3VKR-U2VX>].

Street’s business. It had spent \$80 million pursuing a coveted approval for a national trust charter, winning conditional approval in 2021. It then raised more than \$100 million—at a reported \$2 billion valuation. . . . But when Protego told the OCC in February that it had completed all of the agency’s requirements for full approval, its application was denied on a technicality—one that the OCC had never mentioned before.<sup>317</sup>

Fintechs see federal preemption of state banking laws as a powerful justification for seeking a national trust charter because it allows nationally chartered banks to circumvent individual state usury and money transmitter laws—a particular concern for firms on the internet, which know no state borders. According to Anchorage, for example, “a national bank charter would preempt existing piecemeal regulatory structure and certain requirements at the state level, eliminating the need to obtain money transfer licenses on a state-by-state basis.”<sup>318</sup> And, according to Paxos, to whom the OCC granted a *de novo* national trust charter on April 23, 2021, “[t]he national charter was designed expressly to allow banks to conduct business across state lines more easily.”<sup>319</sup> One fintech has sought a conventional bank charter. To Figure, “[i]nconsistencies across state licensing creates confusion for Figure applicants and members,” noting that it may not be able to offer the same products to customers in different states.<sup>320</sup>

The OCC, in November 2021, walked back some of the invitations in earlier OCC correspondence to cryptocurrency custody services, stablecoin issuances, participation in crypto verification processes, and the like.<sup>321</sup> The OCC emphasized that it “retains discretion to determine if an applicant’s activities that are considered trust or fiduciary activities under state law are considered trust or fiduciary activities for purposes of applicable federal law.”<sup>322</sup> It emphasized that its chartering authority did not change the powers under national banks that had trust subsidiaries, but the tone suggested that Novo entrants were unlikely to enjoy the willing nature of the agency’s other letters earlier.<sup>323</sup>

This deep dive into the past and present of the trust charter shows how regulatory tools evolve, illustrates the permeability of the regulatory perimeter, and serves as a reminder

317. *See id.* (describing why the charter was denied).

318. Georgia Quinn, *The Best of Both Worlds’: Why Anchorage Seeks a National Trust Charter*, MEDIUM (Dec. 10, 2020), <https://medium.com/anchorage/the-best-of-both-worlds-why-anchorage-seeks-a-national-trust-charter-b0b3fbd88a65> [https://perma.cc/SR4S-4WAK].

319. Anna Hrushka, *Crypto Firm Paxos Gets OCC’s Conditional Approval for Trust Charter*, BANKING DIVE (Dec. 14, 2020), <https://www.bankingdive.com/news/paxos-bitpay-national-bank-charter-OCC/592131/> [https://perma.cc/MWP4-S5TC]; Dan Burstein, *Why Paxos is Seeking a National Trust Bank Charter – and Why We Remain Committed to New York*, PAXOS BLOG (Dec. 9, 2020), <https://www.paxos.com/why-paxos-is-seeking-a-national-trust-bank-charter-and-why-we-remain-committed-to-new-york/> [https://web.archive.org/web/20210615055139/https://paxos.com/why-paxos-is-seeking-a-national-trust-bank-charter-and-why-we-remain-committed-to-new-york/].

320. Mark Cagney, *Why Figure Applied for the US National Bank Charter and What it Means for the Industry*, LINKEDIN (Dec. 1, 2020), <https://www.linkedin.com/pulse/why-figure-applied-us-national-bank-charter-what-means-mike-cagney> [https://perma.cc/D9TX-YQZB].

321. OCC, Interpretive Letter No. 1179 Chief Counsel Interpretation Clarifying: (1) Authority of a Bank to engage in certain Crypto Currency Activities; and (2) Authority of the OCC to Charter a National Trust Bank 5 (Nov. 18, 2021), <https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2021/int1179.pdf> [https://perma.cc/RZ96-ND9J].

322. *Id.*

323. *Id.* at 2.

that the dual banking system is real—state and federal regulators are both using the trust charter to respond to new would-be entrants into banking.

### III. THE LICENSE: PUBLIC INTEREST, PUBLIC CHOICE, AND COMMON LAW

The struggles around the regulatory perimeter allow not just for an analysis of the state of the banking regulatory regime and how it might be adjusted. The evolution of the system allows for reflection on the license as an important but undertheorized tool of administrative law. The two lenses through which academics have viewed licensing regimes are through a public choice and a public interest perspective; the two views are irreconcilable.

#### A. Public Interest

The public interest view takes the perspective that a regulatory scheme is designed to solve a real-world problem, often a problem created by externalities.<sup>324</sup> The three most common ways that licensing can serve these public purposes are to manage scarcity, to ensure that licensees are qualified to offer a service and to use the licensing condition as an opportunity to require licensees to perform other public values.<sup>325</sup> Managing scarcity through licensing explains regimes ranging from the distribution of radio frequencies to hunting licenses. The idea is that if everyone can use a scarce resource as much as they like, people will be incentivized to overuse the resource, and deplete it for everyone—indeed, they will race to do so.<sup>326</sup>

As for ensuring qualifications, in regimes where the licensed activity is dangerous, as in banking, licensing is about limiting participation in the activity to those who can do it safely.<sup>327</sup> Dangerous activities are a part of that class of activities whose costs will be borne by others, while its benefits can be captured by the licensee alone.<sup>328</sup> Those activities are strong candidates for regulation. In banking, the concern is that a bank that takes big risks that do not work out will fail, leaving regulators with an unappetizing choice: let the bank fail, which might lead to a bank run (such a run followed the failure of Lehman Brothers

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324. See Michael E. Levine & Jennifer L. Forrence, *Regulatory Capture, Public Interest, and the Public Agenda: Toward a Synthesis*, 6 J.L. ECON. & ORG. (SPECIAL ISSUE) 167, 168 (1990) (“[W]e can see regulation as the necessary exercise of collective power through government in order to cure ‘market failures,’ to protect the public from . . . effects of externalities.”).

325. See, e.g., *Nat’l Broad. Co. v. United States*, 319 U.S. 190, 227 (1943) (authorizing the FCC to promulgate regulations to encourage more effective use of radio for “public interest, convenience, or necessity”).

326. This is known as the “the tragedy of the commons; each individual is tempted to defect, and enough do so that the resource becomes overwhelmed.” Stuart Minor Benjamin, *Spectrum Abundance and the Choice Between Private and Public Control*, 78 N.Y.U. L. REV. 2007, 2022 (2003).

327. Ryan Nunn, *Eliminating the Anti-Competitive Effects of Occupational Licensing*, BROOKINGS (Jan. 17, 2019), <https://www.brookings.edu/articles/eliminating-the-anti-competitive-effects-of-occupational-licensing/> [https://perma.cc/J9US-DVBX] (acknowledging “there are some occupations in which public health or safety would be endangered by unqualified or unscrupulous practitioners, particularly when the public is not in a good position to distinguish good from bad actors.”).

328. *Id.*

in 2008, leading to a broader financial crisis), or bail it out, which, apart from its unpopularity, encourages more risk-taking by banks that learn that the government will save them if their big bets do not pay off.<sup>329</sup>

In less dangerous licensing regimes, the license is designed to assure consumers that a minimum level of competence will be displayed by licensees who perform services for those consumers. Occupational licensing is the classic example, though, for some occupations, the stakes of the license are so low as to be controversial, about which more in the public choice discussion.<sup>330</sup> It is one thing to only give license to practice law or medicine to people who have been trained in law and medicine.<sup>331</sup> It is quite another to insist on training for cosmetologists or funeral home operators.<sup>332</sup>

Licensing is also an opportunity for the state to implement other values through the licensing criteria. The idea is that the license might be conditioned on some commitment by the licensee to further something that the licensor wants.<sup>333</sup> The evolving regime for the development of dams offers an example, as environmental concerns increasingly occupied Congress. The original hydropower licensing regime in the United States instructed the government to license projects “best adapted to a comprehensive scheme of improvement and utilization for the purposes of navigation, water-power development, and of other beneficial public uses.”<sup>334</sup> In 1986, Congress directed regulators to give “equal consideration” to power and development purposes and “energy conservation, the protection, mitigation of damage to, and enhancement of, fish and wildlife . . . the protection of recreational opportunities, and the preservation of other aspects of environmental quality.”<sup>335</sup>

329. See Vincent Reinhart, *A Year of Living Dangerously: The Management of the Financial Crisis in 2008*, 25 J. ECON. PERSPS. 71, 72 (2011) (arguing that the decision to “let Lehman slip into bankruptcy . . . had widespread consequences” to the financial crisis of 2008); Ran Duchin & Denis Sosyura, *Safer Ratios, Riskier Portfolios: Banks’ Response to Government Aid*, 113 J. FIN. ECON. 1, 3 (2014) (“[T]he bailout may encourage risk taking by protected banks by reducing investors’ monitoring incentives and increasing moral hazard . . .”); see also *U.S. Bank Bailout Encourages Risky Behavior: Watchdog*, REUTERS (Jan. 31, 2010), <https://www.reuters.com/article/us-usa-economy-bailout/u-s-bank-bailout-encourages-risky-behavior-watchdog-idUSTRE60U09L20100131> (on file with the *Journal of Corporation Law*) (“The U.S. taxpayer-funded rescue program set up to save banks from collapse during the financial crisis makes future reckless behavior more likely, the government’s bailout watchdog said in a quarterly report.”).

330. See Chiara Farronato et al., *Consumer Protection in an Online World: An Analysis of Occupational Licensing* 2 (Nat’l Bureau of Econ. Rsch., Working Paper No. 26601, 2020), <https://www.nber.org/papers/w26601> (“[L]icensing may protect consumers from poor service outcomes, guaranteeing at least some minimum standards of quality and safety for consumers . . .”).

331. Though, to be sure, these requirements raise the cost of lawyers and doctors, even if one can assume that patients would be more comfortable seeking medical treatment on the understanding that every doctor they saw had received a particular form of training. Jonathan B. Berk & Jules H. van Binsbergen, *Regulation of Charlatans in High-Skill Professions* 38 (Stanford Univ. Graduate Sch. of Bus., Research Paper No. 17-43, 2019), <https://ssrn.com/abstract=2979134>.

332. These requirements have received some—if not much—in the way of pushback from the courts. See, e.g. *St. Joseph Abbey v. Castille*, 712 F.3d 215, 217–18 (5th Cir. 2013) (refusing to enforce a licensing requirement against monks who built funeral caskets on rational basis review); *Clayton v. Steinagel*, 885 F. Supp. 2d 1212, 1213 (D. Utah 2012) (holding the requirement that hair braiders obtain a cosmetology license unconstitutional for being unrelated to a rational government interest).

333. Farronato et al., *supra* note 330, at 5.

334. Federal Water Power Act, ch. 285, § 10(a), 41 Stat. 1063, 1068 (1920) (current version codified at 16 U.S.C. § 800).

335. 16 U.S.C. § 797 (2005).

These sorts of efforts to promote public values as a condition of licensing exist across the administrative state. Publicly traded manufacturing companies permitted to raise money in the capital markets must report on their use of so-called “conflict minerals” obtained from central Africa.<sup>336</sup> The President issued an executive order directing government agencies to sell off spectrum licenses—a scarcity management form of licensing—to help avoid excessive concentration of spectrum license holdings in the United States, so as to prevent spectrum stockpiling, warehousing of spectrum by licensees, or the creation of barriers to entry,” and thereby prevent monopolization.<sup>337</sup>

The public interest perspective adopts a positive view about what science or experience can bring to a public priority. The idea is that the licensor can determine what the proposed licensee can do to, in exchange for a valuable franchise, further some policy priorities.<sup>338</sup>

### B. Public Choice

The public choice view assumes that licensing regimes exist to create and extract rents.<sup>339</sup> Sometimes, the regulations create barriers to entry for competitors and, therefore, allow licensees to charge high prices and enjoy high profits in the ways that monopolies and oligopolies do. An example of this might be taken from the legal profession itself.<sup>340</sup> High licensing fees and elaborate educational requirements limit the number of lawyers in America, and state bar associations limit legal practice to lawyers who have passed their local bar exam and complied with expensive continuing legal education requirements.<sup>341</sup>

But any licensing regime, by creating a condition precedent before entry into the market, is susceptible to this critique. Hunting licenses mean that hunters enjoy less competition for their prey.<sup>342</sup> Spectrum licenses limit the number of radio stations in any given market, affording opportunities to monopolize advertising revenues.<sup>343</sup> Power plant licenses—sometimes explicitly—create monopolies for the power provider, insulating them

336. See David Zaring, *Financial Reform's Internationalism*, 65 EMORY L.J. 1255, 1276–80 (2016) (discussing conflict mineral monitoring requirement from Dodd-Frank).

337. Exec. Order No. 14036, 86 Fed. Reg. 36987 (July 9, 2021).

338. See Berk & van Binsbergen, *supra* note 331, at 3 (discussing rationale for licensing regimes).

339. See Paul J. Larkin, Jr., *Public Choice Theory and Occupational Licensing*, 38 HARV. J.L. & PUB. POL'Y 209, 229 (2016) (explaining the Public Choice Theory).

340. See Clifford Winston & Quentin Karpilow, *Should the US Eliminate Entry Barriers to the Practice of Law? Perspectives Shaped by Industry Deregulation*, 106 AM. ECON. REV. 171, 171 (2016) (“States’ requirements that lawyers obtain a license to practice law, as well as American Bar Association (ABA) regulations of legal practice, constitute barriers to entry to the legal profession.”).

341. *Id.*

342. Perhaps for this reason, Alaskan officials have begun to “releasing annual hunting licenses by using mathematical models of herd size.” Karen Bradshaw, *Stakeholder Collaboration as an Alternative to Cost-Benefit Analysis*, 2019 BYU L. REV. 655, 664 (2020).

343. About this possibility, Mark Lemley and Philip Weiser have mused that “ill-defined property rights regimes create challenges of their own making—the possibility of firms acquiring rights that give rise to holdup-type behavior.” Mark A. Lemley & Philip J. Weiser, *Should Property or Liability Rules Govern Information?*, 85 TEX. L. REV. 783, 808 (2007).

from the rigors of competition.<sup>344</sup> Even more worryingly, license regimes can create the possibility of corruption by the licensing agency.<sup>345</sup>

Libertarians believe that this sort of self-dealing characterizes many if not most, licensing regimes. Milton Friedman thought that there ought to be no legal licensing regimes; he famously weighed in against the licensing of physicians, meaning that he thought the market could provide sufficient information about the qualifications of a brain surgeon or oncologist to the would-be patient about the qualifications of such expert doctors.<sup>346</sup>

Rather than a license, this view posits that the market will establish who is a good oncologist (or whatever), and who ought to be avoided. The public choice view presses for the abolition of licenses as likely rent-seeking behavior. It is entirely incompatible with the public interest view.

### C. Licensing As Common Law

If these two rubrics are the ones most often deployed by academics when thinking about licensing, there are aspects of the licensing regime that can be missed. A critical one is that licensing quickly takes on the common law features that a licensing regime was designed to replace. Licensing quickly becomes susceptible to governance through precedents and *stare decisis*. Should a license application be granted? It is easy for the licensing regime to answer that question by reviewing how similar the application is to other successful license applications—a form of adjudication that uses the techniques of the common law outside of the courtroom.

These common law analogies are ironic because, in many ways, a licensing regime is meant to supplant the old common law way of ordering conduct. A purely common-law-ruled society would broadly permit any conduct, and sanction unreasonable versions of that conduct after the fact—it is how the tort system works, for example.<sup>347</sup> Licensing may be thought of as a pre-approval process—license applicants are forbidden from doing

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344. Michael Wara, *Competition at the Grid Edge: Innovation and Antitrust Law in the Electricity Sector*, 25 N.Y.U. ENV'T L.J. 176, 184 (2017) (“[B]ecause investor owned electric utilities are state-chartered monopolies, they are generally exempt from federal regulation of their anticompetitive conduct.”); Barry R. Litman, *The Economics of Television Networks*, in MEDIA ECONOMICS: THEORY AND PRACTICE 131, 132–33 (Alison Alexander, James Owers & Rod Carveth eds., 1998) (discussing spectrum scarcity as a moat that could keep out competitors).

345. Some observers think that there can be a second order rent extraction from licensing requirements—politicians can extract support from industries affected by regulation as they consider whether and how to dole out the moats that keep competitors out of the licensee’s market. Larkin, Jr., *supra* note 339, at 229 (“[P]oliticians can pursue the complementary strategy of ‘rent extraction.’ Legislators can obtain the continued support of regulated entities by threatening them with new legislation that would reduce the rents that they garner from the existing scheme.”). In the context of tax, Richard Doernberg has observed that “politicians can exact payments just by threatening harmful tax legislation” to interest groups. Richard L. Doernberg & Fred S. McChesney, *Doing Good or Doing Well? Congress and the Tax Reform Act of 1986*, 62 N.Y.U. L. REV. 891, 898 (1987). Threatened legislation, even if repeatedly threatened, can incentivize donors to respond to stop the legislation from happening. *Id.* Licenses, by the same token, can offer something similar.

346. See generally MILTON FRIEDMAN, CAPITALISM AND FREEDOM 137–61 (40th Anniversary ed., 2002) (“I am myself persuaded that licensure has reduced both the quantity and quality of medical practice . . . I conclude that licensure should be eliminated as a requirement for the practice of medicine.”).

347. See BARRY FRIEDMAN ET AL., JUDICIAL DECISION-MAKING: A COURSEBOOK 200–01 (2020) (describing the “wise-Cadi approach,” which exemplifies a pure common law society where no rules are set in advance and disputes are resolved as they arise).



something that, once they obtain the license (and establish their qualifications for it), they can then begin to do.<sup>348</sup> A no-license regime—the classical common law regime, for example—permits the activity, but sanctions beyond-the-norms practices of the conduct.

In this way, an alternative to licensing may be found in negligence law. The tort regime even has a substitute for the sorts of dangerous activities for which a license is generally required—strict liability for unreasonably dangerous activities.<sup>349</sup> Strict liability would not work for a nuclear power operator, who might be judgment-proof, at least if the operator unleashes a nuclear disaster.<sup>350</sup> But early applications of strict liability—for keeping dangerous animals, for example—that used to be handled through tort doctrine are now very likely to require licensing.<sup>351</sup> As the New York Court of Appeals put it in 1878:

[T]he owner is held to a rigorous rule of liability on account of the danger to human life and limb, by harboring and keeping such animals, it follows that he ought not to be relieved from it by slight negligence or want of ordinary care. To enable an owner of such an animal to interpose this defense, acts should be proved with notice of the character of the animal which would establish that the person injured voluntarily brought the calamity upon himself.<sup>352</sup>

Today, rather than permitting the animal owner to display the animals, but pay for any injury, dangerous animal owners must acquire a license to hold their charges.<sup>353</sup> The idea has been generalizable. When the regime starts to follow precedent, it begins to look like the common law regime that it replaced.

#### IV. QUALITATIVE AND QUANTITATIVE ANALYSIS OF CHARTER GRANTS

We can offer a case study of the common law nature of a licensing regime by applying plagiarism software to a set of recent licensing decisions by the OCC on new banks, fintech firms, and trust charter applicants. A quantitative comparison using plagiarism software

348. See, e.g., CAL. VEH. CODE § 12500 (2007) (“A person may not drive a motor vehicle upon a highway, unless the person then holds a valid driver’s license issued under this code, except those persons who are expressly exempted under this code.”).

349. RESTATEMENT (THIRD) OF TORTS § 20(B) (AM. L. INST. 2009).

350. The Fukushima Nuclear Disaster serves a great example. Based on the Japanese law, the operator of the nuclear power plant has unlimited liability and is responsible for the full cost of the accident even if it is not negligent. However, in practice, “the Japanese taxpayer is bearing most of the burden” as the insurance of TEPCO, the operator of Fukushima Nuclear Power plant, could only cover up to \$1.1 billion dollars, while the expected cost of the disaster is at around \$200 billion dollars. See Makoto Takahashi, *Five Years After Fukushima, There Are Big Lessons For Nuclear Disaster Liability*, THE CONVERSATION (Mar. 11, 2016), <https://theconversation.com/five-years-after-fukushima-there-are-big-lessons-for-nuclear-disaster-liability-56167>

[<https://perma.cc/9UC9-AN7A>] (describing the aftermath of “the biggest civil liability case in history”); see also Ben Dooley, Elmi Yamamitsu & Makiko Inoue, *Fukushima Nuclear Disaster Trial Ends With Acquittals of 3 Executives*, N.Y. TIMES (Sept. 19, 2019), <https://www.nytimes.com/2019/09/19/business/japan-tepco-fukushima-nuclear-acquitted.html> (on file with the *Journal of Corporation Law*) (“A Japanese court on Thursday acquitted three former Tokyo Electric Power Company executives who had been accused of criminal negligence for their roles in the meltdown of the Fukushima Daiichi nuclear plant.”).

351. See, e.g., ARIZ. ADMIN. CODE § 12-4-406 (2021) (“In order to lawfully possess wildlife listed as restricted under this Section. . . a person shall possess: 1. All applicable federal licenses and permits; and 2. The appropriate special license. . .”).

352. *Muller v. McKesson*, 73 N.Y. 195, 202 (N.Y. 1878).

353. See ARIZ. ADMIN. CODE § 12-4-406 (2021) (describing one such licensing regime).

can tell us what kind of aspects of the license grant the agency cared about, at least if a tailored portion of the conditional approval reflected care. As it turns out, there's lots of boilerplate—a form of following precedent, in OCC orders: The important takeaway is that the copying of prior orders shows the resiliency of *stare decisis* even in a licensing regime designed to replace common law. We can also see from those charters that descriptively new banks and trusts are likely to be online institutions.

The OCC has imposed a standard set of requirements on almost every bank that has applied to become a national bank, trust or otherwise. It conditions approval on the execution of a Capital and Liquidity Support Agreements (CSA) with the bank or trust's parent company along with an execution of a Capital Assurance and Liquidity Maintenance Agreement (CALMA) that sets forth the charter recipient's "rights and obligation to seek and obtain all necessary capital and liquidity support from" the parent, as the operating agreement associated with the conditional approval of Anchorage Digital Bank put it.<sup>354</sup> It also imposes capital requirements on the bank and identifies a relatively tiny minimum capital requirement prior to opening, usually in the low single-digit millions of dollars.<sup>355</sup>

As a matter of business operations, the agency approves the bank's directors and senior executives,<sup>356</sup> requires the designation of a full-time compliance officer,<sup>357</sup> requires the engagement of an independent, external auditor,<sup>358</sup> and requires the establishment of the Fiduciary Audit Committee within the bank.<sup>359</sup> To vet the personnel, the OCC requires all holders of 10% or more of the initial stock offering to submit biographical and financial reports for the agency's review.<sup>360</sup> The bank also must purchase adequate fidelity bond coverage.<sup>361</sup>

I used the plagiarism software WCopyFind 4.1.5 to analyze a sample of OCC national bank and national trust bank approval letters. Created at the University of Virginia, WCopyFind is an open-source program that searches for matching language in a collection of documents and has been used in law and court research as well as legal scholarship.<sup>362</sup>

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354. OCC, OPERATING AGREEMENT BY AND BETWEEN ANCHORAGE DIGITAL BANK NATIONAL ASSOCIATION, AND THE OFFICE OF THE COMPTROLLER OF THE CURRENCY 4 (2021), <https://www.occ.gov/news-issuances/news-releases/2021/nr-occ-2021-6b.pdf> [<https://perma.cc/9C25-LDKC>].

355. ANDREW P. SCOTT & MARC LABONTE, CONG. RSCH. SERV., R47447, BANK CAPITAL REQUIREMENTS: A PRIMER AND POLICY ISSUES 9–11 (2023).

356. OCC, *supra* note 215, at 6–7.

357. *Id.* at 80.

358. *Id.* at 44.

359. OCC, COMPTROLLER'S HANDBOOK: INTERNAL AND EXTERNAL AUDITS 11 (2019), <https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-handbook/files/internal-external-audits/pub-ch-audits.pdf> [<https://perma.cc/ZE44-B4AU>].

360. *See generally* OCC INTERAGENCY BIOGRAPHICAL AND FINANCIAL REPORT FORM, <https://www.occ.treas.gov/static/licensing/form-ia-bio-financial-v2.pdf> [<https://perma.cc/PM24-8WAV>] (providing the relevant form).

361. 12 C.F.R. § 713.3 (2024).

362. *See, e.g.*, David Zaring, *CFIUS as a Congressional Notification Service*, 83 S. CAL. L. REV. 81, 114–15 (2009) (using Wcopyfind to find data suggesting that CFIUS treated like mitigation agreements similarly); David Zaring, *Sovereignty Mismatch and the New Administrative Law*, 91 WASH. U. L. REV. 59, 98 (2013) (comparing Basel Committee proposed rules to final ones); Adam Feldman, *Who Wins in the Supreme Court: An Examination of Attorney and Law Firm Influence*, 100 MARQ. L. REV. 429, 438 (2016) (comparing overlapping language between briefs and opinions); Pamela C. Corley, *The Supreme Court and Opinion Content: The Influence of the*

I used the software to compare the ten most recent national bank approval letters and the ten most recent national trust bank approval letters with each other, resulting in 200 total comparisons. I looked for phrases that overlapped at least 80% between compared documents with the minimum length of each phrase set to five words.

Descriptively, twenty recent conditional approvals tell us something about the state of entrants into the banking business today. Of the ten banking charters issued between 2018 and 2020, eight were so-called *de novo* banks—new banks. Two were charter conversions, turning a state charter into a federal charter. The conversions included one relatively large bank, Fifth Third, an Ohio institution that gave up its Ohio charter to become a national charter and a bank holding company. The other charter conversion came from the online peer-to-peer lender LendingClub, which obtained Radius Bank, a federally chartered thrift, and in the merger, converted the charter into a national bank charter.<sup>363</sup>

The ten national bank charters included five digital banks, including LendingClub, and four small community bank startups, with Fifth Third rounding out the group. The average length of their conditional approvals was 1675 words, with the time from application to approval applicant 189 days.<sup>364</sup>

The 11 trust charters issued between 2017 and 2021 reflected the diversity of the trust model. There were two *de novo* applicants, three charter conversions, and four trusts created as the result of a merger. One new trust was a payroll processor and the other one of the three controversial digital asset custodians. The two other digital asset custodians converted their charter; so did Chilton Trust, a wealth manager. Computershare, a provider of corporate governance and financial services, obtained its trust charter pursuant to a change in control.<sup>365</sup> Four of the other trusts, Evercore, Rockefeller Trust, Stifel Trust, and First Community, also used a merger to provide a trust to assist with those firm’s wealth management businesses, while National Advisors offers custodial services to financial advisors, and obtained its trust charter pursuant to a business combination.

The average length of these orders was approximately 1618 words, not measurably different from the length of the charter approvals of new banks. But the time it took for the trust to obtain their charters was substantially quicker than was the time it took the banks to do so; OCC granted its trust charters on average in 128 days, with two of the digital trusts containing applications and half that time.

One could also compare the “Conclusion” sections of each national trust bank approval letter. This section—a similar version of which is also inserted into the national bank approval letters—is a reminder that the conditional approval does not constitute a

*Parties’ Briefs*, 61 POL. RES. Q. 468, 471 (2008) (discerning which factors affect the extent to which parties’ briefs influence the content of Supreme Court opinions). WCopyFind may be accessed online. *WCopyFind*, THE PLAGIARISM RES. SITE, <https://plagiarism.bloomfieldmedia.com/software/wcopyfind/> [https://perma.cc/6UB2-P8SP].

363. *Corporate Applications Search Result Details*, OCC, [https://apps.occ.gov/CAAS\\_CATS/CAAS\\_Details.aspx?FilingID=314475&FilingTypeID=23&FilingSubtypeID=1116](https://apps.occ.gov/CAAS_CATS/CAAS_Details.aspx?FilingID=314475&FilingTypeID=23&FilingSubtypeID=1116) [https://perma.cc/83PQ-YTQK].

364. Unless otherwise noted, all percentages and descriptions of the dataset are based on the results of the research methodology using Wcopyfind described in Part IV.

365. Letter from Marva V. Cummings, Dir. for Dist. Licensing, OCC, to Richard L. Johnson, Jr., Chief Compliance Officer, Computershare Tr. Co., Conditional Approval #1272: Substantial Asset Change Application Filed by Computershare Trust Company (July 29, 2021), <https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2021/ca1272.pdf> [https://perma.cc/B7D3-PAXZ].

contract, is based on the bank's representations and submissions, and may be rescinded. The median overlap among the national trust banks is 78% (compared to 25% for approval letters as a whole).<sup>366</sup>

Trusts have very similar CALMAs, Operating Agreements, and CSAs.<sup>367</sup> The median overlap percentage among the eight "Condition" sections is 57%.

National bank conditional approvals offer an interesting comparison. Here, the business model did not matter as much as the kind of application; conversion charters looked quite different—with one notable exception, while de novo approvals shared more language. Among the ten most recent national bank approval letters, the lowest overlap percentages occurred among the two conversions (LendingClub and Fifth Third Bank)<sup>368</sup> and the two internet banks (Varo Bank and SoFi),<sup>369</sup> both of whom acquired community banks in order to receive their national bank charters.

The boilerplate obscures any differences in the applications—the fact that the recommendations follow such a similar format suggests a common law component to a licensing regime designed to replace it. Is this surprising? Perhaps not, but it does highlight that reform is often less transformational than some might assume.

## V. THE SKINNY CHARTER

The Obama administration's OCC developed a fintech charter, a charter that would apply to financial technology firms that did not hold deposits, so did not need deposit insurance, and so did not need the approval of the FDIC.<sup>370</sup> The charter would make the OCC the supervisors of fintech firms that facilitated lending or that made payments; the attraction was that OCC regulation would preempt state oversight through money processor licensing and other consumer protection laws. The politics behind the rule were initially bipartisan—nationalizing the oversight of internet firms that by definition did not operate in only one or a few states was popular with both Democrats and Republicans, and the Trump Administration successfully defended the fintech charter from a suit against state banking supervisors arguing that the OCC did not have the power to issue such a charter.<sup>371</sup> The hope

366. For example, First Community Trust's and Protego Trust's Conclusion section has 86% and 93% overlap, respectively.

367. Anchorage and Protego Trust, two of the most recent national trust approvals, provide anomalous results. Their approval letters have 58% and 47% overlap, respectively. Each, however, have large sections of the approval letter—approximately 65% of Protego's and 54% of Anchorage's—that have much higher overlaps. These sections include "Conversion," "Fiduciary Activities," "Pre-Conversion Requirements," "Conditions," and "Conclusion." Each bank's Conversion, Fiduciary Activities, and Pre-Conversion Requirements has 73% overlap. Protego's and Anchorage's Conditions sections have 88% and 92% overlap, respectively. And the trust banks' Conclusion sections are identical—100% overlap.

368. Although their overlaps when compared to the other national bank approval letters are 14% and 11%, respectively, when compared to each other, their overlap percentages are 25% and 23%, respectively.

369. Although their overlaps when compared to the other national bank approval letters are 37% and 42%, respectively, when compared to each other, their overlap percentages are 63% and 72%, respectively.

370. OCC, EXPLORING SPECIAL PURPOSE NATIONAL BANK CHARTERS FOR FINTECH COMPANIES 2 (2016), <https://www.occ.gov/publications-and-resources/publications/banker-education/files/pub-special-purpose-national-bank-charters-fintech.pdf> [<https://perma.cc/DG4S-UHB9>].

371. Jim Puzanghera, *As Online Lending Companies Gain Popularity, the Trump Administration is Making It Easier for Them to Bypass State Regulations*, L.A. TIMES, (July 31, 2018), <https://www.latimes.com/business/la-fi-fintech-treasury-regulations-20180731-story.html> (on file with the *Journal of Corporation Law*).

was that a limited charter, bringing technology firms inside the regulatory perimeter, and yet allowing for competition in the banking sector, would yield benefits in both innovation and customer improvement.

However, there has never been an application for a fintech charter, which has become a surprisingly controversial and partisan regulatory initiative. Part of the reason for this is legal uncertainty; state banking charter supervisors sued to block the entire charter program before it had even begun operation.<sup>372</sup> But another part of the problem is that liberal banking regulators have suggested some distaste for a skinny charter, and the trust charter gambits by fintechs at the end of the Trump administration politicized the idea.<sup>373</sup>

But constraints on who should be chartered are conservative and anti-innovative, and, as this article has shown, the boundary between charters and non-chartered institutions offering financial services is porous, especially now, but it always has been. We have had vehicles to make the boundary between banking and commerce permeable for decades—the trust charter has been used to manage that boundary and yet bring institutions that want to do things a different way inside the regulatory perimeter for over a century. The trust charter experience, the rise of financial technology firms, and the increasing interventions of commercial firms into the space that used to be occupied by banks, and banks only, suggest that a new era of charter flexibility is an appropriate choice. The reality of charter incursions means that a new approach to chartering, one that is more flexible, is appropriately calibrated to the world that bank regulators have allowed to exist. Skinny charters are the future—payment charters, deposit charters, possibly, although the trust charter handles a lot of that risk, and lending charters are ways to go forward. This Article argues that a more flexible approach to chartering will bring some of the currently possibly illegal but tolerated incursions by commercial firms into the banking space into regulatory compliance, and will continue to keep bank supervision, where the risk is mostly about using on-demand deposits to finance long-term lending, in an appropriately regulated space.

One reason to offer skinny charters is to increase competition in the banking sector.<sup>374</sup> Borrowers can choose between borrowing from the bank and borrowing from a peer-to-peer lender. Homebuyers could choose between the nonbank Rocket Mortgage and the mortgage offered—to the extent that they are still offered—by normal banks. There may be a role for some money managers to acquire a deposit charter and deposit insurance, also in a way that might be beneficial for consumers. Moreover, financial technology firms with charters might broaden access to banking services to the underbanked. Already, those firms appeal to younger consumers, and it is young consumers who are least likely to avail themselves of banking services.<sup>375</sup>

Moreover, there may be good reasons for firms to want to get these kinds of charters. Federal charters preempt state law and might make it easier for these challenger institutions

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372. *Lacewell v. OCC*, 999 F.3d 130, 134 (2d Cir. 2021).

373. See, e.g., Adam Rust, *Victory: Figure Bank's Withdrawn Charter Application Shows the Uninsured National Bank Idea Is Dead*, NAT'L. CMTY. REINVESTMENT COAL. (Aug. 8, 2023), <https://nrc.org/victory-figure-banks-withdrawn-charter-application-shows-the-uninsured-national-bank-idea-is-dead/> [<https://perma.cc/3EW5-FNQD>] (celebrating the regulatory failure of “novel charters”).

374. See *supra* note 10 and accompanying text.

375. See Bennett & Melican, *supra* notes 155 and accompanying text (discussing potential disruptive impact of fintech).

to manage their regulatory remits and operate in many states, with only one regulator, rather than one per state.

#### CONCLUSION

This Article has used the increasingly fraught licensing regime in banking to illustrate how licensing works more generally. It presents a wide array of takeaways—possibly too many. It demonstrates how the persistently porous regulatory perimeter is now being breached by a diverse range of commercial firms assuming banking responsibilities. It advocates for a reimagined, intentionally permeable regulatory perimeter, constructed through the creation of various “skinny charters,” such as fintech charters, payments charters, and potentially deposit and lending charters. The Article delves into the history and current relevance of the trust charter, one of the oldest mechanisms for banks and nonbanks to navigate the regulatory perimeter, and a likely source of future charters for fintechs. Additionally, this evaluation provides an opportunity to examine the underexplored role of licensing in administrative law, which, as the Article contends, often evolves into a common law regime that licensing was originally intended to replace. This argument is supported by a quantitative analysis of federal bank licensing decisions, revealing through plagiarism software that licensing decisions often follow precedent. A more flexible regulatory perimeter would better align with the current landscape of financial services, fostering increased competition while reserving traditional licenses for the most inherently risky types of banks.