On July 31, 2018, the Department of the Treasury issued a report, "A Financial System That Creates Economic Opportunities: Nonbank Financials, Fintech, and Innovation," that examines financial institutions and activities for which the application of traditional regulation may present challenges due to advances in financial technology ("fintech"). It is the last in a series of four reports written in accordance with Executive Order (E.O.) 13772 issued by President Donald Trump on February 3, 2017, which directed the Secretary of the Treasury to report on the financial regulatory system.

The Treasury report covers numerous issues and makes more than 80 recommendations. The report does not does not specifically cover cryptocurrencies and initial coin offerings. This Insight examines selected issues and recommendations in three broad areas: (1) general issues raised by recent technological advances, (2) specific issues facing certain financial industries, and (3) regulators' ability to respond to innovations.

For a broad overview of fintech, see CRS In Focus IF10513, Introduction to Financial Services: "Fintech."

General Fintech Issues

The Treasury report examines certain technological advances affecting finance generally that it asserts present challenges to the existing regulations.

- **Digitization.** The report notes that modern finance intensively uses digital tools and methods, but that policymakers developed many laws and regulations for a system using paper forms and interpersonal communication. It asserts that this shift necessitates certain regulatory changes. One of its recommendations is that regulators promulgate clarifying digital communications' regulations under the Fair Debt Collection Practices Act (P.L. 95-109).

- **Consumer Financial Data.** As digitization has increased, the amount of available data about consumers and their
finances has grown. The report asserts that in certain instances policymakers have not adequately responded to issues related to the collection, use, and safekeeping of that data. Its recommendations include that Congress enact a data breach notification law and regulators adopt a number of measures aimed at providing legal and regulatory clarity surrounding questions of data access rights.

- **Technologies Offering Greater Data and Computing Capacity.** The report notes that the development of cloud computing, big data, machine learning, and artificial intelligence could potentially increase financial efficiency, but that certain regulations may unnecessarily hinder the adoption of these technologies. Its recommendations include that regulators modernize requirements and guidance, establish working groups to study the technologies, and engage in industry outreach.

Industry-Specific Issues

In addition, the report identifies certain financial industries that it asserts are in particular need of regulatory reforms.

- **Lending.** The report describes how lending to consumers and small businesses is increasingly done by nonbank digital lenders—such as marketplace lenders—and how many of them partner with banks to originate loans. It asserts that certain court cases have created uncertainty around the applicability of the "valid-when-made" doctrine to these loans and around what entity is the "true lender" in these arrangements. The report recommends, among other things, that Congress codify the valid-when-made doctrine and the principle that the bank is the true lender in certain third-party lending relationships.

- **Payments.** The report notes that new services are playing an increasingly prominent role in the payment system and these services could potentially offer greater efficiency; however, it asserts that new service providers face entry barriers due to regulatory fragmentation and existing operational complexity. The report's recommendations include that the Federal Reserve publicly set goals and deadlines to achieve a faster payment system.

- **Wealth Management.** The report describes how wealth management technology tools continue to evolve with respect to the scope of products (securities, loans, and insurance) their applications are involved in and the variety of business models (machine-based only or integrated with human advice) used. However, the report asserts that the current regulatory structure is fragmented, with multiple federal and state regulators having overlapping responsibility for specific activities, potentially hindering the development of investment advice products and services. As such, the report includes a recommendation that an existing regulator be appointed as the primary regulator for financial planning oversight.

Changes to Regulatory Framework

The report identifies certain initiatives that it asserts policymakers should undertake to make regulators better able to respond to issues raised by fintech.

- **Modernize Regulatory Framework.** The report identifies changes that it asserts would make the financial regulatory framework more effective and efficient in relation to how it regulates innovation. Its recommendations include that all bank regulators provide clarity to banks regarding their relationships with third-party service providers, the OCC makes the special purpose national bank charter available to fintech firms under certain conditions, and that the Federal Reserve reexamine the regulation of bank holding companies to facilitate investment in innovation.

- **Establish Regulatory "Sandboxes."** The report asserts that the current regulatory system can be inflexible and new firms can find the fragmentation and possible risk of enforcement actions as a hindrance to bringing innovative technologies to market. As such, the report recommends that regulators establish regulatory "sandbox" programs that allow for coordination among regulators and regulatory relief for firms developing innovative products and services.

- **Increase Agility.** The report asserts that as technology has advanced, regulators have faced obstacles to fully understanding new technologies and their implications in a timely manner. It recommends, among other things, that Congress authorizes regulators to use funds to procure the latest technologies and for research and development projects, and that regulators engage in industry and consumer outreach and review existing regulations as new technologies are adopted.
Legislative Role

The report identifies 23 recommendations (a number of which are described above) in which Congress could play a role. For example, some recommendations require the enactment of legislation and some advise Congress to assess whether an issue should be addressed through legislation. The report indicates that the remaining 58 recommendations could be implemented by regulators under existing regulatory authorities. However, Congress could mandate the implementation of a number of these recommendations if it believes regulators are moving too slowly or will choose not to implement the change. Appendix B of the report provides a summary of the recommendations and indicates which recommendations involve congressional responsibility.