The BigTech/Fintech Battle of 2021: The Policy Agenda and Its Outcome

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Key Points

- The scale of tech-finance combined with the epiphanal impact of the meme mania transforms U.S. administrative, legislative, and regulatory action in 2021 from earnest debates to meaningful action.
- U.S. policy-makers will now move past "responsible-innovation" nostrums to specific, tech-skeptical measures addressing competitive, systemic, and consumer-protection flash points.
- Still, statutory change directly affecting finance is unlikely. An incident in which one or more members of Congress is directly affected or a unifying event, tech-finance policy will largely be made by regulatory interventions, including systemic designations, consumer restrictions, and expansion of bank prudential requirements.
- Biden Administration demands that rules consider inequality and inequity dramatically change the context of rules for data ownership, AI, pricing, credit scoring, alternative data, and much more.

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Introduction

2021 is a strategic inflection point. A sharp departure is already underway from longstanding tolerance for tech-finance experimentation and even large-scale market entry due to changing public views on BigTech in general and financial technology in particular. As a result, support has ebbed and even reversed to become opposition to controversial tech-finance applications and charters or "partnerships."

Congress will also lay aside its willingness to tolerate a wide array of practices lumped under a "responsible innovation" umbrella, moving to action as well as investigation as a result of Democratic control, ongoing revelations about BigTech market power, and greater understanding of the transformational nature of fintech wrought by the chaos of the GameStop market mania. This made it clear not only that a relatively small fintech company was about much more than the "financial inclusion" highlighted in all its mantras, posing risks not just to vulnerable investors, but even to equity-market stability.

In the lead-up to the 2007-09 great financial crisis, Congress and regulators tolerated high-risk mortgage finance on grounds of "democratization" until about 2006, when the sudden failures of relatively small nonbank subprime lenders laid bare the scope of growing risk. By then, it was too late for policy to avert a crisis. Now, the Administration, Congress, and financial regulators hope to.

This policy analysis follows earlier FedFin work providing a taxonomy of BigTech/fintech financial-policy issues and a first-ever analysis of resulting economic-equality considerations. We now build on this work and thus omit detailed issue analysis. Before turning to our forecasts, we reiterate a longstanding cautionary note: U.S. financial policy is often set not by reasoned discourse, but by the personal experiences of individual members (e.g., a lost payment or undue dunning letter) and by crisis (e.g., systemic-infrastructure failure). We have already seen a sharp turn-around in political discourse following GameStop and more is sure to come as the Administration's racial-equity and economic-equality agenda takes shape and force. Thus, any significant incidents will alter prioritization and create consensus even where none may have existed, accelerating action that, even if ill-considered, creates a new market landscape. Barring these idiosyncratic developments, FedFin forecasts action on the following priority decision points:

BigTech's Market Power and Data Arsenal

BigTech's overwhelming market presence is among the few issues on which there is broad bipartisan consensus about the need for action even though, as always, there are strong differences about which aspects of BigTech's construct to prioritize for reform and how best to do it. Democratic leaders in both the House and Senate will pursue a new statutory framework for tech-platform companies designed to prevent continued control of social media, advertising, information content, and retailing. Republicans are in general more concerned about market intervention and very focused on political content, but many concur that tech-platform companies have too much power and warrant control.

Policy so far has no direct financial-services component, with legislation and administrative action focused instead on standards to hold platform companies accountable for content much like other publishers and to enforce the equivalent of fair-use access and pricing policies. However, many aspects of pending provisions would have significant indirect financial-services implications even if legislation is not expressly expanded.

For example, standards being advanced could well affect organic BigTech entry into new financial services, redesign stablecoin projects such as Facebook's Diem, or reduce their payment-system growth. Acquisitions – e.g., efforts to acquire or establish bank charters – will face growing obstacles not only at the banking agencies, but also under a new antitrust framework sure to emerge for BigTech firms in the Biden Administration.

Regardless of antitrust actions or legislation, BigTech platforms, fintech firms, and companies such as PayPal that straddle this divide and engage in nonbank financial services also face more direct and immediate structural challenges: potential systemic designation and/or barriers to relationships with insured depositories. We expect this regulatory framework to follow two tracks at more or less the same time: entity-based designation for core financial infrastructure (e.g., cloud and payment services) and affirmative standards based on a 2020 statement from the Office of the Comptroller of the Currency that companies that rest their services on bank platforms must be held to bank-like consumer-protection and prudential standards. Treasury's Financial Stability Oversight Council (FSOC) has no ability to regulate tech-finance other than via designation even if activity/practice standards are set except via the banking-institution interface and it will not hesitate to use this tool as desired.

Payment-System Pain

Although the Fed has talked about faster payments since at least 2013, its instant-payment system is still at least two years off. Even then, inter-operability is at best uncertain, as is cross-border capability.

Democrats won't wait – they want immediate instant-payment capacity with or without these features and will push the Fed hard to get it. However, we do not think Democrats will go beyond reintroducing legislation demanding instant payments unless another set of emergency-stimulus payments goes astray.

The real battle in 2021 thus isn't about forcing the Fed to speed up as much as requiring the Fed to open both its existing payment system and new instant options to non-depository institutions. So far, the Fed has held firm, but market developments may force it to reconsider direct entry by fintech and even BigTech firms. Key to this will be the Fed's decision on pricing parity and whether it has the statutory authority to open the payment system and, if it does, the extent to which nonbanks must abide by stringent sterile reserve requirements to ensure finality under all foreseeable circumstances. Set these standards high enough and banks may concur with tech access, especially if it's accompanied by the systemic standards referenced above. Set them low and without other rules, and existing payment systems and banking organizations will take considerable umbrage.

Data Ownership

Who owns personally-identifiable data and what may then be done with it is a threshold frontline in the battle over tech finance. Although there are many calls for U.S. "open banking" akin to that in the European Union, differences in the U.S. regulatory landscape and growing fears of tech-finance's power make this unlikely.

Instead, federal regulation will establish the new construct. The Bureau of Consumer Financial Protection (CFPB) got an earful after it last year asked for views on consumer-data ownership. Under

the Biden Administration, this standard will be built out very differently than it might have been under President Trump, focusing on consumer rights rather than the putative benefits of innovation. Although commenters sought resolution of their liking to ongoing battles between banks and data aggregators, the CFPB's rule-making comes at a time of heightened awareness of the power of personal data and growing consumer demands to control or even be paid for it.

The power of data also to fuel artificial-intelligence and machine-learning algorithms across an array of consumer-finance products is also closely tied to the question of ownership, with serious consideration also for allowing consumers to delete personal data they believe adversely affect their economic prospects or personal rights. These questions of course have important bearing also for credit scoring above and beyond longstanding Democratic demands that medical or other debt be omitted from furnisher reports.

Digital Currency

This is an arena particularly prone to the surprises and even crises that alter policy forecasts. With bitcoin reaching unheard-of highs as of this writing, crypto-currencies and related assets are either set for a final phase of institutionalization presaged by Tesla's investment or a catastrophic fall that returns cryptocurrencies to the realm of illicit commerce and inveterate libertarians. Which path it follows will of course have profound policy impact.

Assuming relative stability, we do not believe that the Biden Administration and Congress will be content to allow federal regulators to design the U.S. crypto-asset framework by individual and often idiosyncratic actions such as those taken in 2020 by Acting Comptroller Brooks. Many of the new charters Mr. Brooks authorized are conditional and we expect these conditions to become even greater barriers to actual operation under new agency leadership.

That said, U.S. policy-makers also know that a holding action – i.e., doing nothing forward-looking – will not suppress innovation outside their reach. Stablecoins are a top concern given Facebook's clout and Treasury and the banking agencies will turn quickly to implementing the policy framework sketched out in the final days of the Trump Administration. Systemic designation combined with activity-and-practice standards will come into their powerful own for stablecoins. AML requirements are already coming into force in this arena, but sterile reserve questions are also critical here along with conflict-of-interest, disclosure, and payment finality standards.

Overhanging all private crypto-currencies and payment systems is the question of if and when the Fed will decide to create a central-bank digital currency (CBDC). Congressional Democrats want to force it quickly to do so, opening up the central bank not only as the arbiter of a digital version of the dollar, but also as a depository offering "FedAccounts" to the American citizenry.

However, even a relatively unambitious CBDC is a formidable undertaking and, as with its slow-go instant payment system, the Fed is moving at deliberative speed in its contemplation of a CBDC. Congressional Democrats will press hard for rapid action and, as with instant payments, get in return only promises and interim reports. Democrats will instead reserve their firepower to promote limited postal banking and new forms of public banks.

CRA for Everyone

In addition to the consumer-protection and safety-and-soundness rules referenced above, there are strong demands – especially from Democrats – that nonbanks active in retail finance fall under the Community Reinvestment Act (CRA) in ways comparable to insured depositories. Indeed, Democrats aren't the only ones seeking CRA parity – the Trump Administration in 2018 called for further research into nonbank CRA coverage. The question of an expanded CRA has largely been dormant ever since, but it became a live wire again earlier this year when a fintech company, Figure, sought a special-purpose OCC charter that, among its other features, exempted the resulting bank from CRA.

We cannot see a Biden-appointed Comptroller approving any special-purpose charters without careful consideration of all the rules applicable to them, including CRA. Indeed, we expect bank charters to be conditioned on CRA compliance as it will come to be determined later this year by inter-agency regulation departing significantly from the OCC's 2020 regulation. The OCC and other agencies may well also use their power over banks to demand that fintechs and others that leverage their services atop a bank's platform comply with the CRA with regard to all loans or other services developed in connection with the bank.

Going farther and applying CRA to tech-finance firms and other nonbanks requires new law. We do not expect this to be a major 2021 legislative priority unless the Biden Administration or its regulators expressly press for it. If so, Congress could well enact an expansion, with Republicans accepting it on grounds of competitive equity.