

## KEY TAKEAWAYS – 2021 UNC BANKING INSTITUTE IN CHARLOTTE

## Partner with Care: Lessons for Banks and Fintechs

A substantial amount of the innovation underway in banking today is being accelerated by partnerships between traditional banks and fintechs. But these third-party arrangements can bring a variety of risks that need to be carefully managed. Banking industry leaders and regulators gathered at the Banking Institute of the University of North Carolina School of Law's Center for Banking and Finance to review the state of these collaborations and emerging best practices. Highlights of the conversation included the following:

### LOOK UNDER THE HOOD, NOT IN THE GLOSSARY

Propelled by the convergence of data, technology and mobile, fintech has moved from the periphery to the center of the banking industry to such an extent that the term "fintech" is of diminishing usefulness, as is the traditional distinction between "bank" and "nonbank." Instead, it is becoming more meaningful to identify entities by their products, partners, customers, and by their place in the banking ecosystem.

### REGULATIONS AREN'T THAT RIGID

There is a common misperception that banking regulations are outdated and slow-moving compared with the pace of industry change. But the reality often is that regulations are more than sufficiently flexible to accommodate innovation. At the same time, however, new business models

are emerging, such as non-bank lenders working with employers to provide small-dollar loans tied to wages, that represent serious excursions into uncharted regulatory waters. Regulators also recognize the need for new guidance on how data is gathered, shared and used.

### PARTNERSHIPS SHARE REWARD BUT NOT RISK

As banks pursue various business arrangements with fintechs, it's important to remember that from the regulator's perspective, the onus for ensuring compliance and safe and sound outputs rests squarely with the bank. Banks thus need to have extensive third-part risk management in place, with adequate governance, onboarding, monitoring and remediation processes.

### MITIGATE CULTURE SHOCK

Within every bank-fintech partnership, there is a fundamental cultural tension between heavily regulated banks and the frictionless ideal sought by fintechs. While banking regulators are trying to address this gap through guidance targeted to fintechs, banks should be prepared to make a significant investment in educating their fintech partners not just on technical compliance but the larger cultural environment they are entering. Fortunately, fintechs have largely evolved past the once-common "innovate first, ask questions later" mindset and now increasingly endeavor to remove friction while respecting regulatory frameworks.

## THE FIRST TIME IS THE HARDEST

The legal issues involved in a bank acquiring or investing in a fintech are usually relatively straightforward. But a true business partnership, involving the integration of each entity's products, services or customers, can require months of legal groundwork to develop an arrangement that can withstand regulatory scrutiny. The good news is that there is a learning curve to the process, making the planning for each successive partnership less onerous.

## CONSIDER COUNSEL AS AN INVESTMENT, NOT AN EXPENSE

Like most technology ventures, fintechs often minimize costs outside of development and marketing, making it easy to put off seeking strategic legal counsel until "later." The reality is, however, that there are significant long-term advantages to identifying and addressing legal issues early on. Once a venture has secured enough funding to ensure ongoing operations, it should factor in the cost of legal advice.

## EXPECT A DYNAMIC PERIOD AHEAD IN REGULATION

At the federal level, the new regulatory leadership has a sizable opportunity to set the pace and direction of agency approaches to the current tsunami of innovation. Among the states, efforts to harmonize the multistate regulatory environment and build a system to allow states to more easily

share examination information are eagerly awaited at a time when bank-fintech arrangements routinely cross state lines.

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## ABOUT THE PANEL

Our thanks to the members of the panel, "Bank Partnerships with FinTech Firms": **Christopher L. Allen**, Arnold & Porter, Washington, D.C. (coordinator); **Amias Gerety**, QED, Washington, D.C.; **Melissa Koide**, FinRegLab, Washington, D.C.; **Chris Ledoux**, FDIC, Washington, D.C.; **Mike Penney**, Arnold & Porter, New York, NY; and **Mike Townsley**, Conference of State Bank Supervisors, Washington, D.C.

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