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FinTech Report:

Summary of Responses to Treasury RFI on Marketplace Lending

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David S. Reidy
Nicholas F.B. Smyth
Heather Cantua Phillips
and Tyler M. Layton

Editorial Team:
*Drew Amoroso, Roxanne Anderson,
Sean Donoghue, Anthony Ford,
Yvonne Pham, Rachel Naor,
Jaclyn Schwizer, Jamie Wells,
and Molly Zapala.*

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I. Introduction

On July 20, 2015, the US Department of the Treasury issued a Request for Information entitled "Public Input on Expanding Access to Credit through Online Marketplace Lending" (the "Treasury RFI").[1] Just fewer than 100 comments were submitted by marketplace lenders and other FinTech companies, as well as banks, industry and consumer groups, politicians, agencies and other concerned parties. This report provides an overview of the substance of those responses, and a summary of their key themes and new ideas.

The RFI poses numerous questions to industry participants, but its issuance by the Treasury Department raises its own questions: Why did Treasury put out the RFI? What will Treasury do with the comments it receives? After all, Treasury is not a regulator. If the Securities and Exchange Commission (SEC) or Consumer Financial Protection Bureau (CFPB) had released a similar RFI, for example, the purpose and potential resulting regulatory action might have been easier to predict. But Treasury's role suggests a broader policy initiative than might be expected had the RFI been issued by a pure industry regulator.

Based on the office that issued the RFI, we believe Treasury's primary goal in releasing the RFI is to encourage marketplace lenders to continue expanding credit to small businesses. The RFI cites a 2015 Federal Reserve Survey that found that "a majority of small firms (under $1 million in annual revenues) and startups (under 5 years in business) were unable to secure any credit in the prior year."[2] Treasury clearly wants to encourage large and small lenders to increase the availability of credit by using "technology-enabled credit provisioning," which Treasury says "offers the potential to reduce transaction costs."[3] With Congress at a stand-still, the Obama administration has made clear that it will pursue policies through executive actions, and it may be that the RFI is a first step in developing executive actions to encourage such lending without relying on action from Congress.

The RFI was released by Treasury's Office of Small Business, Community Development, and Housing (part of the Office of Financial Institutions, within the Office of the Undersecretary for Domestic Finance), and responses were directed to Laura Temel, a Policy Advisor in that office. According to public sources, Temel is a successful entrepreneur who has founded two companies, one of which was selected to participate in the inaugural class of the Nike+ Accelerator. Previously, she was an

[1] 80 FR 42866.

[2] *See* Appendix A, Treasury RFI, p. 5 (citing "The Joint Small Business Credit Survey, 2014," a collaboration among the Federal Reserve Banks of New York, Atlanta, Cleveland and Philadelphia. Released February 2015.).

[3] *Id.*, p. 6.

investment banker. Treasury's choice to lead the RFI underscores the business focus of the project.

The Small Business Office is a policy-making office; its mission is to coordinate "policy on the following areas: small business finance and development; housing policy; community and economic development; capital access; and issues related to underserved communities."[4] The Office also oversees the Small Business Lending Fund and the State Small Business Credit Initiative. This office is small but influential; its alumni include, among others, Don Graves (now Deputy Assistant to the President and Counselor to the Vice President) and Sameera Fazili (now senior visiting adviser to the Federal Reserve Bank of Atlanta's community and economic development group, formerly senior policy adviser at the White House's National Economic Council).

Given the responsibilities of the Small Business Office and the entrepreneurial background of the Treasury official who is behind the RFI, it seems clear that learning how the government and marketplace lenders can work together to further improve small business credit access, cost, and speed is the primary focus of the RFI. However, it likely is not the only focus.

[4] https://www.treasury.gov/about/organizational-structure/offices/Pages/Sm-Business-Community-Dev-Housing-Policy.aspx

A secondary purpose of the RFI may be to enhance the public conversation with respect to the potential benefits and risks of marketplace lending. Treasury no doubt recognizes that in an industry that is evolving as rapidly as marketplace lending, it would be helpful to have a public repository of data and analysis from industry actors, consumer advocates, and others. This will provide the CFPB or SEC with a helpful baseline in the event that one of those agencies decides to promulgate rules to reduce the potential risks of or otherwise encourage marketplace lending. Although we have no reason to expect that new SEC or CFPB rules are imminent,[5] those agencies nonetheless are focused on FinTech and will be interested in the industry responses.

The combined 1,000 pages of comments submitted in response to the RFI provide a unique insight into the development of online lending, as well as a range of proposals and suggestions for its future growth and regulation. Thus far, the only comment from Treasury that discusses the responses to the RFI is an October 2015 speech by Antonio Weiss, Counselor to the Secretary. His remarks support our conclusions above:

[5] The CFPB is currently working on a proposed rule that will significantly change the market for online and brick and mortar payday lending, auto title lending, and high-cost installment lending, but the Treasury RFI explicitly excluded these types of loans – to the extent they are made by marketplace lenders – from the scope of the RFI. Treasury RFI, p. 1.

> *At Treasury, we will seek to foster, not impede, innovation that increases competition and broadens access to affordable credit for creditworthy borrowers and businesses. But we will also be vigilant in ensuring that innovation does not undermine important privacy and consumer protection priorities.*[6]

We expect Treasury may soon release a white paper that summarizes the responses and possibly makes recommendations for executive actions or regulatory or legislative changes to encourage additional small business lending. Although Treasury cannot write rules or enact statutes itself, it can recommend actions for the White House to implement through executive order or other executive actions. In addition, a future Congress or other agency might be persuaded by a well-researched and carefully reasoned report from Treasury's Small Business Office.

As we await Treasury's report, Reed Smith's FinTech Team thought it would be helpful to sit down and read the RFI responses, and to provide our own report on the themes, arguments and proposals contained in their pages. We hope you find it as interesting to read as it was to write!

[6] available at : https://www.treasury.gov/press-center/press-releases/Pages/jl0238.aspx

II. Treasury's RFI on Marketplace Lending

The Treasury RFI begins with a 5-page introduction, which we have abridged here:

> *The Treasury Department is seeking public comment through this Request For Information (RFI) on (i) the various business models of and products offered by online marketplace lenders to small businesses and consumers; (ii) the potential for online marketplace lending to expand access to credit to historically underserved market segments; and (iii) how the financial regulatory framework should evolve to support the safe growth of this industry. . . .*
>
> *We also seek any additional information beyond these questions that market participants believe would assist in our efforts to become better informed of the impact of online marketplace lending on small businesses, consumers, and the broader economy.*
>
> *Historically, many American households, small businesses, and promising new enterprises have faced barriers in accessing affordable credit from traditional lenders. To date, the large majority of online marketplace consumer loans have been originated to prime or near- prime consumers to refinance existing debt. . . . Some online marketplace lenders, however, are developing product structures and underwriting models that might allow making loans to non-prime borrowers at lower rates.[7]*
>
> *With respect to small businesses, a number of studies have shown that these borrowers are more dependent on community banks for financing than larger firms. . . . Small business lending, however, has high search, transaction, and underwriting costs for banks relative to potential revenue – it costs about the same to underwrite a $5 million dollar loan as a $200,000 loan[8] – and many small business owners report they are unable to access the credit needed to grow their business. . . . More than half of small businesses that applied for credit in 2014 sought loans of $100,000 or less. . . . Technology-enabled credit provisioning offers the potential to reduce transaction costs for these products, while investment capital may offer a new source of financing for historically underserved markets.*
>
> *Online marketplace lending . . . initially emerged with companies giving investors the ability to provide financing that would be used to fund individual borrowers through what became known as a "peer-to-peer" model. However, it has since evolved to include a diverse set of*

[7] As noted elsewhere, the CFPB is contemplating issuing a rule that would regulate "payday" and related loans, including loans with terms greater than 45 days and an APR greater than 36%, if the loan also provides for repayment directly from a consumer's account or paycheck or includes a non-purchase money security interest in a vehicle. Such consumer loans are outside the scope of this RFI.

[8] "The Future of Finance," Goldman Sachs Equity Research, March 3, 2015.

> *individual and institutional credit investors who seek to provide financing that ultimately is used to fund small business and consumer loans of various types to gain access to additional credit channels and favorable rates of return.*

Treasury posed 14 “Key Questions” (closer to 40 questions counting subparts) that explore the three big topic areas framed by the RFI: business models, expanding access to credit, and potential regulatory evolution. We have synthesized some of the main comments submitted in response to the RFI.

III. Summary of Responses to the Treasury RFI

A. Business Models

Three of Treasury's questions focus on the marketplace business models and products. *See* RFI Question 1, 5, and 7. These questions asked:

- How policymakers should be thinking about different business models and market segmentation;
- What kinds of marketing channels are used to reach new customers; and
- How marketplace lending relies on services or relationships provided by traditional lending institutions or insured depository institutions.

In its comment, the Conference of State Bank Supervisors provides a helpful overview of the marketplace lending business models, organized on the basis of funding sources:[9]

- Balance Sheet Lenders –lenders that originate loans and retain credit risk in their own portfolios;
- Online Platforms (peer-to-peer) – platform lenders utilize a pass-through securitization structure where loans are immediately sold to investors, and retain the credit risk and provide funding;
- Bank-Affiliated lenders – banks originate and hold, distribute and/or return loans to the marketplace lenders; and
- Bank-Partnership – many marketplace lenders utilize a bank partnership model, either in whole or in part, in which loans are funded by a bank and sold to an investor or to the marketplace lender.

Many comments acknowledge that automation and technology have lowered the operating cost of online lenders, thereby increasing the likelihood that more customers can be served.[10] The Online Lenders Alliance (OLA), responding on behalf of "the growing industry of online companies offering consumers small-dollar, short-term loans," argues that banks have been slow to adapt to "rapid changes in technology," and that marketplace lenders have been able to "disrupt the traditional lending industry in a very short period of time."[11]

Nonetheless, as the list above illustrates, many marketplace lenders work with the banks cooperatively. For example, Affirm, Inc., provides point-of-sale financing to consumers through a partnership with a state-chartered bank, and states that this partnership gives the company the benefit of being able to "export its home-state's interest rate on loans."[12] Many other platform lenders similarly acknowledge these bank partnerships, and indeed this

[9] *See* Conference of State Bank Supervisors (CSBS), p. 2. Readers are encouraged to review the comment letters and the myriad primary source materials that the letters cite. We do not cite any of the primary sources here.

[10] *See e.g.*, Kabbage, p. 2.

[11] OLA, pp. 1, 3.

[12] *See* Affirm, p. 2-3.

tension between competition and cooperation has, inevitably, gained a label: "coopetition."

"Coopetition"

Several comments discussed the notion of "coopetition" between traditional banks and marketplace lenders. GLI Finance, an investment company, emphasized the cooperative nature of the relationship since traditional banks are "a source of capital, a repository for funds, and a source of new customers."[13] Godolphin Capital Management noted that "[s]everal platforms have entered into alliances with banks and other institutions such as accounting software providers to both provide leads as well as 'white-label' the intellectual property on behalf of these institutions. This "coopetition" model is likely to grow further as smaller regional banks can use marketplace lending platforms with a national footprint to diversify both regionally and across asset classes."[14]

The bank partnership model has proven attractive to bigger players like Lending Club and Prosper. However, it has not been a good fit for some small-dollar lenders because of issues that come with a bank charter. According to Opportun, a marketplace lender that targets the Hispanic market, "prudential regulation and legal risk management often create profitability challenges when considering the traditionally underserved consumer's need for non-traditional underwriting and credit models, and a retail-based channel option."[15]

Other comments view the industry business models in terms of the different markets served by marketplace lending products. PeerIQ, an information services company, describes the business models as differentiated primarily by:

- Market segments (*i.e.*) consumer, small business, commercial loans;
- Products (*e.g.*) installment loans, lines of credit, merchant cash advances;
- Origination channels (*e.g.*) direct mail, online, partner affiliate, branch, and paid search;
- Credit risk (*i.e.*) prime, near-prime, sub-prime, thin-file;
- Funding mechanisms (*i.e.*) balance sheet, marketplace, hybrid, bank-affiliated[16]

PeerIQ goes on to point out the "diversity of value propositions and business models" in each borrower segment:

> *". . . Lending Club has established partnerships with data companies to improve customer acquisition and underwriting. Prosper has recently acquired a spending-and-tracking app company, to improve customer engagement. Lenddo is using social media criteria to assess creditworthiness. Upstart factors in education and experience in determining creditworthiness for thin-*

[13] GLI Finance, p. 3.

[14] Godolphin, pp. 2-3.

[15] Opportun, p. 13.

[16] PeerIQ, p. 2.

> *file borrowers. Affirm is creating speedy point-of-sale algorithms as an alternative to credit cards. As for small business lending, PayPal is relying on its merchant payment data to extend credit to small business; Amazon offers lending services to "help sellers grow"; and Dealstruck provides lending tools for the mid-prime market, which includes [small and midsize businesses] who are not eligible for traditional bank financing."*[17]

Another example of coopetition is offered by Income& Technologies, Inc., a marketplace lending platform focusing on high credit-quality 1-4 family residential mortgages that do not meet the definition of a Qualified Mortgage. Income& does not originate loans but partners with institutions originating high-quality non-QM mortgages (mostly small banks and credit unions) and sells investors the cash flow from those mortgages with the goal of expanding available credit for the small banks and credit unions to make more loans.[18]

OnDeck, a marketplace lender focused on small business lending, relies on a diversified model that includes large bank credit facilities "which allow OnDeck to hold the majority of our loans on our balance sheet" and to "retain the first loss position" on those facilities.[19] The company also sells whole loans to institutional investors, and it has completed an investment-grade small business loan securitization in which it retained a 5% first loss risk position.[20]

The collective comments on the industry business models therefore create a more nuanced picture than the "fintech v. banks" headlines sometimes suggest. Many commenters, and Treasury itself, recognize that marketplace lending—and technology generally—provides a promising array of tools with which to provide access to credit in underserved markets. This broad policy goal is at the heart of the RFI, and addresses challenges faced specifically by small businesses and the underbanked.

B. Expanding Access to Underserved Market Segments

(1) Small Business Lending

In its RFI, Treasury states that while many small businesses rely on community banks for financing, small business lending has "high search, transaction, and underwriting costs" that make it difficult for banks to serve small business needs in a profitable way—noting that "it costs about the same to underwrite a $5 million dollar loan as a $200,000 loan.[21] The RFI recognizes that "technology-enabled credit provisioning offers the potential to reduce transaction costs for these products, while investment

[17] *Id.*, p.4 (footnotes and citations omitted).

[18] Income&, p. 2.

[19] OnDeck, p. 5.

[20] *Id.*

[21] Treasury RFI, p. 5, citing "The Future of Finance," Goldman Sachs Equity Research, March 3, 2015.

capital may offer a new source of financing for historically underserved markets," and notes that the "2014 Small Business Credit Survey indicated that almost 20 percent of applicants sought credit from an online lender."[22]

Many commenters agreed, observing that large financial institutions operate within a cost structure that may preclude them from making loans below a certain size to small businesses. Kabbage comments that big banks arguably could benefit from deploying the technologies utilized by marketplace lenders, and that policymakers therefore may want to investigate ways to encourage collaboration between banks and new lenders that possess such technologies.[23]

LendingTree, a marketplace of online lenders, states that FinTech is filling an important need particularly for small business owners. In a survey conducted by LendingTree in February through March of 2015 (involving 155 small business owners who had applied for loans within the past year), the most frequently cited struggles were:

> *(i) gathering required documentation;*
>
> *(ii) long application process; and*
>
> *(iii) speed of approval.*[24]

LendingTree claims that increased automation will alleviate these issues, allowing for faster application-to-funding cycles without an inherent reduction in underwriting quality or consumer protection:

> *In turn, borrowers who are able to experience more efficient application processes are more likely to have access to credit when they need it, and less likely to abandon the credit markets due to burdensome processes that leave them discouraged with their chances of obtaining funding.*[25]

Marketplace lenders in the small business space claim to provide better matching between a loan term and expected payback: for example, a higher-interest rate short term loan may end up costing less in total interest and fees than a lower-interest loan with a longer term.[26]

Many other FinTech companies voiced a similar need being fulfilled by FinTech. OnDeck claims that by offering loans with shorter terms, it can decrease credit risk and provide capital to "otherwise non-bankable small businesses," with repayments structured on a daily or weekly basis.[27] OnDeck has made more than $3 billion in loans to small businesses to date, and it cites post-financial crisis data that shows only 36% of small business borrowers have been able to get all the

[22] RFI, p. 6.

[23] *See* Kabbage, pp. 1, 6.

[24] LendingTree, p. 3.

[25] *Id.*

[26] *See* OnDeck, p. 3.

[27] OnDeck, p. 4.

financing they sought, leaving $80-$120 billion in unmet demand for small business lines of credit.[28]

(2) Underbanked Consumers

A series of RFI questions focused on the theme of expanding access to credit to historically underserved market segments.[29] Many of the comments in response take the position that FinTech companies are serving the underbanked consumer market despite the fact that, as the RFI points out, most online lending to date has been to "prime or near-prime consumers to refinance existing debt."

In its comment, LendAcademy lists several lending platforms focused on expanding access to consumer credit:

- Upstart is a lender focused on young people with a good education who are starting out and have little or no credit history.
- Avant targets the "middle class" borrower who has fewer options than prime borrowers.
- Freedom Financial works with borrowers who have experienced financial distress, a group that many platforms ignore.
- Opportun, formerly Progresso Financiero, targets the Hispanic market, a market that has historically been underserved.
- LendUp helps sub-prime borrowers transition from payday lending through education and a system designed to improve borrowers' credit scores.
- Lenddo is working to establishing an alternative credit scoring system for people without a credit score.
- Kiva Zip is an impact investment platform to help customers and brand ambassadors support their local business.[30]

Indeed, because both traditional lenders and many larger marketplace lenders rely on a minimum FICO score, marketplace lenders such as Opportun who are focused on small-dollar lending to traditionally underserved communities state that "many of the 64 million credit-eligible borrowers who are unscoreable or have no or thin files, living in the US are automatically excluded from qualifying for most online marketplace loan pools."[31] Opportun focuses on the "25 million unbanked or underbanked Hispanic individuals" in the US, a customer base with an average income of $32,100 per year, and an average loan amount of $2,000,[32] and targets these customers by relying on alternative data sources—such as utility information, transactional data, or bank account information—to "score" potential borrowers; Opportun also provides documentation in Spanish and English, as well as mobile phone access[33], physical

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[28] *Id.*, pp. 1, 2, 5.

[29] *See* RFI Questions 2, 3, 4, and 6.

[30] *See* Lend Academy, p. 13.

[31] Opportun, p. 3.

[32] *Id.*, pp. 1, 7.

[33] Opportun cites a Federal Reserve study that found that 82% of Hispanic mobile phone users have a smartphone, compared to 68% of non-

locations in the communities it serves, and cash repayment options to serve its customers.[34]

Opportun and others cite an array of statistics on the underbanked in America, including: one in thirteen US households remains unbanked; an additional 20 percent of American households are "underbanked—meaning that they rely upon alternative financial services outside of the banking system to fully meet their financial needs"; and 25% of credit-eligible consumer in the US have little or no history at the three major US credit reporting agencies. *Id.*

Although many comments point out that Prosper and Lending Club cater primarily to borrowers with good credit, for its part Lending Club states that in 2015 it expanded its platform's reach to low- and moderate-income individuals through partnerships with Citi bank and Varadero Capital, "designed to deliver $150mm of affordable credit to underserved, low- to moderate- income borrowers."[35]

New Jersey-based Cross River Bank's comment reinforces the argument that online lenders are expanding the credit box:

> *"Marketplace lenders are able to develop models which they find to be more effective at predicting credit outcomes than traditional scoring models, such as FICO based models. These enhanced scoring models enable marketplace lenders to make loans to borrowers who would not receive credit under traditional market standards, but are demonstrated to be worthwhile credits when considering additional information."*[36]

Affirm emphasizes that its online point-of-sale loans are widely available and that its services are utilized by borrowers who may be turned down by other lenders. "Affirm's loans span the spectrum of credit worthiness from subprime to super prime."[37] Affirm believes that broad access to its services benefits both its banking partner (Cross River Bank), as well as traditionally underserved borrowers. "By lending to consumers across the credit spectrum,

Hispanic white and 66 percent of non-Hispanic black phone users. *See* Opportun, p. 15.

[34] Opportun, p. 3, 8.

[35] Lending Club, p. 14. Low- to moderate income individuals are defined in the comment as those with reported adjusted household income less than 80% of the median income of their zip code and live in majority or greater low to moderate income census tracts as of June 30, 2015. Lending Club, p. 14, fn. 9.

[36] Cross River Bank, p. 4.

[37] Affirm, p. 1.

Affirm has a more diverse credit and risk portfolio. Most importantly, its products can be used by all consumers and small businesses."[38]

Like Affirm, Upstart partners with Cross River Bank to offer online loans. Both Affirm and Upstart say that they leverage innovative technology to underwrite their loans, which results in credit being extended to borrowers who may be rejected under traditional underwriting techniques.[39] For example, Affirm uses technology to survey an applicant's liquidity, which Affirm believes gives it a more accurate picture of the applicant's creditworthiness than a credit score alone. Affirm believes that its "dynamic credit" model, which places insular negative credit events in a larger context of a borrower's overall creditworthiness, will increase consumers' access to credit, and that "traditionally non-credit worthy consumers may actually be offered credit to assist with improving their financial well-being."[40]

Upstart similarly points out that "[b]y complementing (not replacing) traditional underwriting factors with factors that are correlated with financial capacity and propensity to repay, the [Upstart] underwriting model better understands and quantifies risk associated with all borrowers – those with credit history, and those without."[41]

In its comment, credit bureau Equifax notes that the borrower may be additionally protected by better income verification: "Another industry best practice for assessing a consumer's ability to repay is the use of employer payroll information to verify a consumer's income, which is more accurate than consumer stated income."[42]

The Center for Financial Services Innovation (CFSI) believes that "online marketplace lenders may continue to move down the credit spectrum," which would be more beneficial to underserved consumers than alternatives such as payday lending.[43] CFSI believes, however, that "the online marketplace lending environment has not yet reached its full potential in serving underserved consumer segments" because most marketplace lenders do not offer small loans.[44] Thus, when consumers with lower credit scores or those who want to borrow smaller amounts go online, they are still pushed to payday or high-cost installment lenders.[45]

(3) Micro-Lending

An example of a lender focused on very small dollar loans is Kiva, a nonprofit

[38] *Id.*, p. 4.

[39] *See, e.g.,* Upstart, p. 2.

[40] Affirm, p. 6.

[41] *Id.*

[42] Equifax, p. 3.

[43] CFSI, p. 3.

[44] *Id.*, p. 4

[45] *Id.*

organization that allows individuals to fund microloans to borrowers both in the United States and internationally, in increments as small as $25 per lender. Unlike most online marketplace lenders, Kiva does not charge any interest or fees to borrowers and does not allow its users to earn a return on their loans. Users make credit decisions based on "social underwriting" including: the borrower's online presence, endorsements by local community members, and a detailed loan profile.[46] When Kiva first launched its direct lending program, it set aside a small amount of its own funds to lend in case users did not fund the available loans. Interestingly, the loans the crowd chose not to fully fund, and which were therefore partially funded by Kiva, proved to have a higher default rate than those loans that were funded entirely by the crowd.[47]

C. Potential Changes to the Financial Regulatory Framework

The RFI questions what role the federal government might play to facilitate positive innovation in lending.[48] Many commenters responded that due to partnerships with federally chartered banks, many of the FinTech products effectively are issued by federally regulated banks and are therefore subject to the same regulatory protection as other products provided to traditional bank customers.[49] Thus, these commenters did not see an immediate need for new regulation at the federal level.

Another common theme was that, given that the marketplace lending industry is still developing, trying to impose broad regulations at this juncture in the industry's maturity could either unintentionally stifle growth or harm both borrowers and investors.[50]

OnDeck, for example, expressed the view that the "current environment for commercial lenders is conducive to continued innovation" and that it would be "premature and potentially harmful to small business owners if additional regulation were imposed to codify particular lending models or credit products at this early-stage of industry development."[51] WebBank, a Utah-chartered industrial bank located in Salt Lake City, agrees. WebBank, which originates a significant percentage of online marketplace loans, maintains that "from a regulatory perspective, the origination of loans through marketplace platforms does not break new ground" and that online marketplace lenders "are [already] subject to the same legal requirements and borrower protections as other loans."[52]

To the extent regulatory changes were suggested by commenters, however, we

[46] Kiva Microfunds, pp. 3-4.

[47] Kiva Microfunds, p. 4.

[48] *See* RFI 9, 10, 11.

[49] *See*, *e.g.*, Lending Club, p. 4.

[50] *See*, *e.g.*, KPMG, p. 11.

[51] OnDeck, p. 9.

[52] WebBank, p. 1.

have tried here to group those proposals and viewpoints into loose categories:

(1) Addressing State Laws and Judicial Rulings

Beyond the regulatory regime applicable to banks, a number of comments expressed the view that marketplace lenders are not only subject to significant state and federal laws, but that many state laws are inconsistent. Many lament the patchwork of state licensing and consumer protection laws for example—including varying interest rate caps and usury laws, different origination and servicing practices and disclosure requirements, and restrictions on advertising—that apply to marketplace lenders not following the bank partnership model.[53] The comments also contain much discussion about the Second Circuit's recent decision in *Madden v. Midland Funding*: [54]

Madden Madness…

In *Madden v. Midland Funding*, the Second Circuit held that when a national bank sold a loan portfolio to a debt buyer, the purchaser could not avail of the preemptive powers of the National Bank Act and therefore lost the ability to apply the bank's home state interest rate. Many have criticized the decision, calling it "another drag on marketplace lenders"[55] and arguing that the decision ignores the "valid when made" doctrine—which states that a loan that does not violate state usury laws when made, remains valid when transferred or sold to a party in another state. The parties have filed a petition for the case to be heard by the United States Supreme Court.

Affirm also addresses the patchwork quality of the current regulatory landscape in its comment: "[O]nline marketplace lenders have varying degrees of regulation, which is largely dependent on what type of funding the marketplace lender uses… [s]ome must adhere to the regulatory regime of each state in which they lend while others must adhere to the regulatory regime of the home state of their bank affiliated partner."[56] Similarly, Upstart claims that the current regulatory regime subjects marketplace lenders to "overlapping regulation."[57] "As a result [] multiple layers of compliance oversight apply to marketplace lending activities."[58]

[53] *See e.g.*, Opportun, p. 12; Orchard Platform, p. 7.

[54] *See* Appendix C, *Madden v. Midland Funding*, Case No. 14-2131 (2nd Cir., May 22, 2015).

[55] OLA, p. 8.

[56] Affirm, p. 7.

[57] Upstart, p. 3.

[58] *Id.*

As a solution to the "uneven regulatory landscape", Affirm suggests that"[t]he federal government could substantially level the playing field among marketplace lenders by imposing a single federal regulatory agency that supervises and enforces federal law as it relates to marketplace lending."[59]

Perhaps not surprisingly, the state regulators are generally opposed to any efforts to preempt state laws. The Conference of State Bank Supervisors (CSBS) writes that "state regulators urge Treasury to support policies that improve the efficiency of existing licensing regimes and promote protection without undermining the states' ability to regulate and promote consumer protection entities that make loans to the citizens within their borders."[60] At the same time, many commenters agreed that to the extent marketplace lenders already are subject to existing regulations, more regulation is not what is needed—if anything, regulations need to be updated to reflect the modern economy and industry realities.

OnDeck argues, for example, that the existing landscape of federal and state laws was "created at a time that did not contemplate our modern Internet economy, and therefore includes a number of archaic inefficiencies."[61] OnDeck writes that policymakers should create cross-agency FinTech working groups that can engage with industry and streamline and harmonize existing laws.[62] Indeed, the comments address a number of regulatory schemes enacted prior to the development of today's internet and mobile-phone economy. Opportun cites the ESIGN Act, for example, which requires that, prior to consenting to the use of an electronic record, a consumer must be provided with a statement of the hardware and software requirements for access to such electronic records. While the regulation may have been relevant to desktop computer users in the past, "it is unclear how much information a lender needs to provide to ensure that a consumer is able to access and retain an electronic record via mobile device."[63] Some commenters want to revamp the Electronic Fund Transfer Act (EFTA) and Reg. E, arguing the law is outdated based on today's access and convenience to electronically access payments; the National Consumer Law Center (NCLC), a consumer advocacy non-profit disagrees, however, arguing that the "EFTA ban on compulsory electronic repayments is an important protection that helps consumers to maintain control over their bank accounts.[64]

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[59] Affirm, p. 7.

[60] CSBS, p. 8.

[61] OnDeck, p. 10.

[62] *Id.*, pp. 10-11

[63] Opportun, p. 15.

[64] NCLC, p. 5.

(2) A Federal Charter for Online Lenders

In another approach to updating the regulatory landscape and ensuring consistency, some commenters called for a national charter for online lenders. The Center for Financial Markets of the Milken Institute's proposed "National Lender Charter" is one example; it would allow non-banks to operate in the lending industry under the following guidelines[65]:

National marketplace lenders could:	National lenders could not:	National lenders would be responsible for:
• Make loans directly to consumers and businesses. • Advertise loans and solicit borrowers. • Set interest rates and terms for their loans that could be transferred to loan purchasers or securitizers with interest rate export powers similar to banks. • Service debt. • Seek investors.	• Take deposits. • Access the Federal Reserve discount window. • Offer depository services such as checking accounts, or ATMs. • Pay interest on investor money except on active investment in the lender. • Represent itself as a bank or depository institution. • Engage in investment banking except for its own securities.	• Performing necessary checks on borrowers and investors. • Complying with fair lending and privacy laws. • Maintaining client relationships. • Providing appropriate disclosures to both borrowers and investors.

[65] *See* Milken Institute, pp. 10-11.

(3) A New British Invasion…?

Some commenters lauded the regulatory approaches to marketplace lending in the UK, and suggested adopting some here in the US:

Referral Network – OnDeck notes that the British government supports a referral network between banks and marketplace lenders. "The UK government has recognized the significant benefit this will provide to small businesses and has accordingly implemented measures to increase decline referrals."[66] Orchard Platform also cites the U.K.'s Financial Conduct Authority's (FCA) "light touch approach" to regulating marketplace lending.[67] After taking control of the regulation of marketplace lending, the FCA stated in February 2015 that "we see no need to change our regulatory approach to crowdfunding, either to strengthen consumer protections or to relax the requirements that apply to firms."[68]

Government and Technology Platform Initiatives – the US government has access to small business data, for example at the IRS, and some commenters argue that the government should make that data available where the customer consents in order to facilitate small business lending and fraud detection and prevention. "A similar initiative is already underway in the UK" OnDeck says,[69] and suggests that marketplace platforms and technologies could help "government agencies deploy funds to small businesses in the aftermath of natural disasters or emergencies."[70]

Tax Free Investment Savings Accounts – Lending Club suggests that the US government should emulate a program in the U.K., in which investors are able to invest in "P2P loans" tax-free though an Investment Savings Account (ISA) called an Innovative Finance ISA, or "IFI".[71] Investors can deposit up to £15,240 per year (standard for ISAs), or transfer in money from other ISAs. Unlike a US IRA, there is not a tax penalty for withdrawing before retirement. Lending Club suggests that "[t]he proposed US marketplace investing incentive could similarly attract investment in underserved consumers in the same geographies, and in small businesses nationwide."[72]

(4) Other US Tax Reform

Lending Club's response to the RFI contains specific recommendations on how the federal government can help facilitate the safe growth of the marketplace lending industry, specifically through revisions to the tax code and collection process.

First, Lending Club recommends automating the process by which tax return

[66] OnDeck, p. 10; *see also* Lend Academy, pp. 18-19.

[67] Orchard Platform, pp. 7-8.

[68] *Id.*, p. 8

[69] OnDeck, p. 10.

[70] Id.

[71] Lending Club, p. 29

[72] *Id.*

data is shared, thereby enabling lenders to lower cost and improve access to credit across consumer and small business borrowers.[73] Currently, the IRS allows taxpayers to request a summary transcript of their filed tax returns to be provided to a third party – but processing these 4506T forms is manual and can take 2-8 days.[74] As lending is increasingly structured around providing applicants with instant loan offers online, this delay prevents the use of tax data in credit models that price and approve loan applications instantaneously.[75]

Second, the federal government could facilitate an increase in investment and economic growth in underserved communities and certain economic sectors by creating incentives in the tax code that parallel existing tax programs.[76] For example, currently, investors only have the ability to offset charge-offs against capital gains.[77] To encourage investment in underserved areas, Lending Club proposes "that investors who provide capital in defined underserved areas and to low- to moderate-income small businesses borrowers be taxed at the capital gains tax rate, rather than the current marginal income tax rate, if the loan is held for over 12 months."[78] To encourage investment and saving, Lending Club proposes that investors in marketplace loans have "the ability to offset losses and charge-offs against interest income and gains and earn tax-free returns" against a certain dollar amount.[79]

Finally, for ease of operation and to lower costs, Lending Club proposes government regulations allowing "online marketplace companies to make the default delivery method of tax forms electronic," rather than paper copies, as is required by current regulations.[80] Other commenters likewise supported providing access to federal tax return information to help small-dollar loan customers who may have difficulty retrieving paper copies of income or residential information.[81]

(5) Small Business Borrower's Bill of Rights

Many commenters cited the Small Business Borrower's Bill of Rights as a potential guideline for regulation.[82] The Small Business Borrower's Bill of Rights is a consensus on responsible small business lending practices assembled by a coalition of lenders, marketplaces, and brokers.[83]

[73] Lending Club, p. 28.

[74] *Id.*

[75] *Id.*

[76] One such program is the Treasury Department's New Markets Tax Credit program, which attracts investment in commercial real estate development in low-income census tracts. Lending Club, p. 29.

[77] *Id.*

[78] *Id.*

[79] *Id.*

[80] *Id.*, p. 30

[81] Opportun, p. 14.

[82] *See* Lending Club, p. 49; Small Business Majority, p. 2; CFSI, p. 2.

[83] *Id.*, p. 41

Lending Club recommends that the marketplace lending industry fully adopt the practices and principles enumerated in the Small Business Borrower's Bill of Rights, and that the regulatory agencies monitor the industry's progress in extending credit to historically underserved populations.[84]

(6) Data Privacy Protection

Given the recent large scale data breaches many commenters addressed data privacy and fraud protection. Equifax specifically noted that determining and then protecting the identity of consumers will necessarily be a multi-step process in marketplace lending: "As loan applications, supporting documentation, and decisions move online, it is important that lenders use all available tools to validate and authenticate consumer identity. Failure to properly do so will open up this channel to significant fraud perpetration."[85]

The NCLC stressed its concerns regarding the use of consumer data in ways it argues are inconsistent with the Fair Credit Reporting Act (FCRA). It also emphasized the potential consumer harm that it claims "lead generators" can cause by selling consumer data to companies that use it to perpetrate fraud.[86]

[84] *Id.*, pp. 14, 42

[85] Equifax, p. 3.

[86] NCLC, p. 2.

(7) Reforms of the Secondary Market

Commenters are split on the necessity and effects of regulation on the secondary market for marketplace loans. While commenters agree that there is currently no robust secondary market for marketplace loans, they are split on the reason for this.[87] Commenters agree on the advantages of a secondary market for marketplace loans to provide access to liquidity, but offer little consensus on how to establish or administer such a market.

Kabbage writes that however the secondary market is developed, it is important that there is some alignment between the performance risk associated with a particular loan and the organization that has determined that risk. Marketplace lenders without any capital risk put themselves in a position of mismatched incentives, the argument goes, because slightly lower stated risk can greatly increase the perceived return to the investors, and can also create long-term challenges if the assets do not perform in the manner promoted.[88]

Cross River Bank suggests that the secondary market is robust, and that "[t]he Federal government should promote standards for securitization of these assets to promote a liquid and efficient secondary

[87] *See* Lend Academy, p. 29, Kabbage, p. 2.

[88] *See* Kabbage, p. 2.

market for loans to, in turn, expand the availability of credit."[89]

However, other commenters believe that a broker-dealer with an alternative trading designation could establish a secondary market for marketplace loans today, but that broker-dealers are not presently incentivized to do so. These commenters point to a current lack of profitability and regulation as the primary hurdle for such a market.[90] Lending Club and Prosper point out that, due to cash from institutional investors, they do not have an immediate need for a secondary market to provide liquidity.[91]

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[89] Cross River Bank, p. 7.

[90] Pepper Hamilton, p. 9.

[91] Lending Club, p. 47; Prosper, p. 15.

IV. Conclusion

Inevitably, many of the industry responses to Treasury's RFI promote their authors' technologies and products, and promise to revolutionize lending as we know it. Some mild puffery is to be expected. But taken as a whole, the advent of marketplace lending marks a significant evolutionary moment in the historical development of consumer financial services. The industry comments are sincere, insightful and forward-looking. And the exchange with Treasury pulls the curtain back on a financial services industry that has been changed irrevocably, and very quickly, by technology.

In its comment, the OLA recalls a parallel in the "development of the national credit card industry in the 1980s." [92] OLA cites the 1978 Supreme Court case of *Marquette v. Omaha Serv. Corp.*, and the subsequent passage of the Depository Institution and Deregulatory Monetary Control Act of 1981, which granted "exportation powers to state chartered banks . . . and prompted the explosion of the credit card marketplace."[93] But online marketplace lending also evokes a more distant historical parallel as well.

During the Depression of the 1930s, almost 10,000 American community banks closed their doors forever. Those banks had operated in towns and cities across the country, offering financial services (advice, loans, business networks) to the consumers of the day (local farmers, businesses and families). Community banks pooled resources in order to facilitate lending, but they also had the benefit of social data about their communities and customers that allowed them to make credit decisions and provide a much needed service.

The declining number of US banks has continued. In a December 2013 article, the Wall Street Journal noted that the "number of banking institutions in the US has dwindled to its lowest level since at least the Great Depression," shrinking to less than 7,000 "for the first time since federal regulators began keeping track in 1934."[94] That number has continued to fall; as of September 2015, there were just 6,270 FDIC-insured banks in the US.

Since that Wall Street Journal article was published just two years ago, however, an estimated $12 billion has been invested in FinTech companies and marketplace lenders globally. However, although these companies deploy new underwriting models and substitute social data of a different kind to "know" their customers and make credit decisions, the new tools arguably serve an age-old need to fulfil the demand of small businesses and individual borrowers to access credit.

The US Department of the Treasury explicitly recognizes the promise and

[92] OLA, p. 4.

[93] *Id.*

[94] WSJ.com ("Tally of US Banks Sinks to Record Low"), December 3, 2013, by Ryan Tracy.

potential of marketplace lending, and its goals and the views of a full spectrum of interested parties are collectively expressed in the RFI and the comments submitted in response. We look forward to the government's reaction to those comments, and we will continue to watch its evolving relationship with marketplace lenders with anticipation in the coming months and years.

Thank you for your interest,

David S. Reidy
Nicholas F.B. Smyth
Heather Cantua Phillips
Tyler M. Layton

Reed Smith LLP
FinTech Team
San Francisco, January 14, 2016

APPENDIX A The Reed Smith Team

David S. Reidy
Partner / Practice Leader, FinTech
dreidy@reedsmith.com

San Francisco
+1 415 659 5933

David is a partner in the firm's Financial Industry Group and Practice Leader of the firm's FinTech group. He represents financial services companies and other clients in consumer class and individual actions asserting privacy, fair lending, credit reporting, debt collection and unfair business practices claims, as well as Telephone Consumer Protection Act (TCPA) and California Invasion of Privacy Act (CIPA) cases. In addition to his extensive class action litigation experience, David counsels FinTech and other clients on compliance matters related to consumer financial services. David has tried cases to verdict in federal and state court, defeated dozens of cases at the summary judgment and class certification stages, and negotiated favorable class and individual settlements in many other matters.

Nicholas F.B. Smyth
Associate
nsmyth@reedsmith.com

Pittsburgh
+1 412 288 3167

Nick is a member of the Financial Industry Group, practicing in the area of Financial Services Litigation. Previously, he spent four years as an Enforcement Attorney at the Consumer Financial Protection Bureau (CFPB), and he also helped draft the CFPB's enabling legislation at the Treasury Department. Nick helps bank and nonbank clients prepare for and respond to examinations and investigations by the CFPB, including by conducting mock exams and assisting clients with remediation of self-identified compliance issues and difficult decisions regarding self-reporting. He counsels banks and nonbanks that provide indirect auto finance on complying with the CFPB's fair lending (ECOA) guidance, and he has helped clients navigate CFPB fair lending exams, including responding to PARR letters. Nick has also advised clients on other consumer financial laws, including UDAAP, FCRA, FDCPA, TILA, TISA, CLA, EFTA, RESPA, and implementing regulations.

Heather Cantua Phillips
Associate
hphillips@reedsmith.com

San Francisco
+1 415 659 4925

Heather focuses her practice in the area of financial services litigation, representing banks and other financial institutions in consumer class and individual actions, including mortgage banking, credit reporting, debt collection and unfair business practices litigation. Recently, she defeated consumer class actions brought against financial institutions under the Telephone Consumer Protection Act and Fair Credit Reporting Act. In 2014, Heather helped to defeat class certification and obtained summary judgment in a putative class action alleging violations of the Fair Credit Reporting Act. (*Germain v. Bank of Am.*, N.A., No. 13-CV-676-BBC, 2014 WL 5802018, at *1 (W.D. Wis. Nov. 7, 2014)).

Tyler M. Layton
Associate
tlayton@reedsmith.com

San Francisco
+1 415 659 5959

Tyler is an associate in the Financial Industry Group, whose practice focuses primarily on representing banks and other financial institutions in mortgage banking, consumer protection, credit reporting, debt collection and unfair business practices litigation. Tyler has experience representing and counseling clients in all phases of federal and state litigation. Tyler's practice also focuses on counseling emerging and established FinTech clients.

APPENDIX B
Treasury's RFI

PTC implementation status update	Respondent universe	Total annual responses	Average time per response	Total annual burden hours
Questionnaire to be completed by railroads required to implement PTC.	38 Railroads	456 Surveys	10 minutes	76

Form Number(s): N/A.

Respondent Universe: 38 Railroads.

Frequency of Submission: Monthly.

Total Estimated Responses: 456 Surveys.

Total Estimated Annual Burden: 380 hours.

Status: Emergency Review.

Pursuant to 44 U.S.C. 3507(a) and 5 CFR 320.5(b), 1320.8(b)(3)(vi), FRA informs all interested parties that it may not conduct or sponsor, and a respondent is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

Authority: 44 U.S.C. 3501–3520.

Issued in Washington, DC, on July 15, 2015.

Rebecca Pennington,

Chief Financial Officer.

[FR Doc. 2015–17689 Filed 7–17–15; 8:45 am]

BILLING CODE 4910–06–P

DEPARTMENT OF THE TREASURY

Public Input on Expanding Access to Credit Through Online Marketplace Lending

AGENCY: Office of the Undersecretary for Domestic Finance, Department of the Treasury.

ACTION: Notice and request for information.

SUMMARY: Online marketplace lending refers to the segment of the financial services industry that uses investment capital and data-driven online platforms to lend to small businesses and consumers. The Treasury Department is seeking public comment through this Request For Information (RFI) on (i) the various business models of and products offered by online marketplace lenders to small businesses and consumers; (ii) the potential for online marketplace lending to expand access to credit to historically underserved market segments; and (iii) how the financial regulatory framework should evolve to support the safe growth of this industry.[1] [2]

DATES: Submit comments on or before: August 31, 2015.

ADDRESSES: Submit your comments through the Federal eRulemaking Portal or via U.S. mail or commercial delivery. We will not accept comments by fax or by email. To ensure that we do not receive duplicate copies, please submit your comments only one time. In addition, please include the Docket ID and the term ''Marketplace Lending RFI'' at the top of your comments.

- *Federal eRulemaking Portal:* You are encouraged to submit comments electronically through *www.regulations.gov*. Information on using Regulations.gov, including instructions for accessing agency documents, submitting comments, and viewing the docket, is available on the site under a tab titled ''Are you new to the site?'' Electronic submission of comments allows the commenter maximum time to prepare and submit a comment, ensures timely receipt, and enables the Department to make them available to the public.
- *U.S. Mail or Commercial Delivery:* If you mail your comments, address them to Laura Temel, Attention: Marketplace Lending RFI, U.S. Department of the Treasury, 1500 Pennsylvania Avenue NW., Room 1325, Washington, DC 20220.
- *Privacy Note:* The Department's policy for comments received from members of the public (including comments submitted by mail and commercial delivery) is to make these submissions available for public viewing in their entirety on the Federal eRulemaking Portal at *www.regulations.gov*. Therefore, commenters should be careful to include in their comments only information that they wish to make publicly available on the Internet.

FOR FURTHER INFORMATION CONTACT: For general inquiries, submission process questions or any additional information, please email *Marketplace_Lending@treasury.gov* or call (202) 622–1083. All responses to this Notice and Request for Information should be submitted via *http://www.regulations.gov* to ensure consideration. If you use a telecommunications device for the deaf (TDD) or a text telephone (TTY), call the Federal Relay Service (FRS), toll free, at 1–800–877–8339.

SUPPLEMENTARY INFORMATION:

I. Request for Information

The Treasury Department is seeking public comment through this RFI to study (i) the various business models of and products offered by online marketplace lenders to small businesses and consumers; (ii) the potential for online marketplace lending to expand access to credit to historically underserved market segments; and (iii) how the financial regulatory framework should evolve to support the safe growth of this industry.

In particular, the Treasury Department is interested in responses to the following questions. We also seek any additional information beyond these questions that market participants believe would assist in our efforts to become better informed of the impact of online marketplace lending on small businesses, consumers, and the broader economy.

Online marketplace lenders may be subject to regulations promulgated by various agencies including, but not limited to, the CFPB and the Federal Trade Commission.

Respondents should provide as much detail as possible about the particular type of institution, product (*e.g.,* small business loan, consumer loan), business model, and practices to which their

[1] The Consumer Financial Protection Bureau (CFPB) has broad authority governing standards that may apply to a variety of consumer loans issued through this segment, and it has recently announced that it is considering proposing rules that would apply to payday loans, vehicle title loans, deposit advance products, and certain high-cost installment loans and open-end loans. *See* ''Small Business Advisory Review Panel for Potential Rulemakings for Payday, Vehicle Title, and Similar Loans: Outline of Proposals Under Consideration and Alternatives Considered'' (March 26, 2015), *available* at *http://files.consumerfinance.gov/f/201503_cfpb_outline-of-the-proposals-from-small-business-review-panel.pdf*. The potential content, effects, and policy underpinnings of CFPB rules are outside the scope of this RFI, and comments responding to this RFI should not address these CFPB rulemakings or their potential effects on marketplace lending to consumers. Thus, the RFI only seeks comment on online marketplace lending not covered in the potential rulemakings, which, under the current framework, would include comments on the making or facilitating of a loan by online lender to consumers with a term of more than 45 days and an annual percentage rate (as defined in 10 U.S.C. 987(i)(4)) that (I) does not exceed 36% or (II) exceeds 36% provided the loan neither provides for repayment directly from a consumer's account or paycheck nor creates a non-purchase money security interest in a vehicle. This framework is currently under discussion, however, and the CFPB may ultimately change the scope of any proposed or final CFPB regulation.

[2] The activities on online marketplace lending platforms also may entail the offering of securities that are subject to the federal securities laws.

comments apply. Responses to this RFI will be made public.

II. Purpose

Historically, many American households, small businesses, and promising new enterprises have faced barriers in accessing affordable credit from traditional lenders. To date, the large majority of online marketplace consumer loans have been originated to prime or near-prime consumers to refinance existing debt. Online marketplace lending has filled a need for these borrowers by often delivering lower costs and faster decision times than traditional lenders. Non-prime consumers face other challenges in obtaining traditional bank-originated credit, particularly due to having thin or no credit files or damaged credit. Moreover, high underwriting costs can make it uneconomical to make small-value consumer loans. For example, it can cost the same amount to underwrite a $300 consumer loan as a $3,000 loan. Small-value loans to non-prime consumers thus have often come with triple digit annual percentage rates (APR). Some online marketplace lenders, however, are developing product structures and underwriting models that might allow making loans to non-prime borrowers at lower rates.[3]

With respect to small businesses, a number of studies have shown that these borrowers are more dependent on community banks for financing than larger firms, which have access to other forms of finance including public debt and equity markets. While larger businesses typically rely on banks for 30 percent of their financing, small businesses receive 90 percent of their financing from banks.[4] Small business lending, however, has high search, transaction, and underwriting costs for banks relative to potential revenue—it costs about the same to underwrite a $5 million dollar loan as a $200,000 loan [5]—and many small business owners report they are unable to access the credit needed to grow their business. According to Federal Reserve survey data released in February 2015, ''a majority of small firms (under $1 million in annual revenues) and startups (under 5 years in business) were unable to secure any credit in the prior year.'' [6]

The challenge is particularly acute for small business loans of lower value and shorter terms. More than half of small businesses that applied for credit in 2014 sought loans of $100,000 or less. At the same time, more than two thirds of businesses with under $1 million in annual revenue that applied for credit received less than the full amount that they sought and half received none.[7] Technology-enabled credit provisioning offers the potential to reduce transaction costs for these products, while investment capital may offer a new source of financing for historically underserved markets. The 2014 Small Business Credit Survey indicated that almost 20 percent of applicants sought credit from an online lender.

While online marketplace lending is still a very small component of the small business and consumer lending market, it is a rapidly developing and fast-growing sector that is changing the credit marketplace. In less than a decade, online marketplace lending has grown to an estimated $12 billion in new loan originations in 2014, the majority of which is consumer lending.[8] Through this RFI, Treasury is seeking to study the potential for online marketplace lending to expand access to credit and how the financial regulatory framework should evolve to support the safe growth of this industry.

III. Background

Online marketplace lending broadly refers to the segment of the financial services industry that uses investment capital and data-driven online platforms to lend either directly or indirectly to small businesses and consumers. This segment initially emerged with companies giving investors the ability to provide financing that would be used to fund individual borrowers through what became known as a ''peer-to-peer'' model. However, it has since evolved to include a diverse set of individual and institutional credit investors who seek to provide financing that ultimately is used to fund small business and consumer loans of various types to gain access to additional credit channels and favorable rates of return.

Companies operating in this industry tend to fall into three general categories: (1) Balance sheet lenders that retain credit risk in their own portfolios and are typically funded by venture capital, hedge fund, or family office investments; (2) online platforms (formerly known as ''peer-to-peer'') that, through the sale of securities such as member-dependent notes, obtain the financing to enable third parties to fund borrowers and, due to the contingent nature of the payment obligation on such securities, do not retain credit risk that the borrowers will not pay; and (3) bank-affiliated online lenders that are funded by a commercial bank, often a regional or community bank, originate loans and directly assume the credit risk.

Additionally, some of these companies have adopted a business model in which they partner and have agreements with banks. In these arrangements, the bank acts as the lender to borrowers that apply on the platform. The loans are then purchased by a second party — either by an investor, in which the transaction is facilitated by the marketplace lender, or by the marketplace lender itself, which funds the loan purchase by note sales. While the loans are not pooled, small investors can obtain a return by making small investments in a number of notes offered by a marketplace lender through its platforms.

Online marketplace lenders share key similarities. They provide funding through convenient online loan applications and most have no retail branches. They use electronic data sources and technology-enabled underwriting models to automate processes such as determining a borrower's identity and credit risk. These data sources might include traditional underwriting statistics (*e.g.,* income and debt obligations), but also often include other forms of information, including novel data points or combinations. Online marketplace lenders typically provide borrowers with faster access to credit than the traditional face-to-face credit application process. Small business online market place lenders, provide small businesses with lower value (less than $100,000) and shorter terms.

Key Questions

1. There are many different models for online marketplace lending including platform lenders (also referred to as ''peer-to-peer''), balance sheet lenders, and bank-affiliated lenders. In what ways should policymakers be thinking about market segmentation; and in what ways do different models raise different policy or regulatory concerns?

2. According to a survey by the National Small Business Association, 85

[3] As noted elsewhere, the CFPB is contemplating issuing a rule that would regulate ''payday'' and related loans, including loans with terms greater than 45 days and an APR greater than 36%, if the loan also provides for repayment directly from a consumer's account or paycheck or includes a non-purchase money security interest in a vehicle. Such consumer loans are outside the scope of this RFI.

[4] ''2011 Economic Report of the President,'' Council of Economic Advisors. The White House.

[5] ''The Future of Finance,'' Goldman Sachs Equity Research, March 3, 2015.

[6] ''The Joint Small Business Credit Survey, 2014,'' a collaboration among the Federal Reserve Banks of New York, Atlanta, Cleveland and Philadelphia. Released February 2015.

[7] Ibid.

[8] ''Global Marketplace Lending: Disruptive Innovation in Financials,'' Morgan Stanley Research, May 2015.

percent of small businesses purchase supplies online, 83 percent manage bank accounts online, 82 percent maintain their own Web site, 72 percent pay bills online, and 41 percent use tablets for their businesses.[9] Small businesses are also increasingly using online bookkeeping and operations management tools. As such, there is now an unprecedented amount of online data available on the activities of these small businesses. What role are electronic data sources playing in enabling marketplace lending? For instance, how do they affect traditionally manual processes or evaluation of identity, fraud, and credit risk for lenders? Are there new opportunities or risks arising from these data-based processes relative to those used in traditional lending?

3. How are online marketplace lenders designing their business models and products for different borrower segments, such as:

- Small business and consumer borrowers;
- Subprime borrowers;
- Borrowers who are ''unscoreable'' or have no or thin files;

Depending on borrower needs (*e.g.,* new small businesses, mature small businesses, consumers seeking to consolidate existing debt, consumers seeking to take out new credit) and other segmentations?

4. Is marketplace lending expanding access to credit to historically underserved market segments?

5. Describe the customer acquisition process for online marketplace lenders. What kinds of marketing channels are used to reach new customers? What kinds of partnerships do online marketplace lenders have with traditional financial institutions, community development financial institutions (CDFIs), or other types of businesses to reach new customers?

6. How are borrowers assessed for their creditworthiness and repayment ability? How accurate are these models in predicting credit risk? How does the assessment of small business borrowers differ from consumer borrowers? Does the borrower's stated use of proceeds affect underwriting for the loan?

7. Describe whether and how marketplace lending relies on services or relationships provided by traditional lending institutions or insured depository institutions. What steps have been taken toward regulatory compliance with the new lending model by the various industry participants throughout the lending process? What issues are raised with online marketplace lending across state lines?

8. Describe how marketplace lenders manage operational practices such as loan servicing, fraud detection, credit reporting, and collections. How are these practices handled differently than by traditional lending institutions? What, if anything, do marketplace lenders outsource to third party service providers? Are there provisions for back-up services?

9. What roles, if any, can the federal government play to facilitate positive innovation in lending, such as making it easier for borrowers to share their own government-held data with lenders? What are the competitive advantages and, if any, disadvantages for non-banks and banks to participate in and grow in this market segment? How can policymakers address any disadvantages for each? How might changes in the credit environment affect online marketplace lenders?

10. Under the different models of marketplace lending, to what extent, if any, should platform or ''peer-to-peer'' lenders be required to have ''skin in the game'' for the loans they originate or underwrite in order to align interests with investors who have acquired debt of the marketplace lenders through the platforms? Under the different models, is there pooling of loans that raise issues of alignment with investors in the lenders' debt obligations? How would the concept of risk retention apply in a non-securitization context for the different entities in the distribution chain, including those in which there is no pooling of loans? Should this concept of ''risk retention'' be the same for other types of syndicated or participated loans?

11. Marketplace lending potentially offers significant benefits and value to borrowers, but what harms might online marketplace lending also present to consumers and small businesses? What privacy considerations, cybersecurity threats, consumer protection concerns, and other related risks might arise out of online marketplace lending? Do existing statutory and regulatory regimes adequately address these issues in the context of online marketplace lending?

12. What factors do investors consider when: (i) Investing in notes funding loans being made through online marketplace lenders, (ii) doing business with particular entities, or (iii) determining the characteristics of the notes investors are willing to purchase? What are the operational arrangements? What are the various methods through which investors may finance online platform assets, including purchase of securities, and what are the advantages and disadvantages of using them? Who are the end investors? How prevalent is the use of financial leverage for investors? How is leverage typically obtained and deployed?

13. What is the current availability of secondary liquidity for loan assets originated in this manner? What are the advantages and disadvantages of an active secondary market? Describe the efforts to develop such a market, including any hurdles (regulatory or otherwise). Is this market likely to grow and what advantages and disadvantages might a larger securitization market, including derivatives and benchmarks, present?

14. What are other key trends and issues that policymakers should be monitoring as this market continues to develop?

Guidance for Submitting Documents: We ask that each respondent include the name and address of his or her institution or affiliation, and the name, title, mailing and email addresses, and telephone number of a contact person for his or her institution or affiliation, if any.

Dated: July, 13, 2015.

David G. Clunie,

Executive Secretary,

[FR Doc. 2015–17644 Filed 7–17–15; 8:45 am]

BILLING CODE 4810–25–P

[9] ''2013 Small Business Technology Survey,'' National Small Business Association.

APPENDIX C
List of Comments in Response to RFI

ReedSmith

	Company Name	Page Count
1	Accion U.S. Network	12
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3	Alliance Partners	22
4	Amalgamated Bank	3
5	Americans for Financial Reform	3
6	Association for Enterprise Opportunity	5
7	Avant, Inc.	4
8	Banking Up	2
9	Blue Elephant Capital Management	12
10	Bond Street	11
11	Broadmoor Consulting LLC	4
12	BuckleySandler	13
13	CAN Capital, Inc.	10
14	Center for Capital Markets Competitiveness	7
15	Center for Financial Services Innovation	6
16	Center for Responsible Lending	7
17	CommonBond, Inc.	11
18	Community Reinvestment Fund, Inc	15
19	Conference of State Bank Supervisors	9
20	Connect Lending	4
21	Cross River Bank	11
22	Crowdnetic	9
23	CUNA	3
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28	Edward C. Yale CFA	2
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33	Funding Circle	44
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	Company Name	Page Count
35	GLI Finance	7
36	Godolphin Capital Management, LLC	24
37	Habematolel Pomo of Upper Lake	11
38	Income & Technologies, Inc.	10
39	Independent Community Bankers of America	4
40	INSIKT	11
41	Kabbage, Inc.	10
42	Kiva Microfunds	12
43	KPMG LLP	12
44	Lend Academy	31
45	Lending Club	51
46	LendingTree	5
47	Lendio	10
48	LiftFroward	4
49	Manatt, Phelps & Phillips, LLP	5
50	Milken Institute Center for Financial Markets	13
51	Missouri Credit Union Association	2
52	Missouri Credit Union Association	2
53	MonJa	8
54	Mountain BizWorks	6
55	NAFCU	3
56	NASAA	3
57	National Association of Industrial Bankers	10
58	National Association of REALTORS	4
59	National Consumer Law Center	8
60	National Pawnbrokers Association	6
61	Native American Financial Services Association	9
62	Nelson Mullins	4
63	Office of the Mayor Chicago	1
64	OnDeck	22
65	Online Lenders Alliance	77
66	Oportun, Inc	19
67	Opportunity Finance Network	6
68	Opportunity Fund	7

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	Company Name	Page Count
69	Orchard Platform	16
70	Otoe-Missouria	10
71	PayNet	9
72	PayPal Inc.	5
73	PeerIQ	22
74	Peer-to-Peer Finance Association	19
75	Pepper Hamilton	11
76	PIRG and Center for Digital Democracy	15
77	Prosper Marketplace	15
78	QTX Systems	21
79	RapidAdvance	15
80	RevenueTrades	15
81	Rosette, LLP	4
82	SIFMA	11
83	Small Business Majority	3
84	SoFi	7
85	Structured Finance Industry Group	15
86	The American Bankers Association and The Consumer Bankers Association	10
87	The Heritage Foundation	4
88	The Support Center	3
89	U.C. Berkeley Law School	11
90	University of Colorado Boulder	2
91	Upstart	4
92	WebBank	4
93	Woodstock Institute	8
94	ZestFinance	3

APPENDIX D
Madden v. Midland

14-2131-cv
Madden v. Midland Funding, LLC

1 In the
2 United States Court of Appeals
3 For the Second Circuit

4
5 August Term, 2014
6 No. 14-2131-cv

7 SALIHA MADDEN,
8 on behalf of herself and all others similarly situated,
9 *Plaintiff-Appellant*,

10 *v.*

11 MIDLAND FUNDING, LLC, MIDLAND CREDIT MANAGEMENT, INC.,
12 *Defendants-Appellees*.
13

14 Appeal from the United States District Court
15 for the Southern District of New York.
16 No. 7:11-cv-08149 — Cathy Seibel, *Judge*.
17

18
19 ARGUED: MARCH 19, 2015
20 DECIDED: MAY 22, 2015
21

22
23 Before: LEVAL, STRAUB and DRONEY, *Circuit Judges*.
24

1 Appeal from an order of the United States District Court for
2 the Southern District of New York (Cathy Seibel, *Judge*), holding that
3 the plaintiff's claims are preempted by the National Bank Act,
4 denying class certification, and granting judgment in favor of the
5 defendants. We hold that non-national bank entities are not entitled
6 to protection under the National Bank Act from state-law usury
7 claims merely because they are assignees of a national bank.
8 Accordingly, we **REVERSE** the District Court's holding as to
9 National Bank Act preemption, **VACATE** the District Court's
10 judgment and denial of class certification, and **REMAND** for further
11 proceedings consistent with this opinion.
12
13
14 DANIEL ADAM SCHLANGER, Schlanger &
15 Schlanger LLP, Pleasantville, NY (Peter Thomas
16 Lane, Schlanger & Schlanger LLP, Pleasantville,
17 NY; Owen Randolph Bragg, Horwitz, Horwitz &
18 Associates, Chicago, IL, *on the brief*), *for Saliha*
19 *Madden*.

20 THOMAS ARTHUR LEGHORN (Joseph L. Francoeur,
21 *on the brief*), Wilson Elser Moskowitz Edelman &
22 Dicker LLP, New York, NY, *for Midland Funding,*
23 *LLC and Midland Credit Management, Inc.*
24

25 STRAUB, *Circuit Judge*:

26 This putative class action alleges violations of the Fair Debt
27 Collection Practices Act ("FDCPA") and New York's usury law. The
28 proposed class representative, Saliha Madden, alleges that the

1 defendants violated the FDCPA by charging and attempting to
2 collect interest at a rate higher than that permitted under the law of
3 her home state, which is New York. The defendants contend that
4 Madden's claims fail as a matter of law for two reasons: (1) state-
5 law usury claims and FDCPA claims predicated on state-law
6 violations against a national bank's assignees, such as the
7 defendants here, are preempted by the National Bank Act ("NBA"),
8 and (2) the agreement governing Madden's debt requires the
9 application of Delaware law, under which the interest charged is
10 permissible.

11 The District Court entered judgment for the defendants.
12 Because neither defendant is a national bank nor a subsidiary or
13 agent of a national bank, or is otherwise acting on behalf of a
14 national bank, and because application of the state law on which
15 Madden's claim relies would not significantly interfere with any
16 national bank's ability to exercise its powers under the NBA, we

1 reverse the District Court's holding that the NBA preempts
2 Madden's claims and accordingly vacate the judgment of the District
3 Court. We leave to the District Court to address in the first instance
4 whether the Delaware choice-of-law clause precludes Madden's
5 claims.

6 The District Court also denied Madden's motion for class
7 certification, holding that potential NBA preemption required
8 individualized factual inquires incompatible with proceeding as a
9 class. Because this conclusion rested upon the same erroneous
10 preemption analysis, we also vacate the District Court's denial of
11 class certification.

12 **BACKGROUND**

13 **A. Madden's Credit Card Debt, the Sale of Her Account, and**
14 **the Defendants' Collection Efforts**
15
16 In 2005, Saliha Madden, a resident of New York, opened a
17 Bank of America ("BoA") credit card account. BoA is a national

1 bank.[1] The account was governed by a document she received from
2 BoA titled "Cardholder Agreement." The following year, BoA's
3 credit card program was consolidated into another national bank,
4 FIA Card Services, N.A. ("FIA"). Contemporaneously with the
5 transfer to FIA, the account's terms and conditions were amended
6 upon receipt by Madden of a document titled "Change In Terms,"
7 which contained a Delaware choice-of-law clause.

8 Madden owed approximately $5,000 on her credit card
9 account and in 2008, FIA "charged-off" her account (i.e., wrote off
10 her debt as uncollectable). FIA then sold Madden's debt to
11 Defendant-Appellee Midland Funding, LLC ("Midland Funding"), a
12 debt purchaser. Midland Credit Management, Inc. ("Midland
13 Credit"), the other defendant in this case, is an affiliate of Midland
14 Funding that services Midland Funding's consumer debt accounts.

---

[1] National banks are "corporate entities chartered not by any State, but by the Comptroller of the Currency of the U.S. Treasury." *Wachovia Bank v. Schmidt*, 546 U.S. 303, 306 (2006).

1 Neither defendant is a national bank. Upon Midland Funding's
2 acquisition of Madden's debt, neither FIA nor BoA possessed any
3 further interest in the account.

4 In November 2010, Midland Credit sent Madden a letter
5 seeking to collect payment on her debt and stating that an interest
6 rate of 27% per year applied.

7 **B. Procedural History**

8 A year later, Madden filed suit against the defendants—on
9 behalf of herself and a putative class—alleging that they had
10 engaged in abusive and unfair debt collection practices in violation
11 of the FDCPA, 15 U.S.C. §§ 1692e, 1692f, and had charged a usurious
12 rate of interest in violation of New York law, N.Y. Gen. Bus. Law
13 § 349; N.Y. Gen. Oblig. Law § 5-501; N.Y. Penal Law § 190.40
14 (proscribing interest from being charged at a rate exceeding 25% per
15 year).

1 On September 30, 2013, the District Court denied the
2 defendants' motion for summary judgment and Madden's motion
3 for class certification. In ruling on the motion for summary
4 judgment, the District Court concluded that genuine issues of
5 material fact remained as to whether Madden had received the
6 Cardholder Agreement and Change In Terms, and as to whether
7 FIA had actually assigned her debt to Midland Funding. However,
8 the court stated that if, at trial, the defendants were able to prove
9 that Madden had received the Cardholder Agreement and Change
10 In Terms, and that FIA had assigned her debt to Midland Funding,
11 her claims would fail as a matter of law because the NBA would
12 preempt any state-law usury claim against the defendants. The
13 District Court also found that if the Cardholder Agreement and
14 Change In Terms were binding upon Madden, any FDCPA claim of
15 false representation or unfair practice would be defeated because the
16 agreement permitted the interest rate applied by the defendants.

1 In ruling on Madden's motion for class certification, the
2 District Court held that because "assignees are entitled to the
3 protection of the NBA if the originating bank was entitled to the
4 protection of the NBA . . . the class action device in my view is not
5 appropriate here." App'x at 120. The District Court concluded that
6 the proposed class failed to satisfy Rule 23(a)'s commonality and
7 typicality requirements because "[t]he claims of each member of the
8 class will turn on whether the class member agreed to Delaware
9 interest rates" and "whether the class member's debt was validly
10 assigned to the Defendants," *id*. at 127-28, both of which were
11 disputed with respect to Madden. Similarly, the court held that the
12 requirements of Rule 23(b)(2) (relief sought appropriate to class as a
13 whole) and (b)(3) (common questions of law or fact predominate)
14 were not satisfied "because there is no showing that the
15 circumstances of each proposed class member are like those of
16 Plaintiff, and because the resolution will turn on individual

1 determinations as to cardholder agreements and assignments of
2 debt." *Id*. at 128.
3 On May 30, 2014, the parties entered into a "Stipulation for
4 Entry of Judgment for Defendants for Purpose of Appeal." *Id*.
5 at 135. The parties stipulated that FIA had assigned Madden's
6 account to the defendants and that Madden had received the
7 Cardholder Agreement and Change In Terms. This stipulation
8 disposed of the two genuine disputes of material fact identified by
9 the District Court, and provided that "a final, appealable judgment
10 in favor of Defendants is appropriate." *Id*. at 138. The District Court
11 "so ordered" the Stipulation for Entry of Judgment.
12 This timely appeal followed.

13 **DISCUSSION**

14 Madden argues on appeal that the District Court erred in
15 holding that NBA preemption bars her state-law usury claims. We
16 agree. Because neither defendant is a national bank nor a subsidiary
17 or agent of a national bank, or is otherwise acting on behalf of a

1 national bank, and because application of the state law on which
2 Madden's claim relies would not significantly interfere with any
3 national bank's ability to exercise its powers under the NBA, we
4 reverse the District Court's holding that the NBA preempts
5 Madden's claims and accordingly vacate the judgment of the District
6 Court. We also vacate the District Court's judgment as to Madden's
7 FDCPA claim and the denial of class certification because those
8 rulings were predicated on the same flawed preemption analysis.
9 The defendants contend that even if we find that Madden's
10 claims are not preempted by the NBA, we must affirm because
11 Delaware law—rather than New York law—applies and the interest
12 charged by the defendants is permissible under Delaware law.
13 Because the District Court did not reach this issue, we leave it to the
14 District Court to address in the first instance on remand.

1 **I. National Bank Act Preemption**

2 The federal preemption doctrine derives from the Supremacy
3 Clause of the United States Constitution, which provides that "the
4 Laws of the United States which shall be made in Pursuance" of the
5 Constitution "shall be the supreme Law of the Land." U.S. Const.
6 art. VI, cl. 2. According to the Supreme Court, "[t]he phrase 'Laws
7 of the United States' encompasses both federal statutes themselves
8 and federal regulations that are properly adopted in accordance
9 with statutory authorization." *City of New York v. FCC*, 486 U.S. 57,
10 63 (1988).

11 "Preemption can generally occur in three ways: where
12 Congress has expressly preempted state law, where Congress has
13 legislated so comprehensively that federal law occupies an entire
14 field of regulation and leaves no room for state law, or where federal
15 law conflicts with state law." *Wachovia Bank, N.A. v. Burke*, 414 F.3d
16 305, 313 (2d Cir. 2005), *cert. denied*, 550 U.S. 913 (2007). The

1 defendants appear to suggest that this case involves "conflict
2 preemption," which "occurs when compliance with both state and
3 federal law is impossible, or when the state law stands as an obstacle
4 to the accomplishment and execution of the full purposes and
5 objective of Congress." *United States v. Locke*, 529 U.S. 89, 109 (2000)
6 (internal quotation marks omitted).

7 The National Bank Act expressly permits national banks to
8 "charge on any loan . . . interest at the rate allowed by the laws of
9 the State, Territory, or District where the bank is located." 12 U.S.C.
10 § 85. It also "provide[s] the exclusive cause of action" for usury
11 claims against national banks, *Beneficial Nat'l Bank v. Anderson*, 539
12 U.S. 1, 11 (2003), and "therefore completely preempt[s] analogous
13 state-law usury claims," *Sullivan v. Am. Airlines, Inc.*, 424 F.3d 267,
14 275 (2d Cir. 2005). Thus, there is "no such thing as a state-law claim
15 of usury against a national bank." *Beneficial Nat'l Bank*, 539 U.S.
16 at 11; *see also Pac. Capital Bank, N.A. v. Connecticut*, 542 F.3d 341, 352

1 (2d Cir. 2008) ("[A] state in which a national bank makes a loan may
2 not permissibly require the bank to charge an interest rate lower
3 than that allowed by its home state."). Accordingly, because FIA is
4 incorporated in Delaware, which permits banks to charge interest
5 rates that would be usurious under New York law, FIA's collection
6 at those rates in New York does not violate the NBA and is not
7 subject to New York's stricter usury laws, which the NBA preempts.

8 The defendants argue that, as assignees of a national bank,
9 they too are allowed under the NBA to charge interest at the rate
10 permitted by the state where the assignor national bank is located—
11 here, Delaware. We disagree. In certain circumstances, NBA
12 preemption can be extended to non-national bank entities. To apply
13 NBA preemption to an action taken by a non-national bank entity,
14 application of state law to that action must significantly interfere
15 with a national bank's ability to exercise its power under the NBA.

1 *See Barnett Bank of Marion Cnty., N.A. v. Nelson*, 517 U.S. 25, 33 (1996);
2 *Pac. Capital Bank*, 542 F.3d at 353.

3 The Supreme Court has suggested that that NBA preemption
4 may extend to entities beyond a national bank itself, such as non-
5 national banks acting as the "equivalent to national banks with
6 respect to powers exercised under federal law." *Watters v. Wachovia*
7 *Bank, N.A.*, 550 U.S. 1, 18 (2007). For example, the Supreme Court
8 has held that operating subsidiaries of national banks may benefit
9 from NBA preemption. *Id.*; *see also Burke*, 414 F.3d at 309 (deferring
10 to reasonable regulation that operating subsidiaries of national
11 banks receive the same preemptive benefit as the parent bank). This
12 Court has also held that agents of national banks can benefit from
13 NBA preemption. *Pac. Capital Bank*, 542 F.3d at 353-54 (holding that
14 a third-party tax preparer who facilitated the processing of refund
15 anticipation loans for a national bank was not subject to Connecticut
16 law regulating such loans); *see also SPGGC, LLC v. Ayotte*, 488 F.3d

1 525, 532 (1st Cir. 2007) ("The National Bank Act explicitly states that
2 a national bank may use 'duly authorized officers or agents' to
3 exercise its incidental powers." (internal citation omitted)), *cert.*
4 *denied*, 552 U.S. 1185 (2008).

5 The Office of the Comptroller of the Currency ("OCC"), "a
6 federal agency that charters, regulates, and supervises all national
7 banks," *Town of Babylon v. Fed. Hous. Fin. Agency*, 699 F.3d 221, 224
8 n.2 (2d Cir. 2012), has made clear that third-party debt buyers are
9 distinct from agents or subsidiaries of a national bank, *see* OCC
10 Bulletin 2014-37, Risk Management Guidance (Aug. 4, 2014),
11 *available at* http://www.occ.gov/news-
12 issuances/bulletins/2014/bulletin-2014-37.html ("Banks may pursue
13 collection of delinquent accounts by (1) handling the collections
14 internally, (2) using third parties as agents in collecting the debt, or
15 (3) selling the debt to debt buyers for a fee."). In fact, it is precisely
16 because national banks do not exercise control over third-party debt

1 buyers that the OCC issued guidance regarding how national banks
2 should manage the risk associated with selling consumer debt to
3 third parties. *See id.*

4 In most cases in which NBA preemption has been applied to a
5 non-national bank entity, the entity has exercised the powers of a
6 national bank—i.e., has acted on behalf of a national bank in
7 carrying out the national bank's business. This is not the case here.
8 The defendants did not act on behalf of BoA or FIA in attempting to
9 collect on Madden's debt. The defendants acted solely on their own
10 behalves, as the owners of the debt.

11 No other mechanism appears on these facts by which
12 applying state usury laws to the third-party debt buyers would
13 significantly interfere with either national bank's ability to exercise
14 its powers under the NBA. *See Barnett Bank*, 517 U.S. at 33. Rather,
15 such application would "limit[] only activities of the third party
16 which are otherwise subject to state control," *SPGGC, LLC v.*

1 *Blumenthal*, 505 F.3d 183, 191 (2d Cir. 2007), and which are not
2 protected by federal banking law or subject to OCC oversight.
3 We reached a similar conclusion in *Blumenthal*. There, a
4 shopping mall operator, SPGGC, sold prepaid gift cards at its malls,
5 including its malls in Connecticut. *Id.* at 186. Bank of America
6 issued the cards, which looked like credit or debit cards and
7 operated on the Visa debit card system. *Id.* at 186-87. The gift cards
8 included a monthly service fee and carried a one-year expiration
9 date. *Id.* at 187. The Connecticut Attorney General sued SPGGC
10 alleging violations of Connecticut's gift card law, which prohibits
11 the sale of gift cards subject to inactivity or dormancy fees or
12 expiration dates. *Id.* at 187-88. SPGGC argued that NBA
13 preemption precluded suit. *Id.* at 189.
14 We held that SPGGC failed to state a valid claim for
15 preemption of Connecticut law insofar as the law prohibited SPGGC
16 from imposing inactivity fees on consumers of its gift cards. *Id.*

1 at 191. We reasoned that enforcement of the state law "does not
2 interfere with BoA's ability to exercise its powers under the NBA
3 and OCC regulations." *Id.* "Rather, it affects only the conduct of
4 SPGGC, which is neither protected under federal law nor subject to
5 the OCC's exclusive oversight." *Id.*

6 We did find, in *Blumenthal*, that Connecticut's prohibition on
7 expiration dates could interfere with national bank powers because
8 Visa requires such cards to have expiration dates and "an outright
9 prohibition on expiration dates could have prevented a Visa
10 member bank (such as BoA) from acting as the issuer of the Simon
11 Giftcard." *Id.* at 191. We remanded for further consideration of the
12 issue. Here, however, state usury laws would not prevent consumer
13 debt sales by national banks to third parties. Although it is possible
14 that usury laws might decrease the amount a national bank could
15 charge for its consumer debt in certain states (i.e., those with firm

1 usury limits, like New York), such an effect would not "significantly
2 interfere" with the exercise of a national bank power.

3 Furthermore, extension of NBA preemption to third-party
4 debt collectors such as the defendants would be an overly broad
5 application of the NBA. Although national banks' agents and
6 subsidiaries exercise national banks' powers and receive protection
7 under the NBA when doing so, extending those protections to third
8 parties would create an end-run around usury laws for non-national
9 bank entities that are not acting on behalf of a national bank.

10 The defendants and the District Court rely principally on two
11 Eighth Circuit cases in which the court held that NBA preemption
12 precluded state-law usury claims against non-national bank entities.
13 In *Krispin v. May Department Stores*, 218 F.3d 919 (8th Cir. 2000), May
14 Department Stores Company ("May Stores"), a non-national bank
15 entity, issued credit cards to the plaintiffs. *Id*. at 921. By agreement,
16 those credit card accounts were governed by Missouri law, which

1 limits delinquency fees to $10. *Id*. Subsequently, May Stores
2 notified the plaintiffs that the accounts had been assigned and
3 transferred to May National Bank of Arizona ("May Bank"), a
4 national bank and wholly-owned subsidiary of May Stores, and that
5 May Bank would charge delinquency fees of up to "$15, or as
6 allowed by law." *Id*. Although May Stores had transferred all
7 authority over the terms and operations of the accounts to May
8 Bank, it subsequently purchased May Bank's receivables and
9 maintained a role in account collection. *Id*. at 923.

10 The plaintiffs brought suit under Missouri law against May
11 Stores after being charged $15 delinquency fees. *Id*. at 922. May
12 Stores argued that the plaintiffs' state-law claims were preempted by
13 the NBA because the assignment and transfer of the accounts to May
14 Bank "was fully effective to cause the bank, and not the store, to be
15 the originator of [the plaintiffs'] accounts subsequent to that time."
16 *Id*. at 923. The court agreed:

1 [T]he store's purchase of the bank's receivables does not
2 diminish the fact that it is now the bank, and not the
3 store, that issues credit, processes and services customer
4 accounts, and sets such terms as interest and late fees.
5 Thus, although we recognize that the NBA governs only
6 national banks, in these circumstances we agree with
7 the district court that it makes sense to look to the
8 originating entity (the bank), and not the ongoing
9 assignee (the store), in determining whether the NBA
10 applies.
11
12 *Id*. at 924 (internal citation omitted).[2]

[2] We believe the District Court gave unwarranted significance to *Krispin*'s reference to the "originating entity" in the passage quoted above. The District Court read the sentence to suggest that, once a national bank has originated a credit, the NBA and the associated rule of conflict preemption continue to apply to the credit, even if the bank has sold the credit and retains no further interest in it. The point of the *Krispin* holding was, however, that notwithstanding the bank's sale of its receivables to May Stores, it retained substantial interests in the credit card accounts so that application of state law to those accounts would have conflicted with the bank's powers authorized by the NBA. The crucial words of the sentence were "in these circumstances," which referred to the fact stated in the previous sentence of the bank's retention of substantial interests in the credit card accounts. As we understand the *Krispin* opinion, the fact that the bank was described as the "originating entity" had no significance for the court's decision, which would have come out the opposite way if the bank, notwithstanding that it originated the credits in question, had sold them outright to a new, unrelated owner, divesting itself completely of any continuing interest in them, so that its operations would no longer be affected by the application of state law to the new owner's further administration of the credits.

1 *Krispin* does not support finding preemption here. In *Krispin*,
2 when the national bank's receivables were purchased by May Stores,
3 the national bank retained ownership of the accounts, leading the
4 court to conclude that "the real party in interest is the bank." 218
5 F.3d at 924. Unlike *Krispin*, neither BoA nor FIA has retained an
6 interest in Madden's account, which further supports the conclusion
7 that subjecting the defendants to state regulations does not prevent
8 or significantly interfere with the exercise of BoA's or FIA's powers.
9 The defendants and the District Court also rely upon *Phipps v.*
10 *FDIC*, 417 F.3d 1006 (8th Cir. 2005). In that case, the plaintiffs
11 brought an action under Missouri law to recover allegedly unlawful
12 fees charged by a national bank on mortgage loans. The plaintiffs
13 alleged that after charging these fees, which included a purported
14 "finder's fee" to third-party Equity Guaranty LLC (a non-bank
15 entity), the bank sold the loans to other defendants. The court held
16 that the fees at issue were properly considered "interest" under the

1 NBA and concluded that, under those circumstances, it "must look
2 at 'the originating entity (the bank), and not the ongoing assignee . . .
3 in determining whether the NBA applies.'" *Id.* at 1013 (quoting
4 *Krispin*, 218 F.3d at 924 (alteration in original)).

5 *Phipps* is distinguishable from this case. There, the national
6 bank was the entity that charged the interest to which the plaintiffs
7 objected. Here, on the other hand, Madden objects only to the
8 interest charged after her account was sold by FIA to the defendants.
9 Furthermore, if Equity Guaranty was paid a "finder's fee," it would
10 benefit from NBA preemption as an agent of the national bank.
11 Indeed, *Phipps* recognized that "'[a] national bank may use the
12 services of, and compensate persons not employed by, the bank for
13 originating loans.'" *Id*. (quoting 12 C.F.R. § 7.1004(a)). Here, the

1 defendants do not suggest that they have such a relationship with

2 BoA or FIA.[3]

3 **II. Choice of Law: Delaware vs. New York**

4 The defendants contend that the Delaware choice-of-law

5 provision contained in the Change In Terms precludes Madden's

6 New York usury claims.[4] Although raised below, the District Court

7 did not reach this issue in ruling on the defendants' motion for

8 summary judgment.[5] Subsequently, in the Stipulation for Entry of

---

[3] We are not persuaded by *Munoz v. Pipestone Financial, LLC*, 513 F. Supp. 2d 1076 (D. Minn. 2007), upon which the defendants and the District Court also rely. Although the court found preemption applicable to an assignee of a national bank in a case analogous to Madden's suit, it misapplied Eighth Circuit precedent by applying unwarranted significance to *Krispin*'s use of the word "originating entity" and straying from the essential inquiry—whether applying state law would "significantly interfere with the national bank's exercise of its powers," *Barnett Bank*, 517 U.S. at 33, because of a subsidiary or agency relationship or for other reasons.

[4] The Change In Terms, which amended the original Cardholder Agreement, includes the following provision: "This Agreement is governed by the laws of the State of Delaware (without regard to its conflict of laws principles) and by any applicable federal laws." App'x at 58, 91.

[5] We reject Madden's contention that this argument was waived. First, although the defendants' motion for summary judgment urged the District Court to rule on other grounds, it did raise the Delaware choice-of-law clause. Defs.' Summ. J. Mem. 4 & n.3, No. 7:11-cv-08149 (S.D.N.Y. Jan. 25, 2013), ECF No. 32. Second,

1 Judgment, the parties resolved in the defendants' favor the dispute
2 as to whether Madden was bound by the Change In Terms. The
3 parties appear to agree that if Delaware law applies, the rate the
4 defendants charged Madden was permissible.[6]

5 We do not decide the choice-of-law issue here, but instead
6 leave it for the District Court to address in the first instance.[7]

7 **III. Madden's Fair Debt Collection Practices Act Claim**

8 Madden also contends that by attempting to collect interest at
9 a rate higher than allowed by New York law, the defendants falsely

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this argument was not viable prior to the Stipulation for Entry of Judgment due to unresolved factual issues—principally, whether Madden had received the Change In Terms.

[6] We express no opinion as to whether Delaware law, which permits a "bank" to charge any interest rate allowable by contract, *see* Del. Code Ann. tit. 5, § 943, would apply to the defendants, both of which are non-bank entities.

[7] Because it may assist the District Court, we note that there appears to be a split in the case law. *Compare Am. Equities Grp., Inc. v. Ahava Dairy Prods. Corp.*, No. 01 Civ. 5207(RWS), 2004 WL 870260, at *7-9 (S.D.N.Y. Apr. 23, 2004) (applying New York's usury law despite out-of-state choice-of-law clause); *Am. Express Travel Related Servs. Co. v. Assih*, 26 Misc. 3d 1016, 1026 (N.Y. Civ. Ct. 2009) (same); *N. Am. Bank, Ltd. v. Schulman*, 123 Misc. 2d 516, 520-21 (N.Y. Cnty. Ct. 1984) (same) *with RMP Capital Corp. v. Bam Brokerage, Inc.*, 21 F. Supp. 3d 173, 186 (E.D.N.Y. 2014) (finding out-of-state choice-of-law clause to preclude application of New York's usury law).

1 represented the amount to which they were legally entitled in
2 violation of the FDCPA, 15 U.S.C. §§ 1692e(2)(A), (5), (10), 1692f(1).
3 The District Court denied the defendants' motion for summary
4 judgment on this claim for two reasons. First, it held that there was
5 a genuine dispute of material fact as to whether the defendants are
6 assignees of FIA; if they are, it reasoned, Madden's FDCPA claim
7 would fail because state usury laws—the alleged violation of which
8 provide the basis for Madden's FDCPA claim—do not apply to
9 assignees of a national bank. The parties subsequently stipulated
10 "that FIA assigned Defendants Ms. Madden's account," App'x
11 at 138, and the District Court, in accord with its prior ruling, entered
12 judgment for the defendants. Because this analysis was predicated
13 on the District Court's erroneous holding that the defendants receive
14 the same protections under the NBA as do national banks, we find
15 that it is equally flawed.

1 Second, the District Court held that if Madden received the
2 Cardholder Agreement and Change In Terms, a fact to which the
3 parties later stipulated, any FDCPA claim of false representation or
4 unfair practice would fail because the agreement allowed for the
5 interest rate applied by the defendants. This conclusion is premised
6 on an assumption that Delaware law, rather than New York law,
7 applies, an issue the District Court did not reach. If New York's
8 usury law applies notwithstanding the Delaware choice-of-law
9 clause, the defendants may have made a false representation or
10 engaged in an unfair practice insofar as their collection letter to
11 Madden stated that they were legally entitled to charge interest in
12 excess of that permitted by New York law. Thus, the District Court
13 may need to revisit this conclusion after deciding whether Delaware
14 or New York law applies.

15 Because the District Court's analysis of the FDCPA claim was
16 based on an erroneous NBA preemption finding and a premature

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1 assumption that Delaware law applies, we vacate the District
2 Court's judgment as to this claim.

3 **IV. Class Certification**

4 Madden asserts her claims on behalf of herself and a class
5 consisting of "all persons residing in New York [] who were sent a
6 letter by Defendants attempting to collect interest in excess of 25%
7 per annum [] regarding debts incurred for personal, family, or
8 household purposes." Pl.'s Class Certification Mem. 1, No. 7:11-cv-
9 08149 (S.D.N.Y. Jan. 18, 2013), ECF No. 29. The defendants have
10 represented that they sent such letters with respect to 49,780
11 accounts.

12 Madden moved for class certification before the District Court.
13 The District Court denied the motion, holding that because
14 "assignees are entitled to the protection of the NBA if the originating
15 bank was entitled to the protection of the NBA . . . the class action
16 device in my view is not appropriate here." App'x at 120. Because

1 the District Court's denial of class certification was entwined with its
2 erroneous holding that the defendants receive the same protections
3 under the NBA as do national banks, we vacate the denial of class
4 certification.

5 **CONCLUSION**

6 We REVERSE the District Court's holding as to National Bank
7 Act preemption, VACATE the District Court's judgment and denial
8 of class certification, and REMAND for further proceedings
9 consistent with this opinion.