October 18th, 2021

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Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551.
Federal Reserve Docket OP-1752

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Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429.

Chief Counsel's Office
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Office of the Comptroller of the Currency
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Proposed Interagency Guidance on Third-Party Relationships: Risk Management

Thank you for the opportunity to comment on the proposed interagency guidance on the management of third-party relationships.

The National Community Reinvestment Coalition (NCRC) consists of more than 600 community-based organizations, fighting for economic justice for almost 30 years. Our mission is to create opportunities for people and communities to build and maintain wealth. NCRC members include community reinvestment

organizations, community development corporations, local and state government agencies, faith-based institutions, fair housing, and civil rights groups, minority and women-owned business associations, and housing counselors from across the nation. NCRC and its members work to create wealth-building opportunities by eliminating discriminatory lending practices, which have historically contributed to economic inequality.

NCRC urges the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal Reserve (collectively, "the Agencies") to apply a high degree of scrutiny to third-party relationships. In instances where third-party relationships consist of agreements to originate loans at rates greater than rates states permit non-banks to make, the Agencies should automatically deem them as "high-risk." Loans that exceed 36% APR, including fees, should be considered to be especially high-risk.

This letter emphasizes our concerns related to third-party relationships between banks and non-banks in the context of providing deposit services, installment loans, lines of credit, and single-repayment loans.

We agree with the principle stated in the proposed update to the guidance that a banking organization's use of third parties should not diminish its responsibility to operate safely and soundly and in compliance with applicable laws.

Discussion

I. Because third-party relationships naturally create a wall between banks and their customers, they undermine the ability of those banks to understand the needs and conveniences of underserved consumers.

a. Although industry literature speaks with confidence, the claim that fintechs are enhancing financial inclusion is unproven.

The most promising result found that in mortgage credit, non-bank lenders were at best less discriminatory than traditional lenders but still charge borrowers of color more for purchase and refinance loans.[1] In non-mortgage consumer lending, while it is true that the use of algorithms and non-traditional credit may lead to more loan approvals,[2] traditional lenders and fintechs are both capable of using these technologies. Notably, it is essential to differentiate between broad access to credit and safe and affordable credit. Research suggests that online mortgage lenders charge higher rates of interest[3] and are more likely to originate refinances.[4]

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[1] Bartlett, Robert P., Adair Morse, Richard Stanton, and Nancy Wallace. "Consumer Lending Discrimination in the FinTech Era." SSRN Scholarly Paper. Rochester, NY: Social Science Research Network, December 7th, 2017. https://doi.org/10.2139/ssrn.3063448.

[2] Puri, Manju, Tobias Berg, Valentin Burg, and Ana Gombović. "On the Rise of the FinTechs - Credit Scoring Using Digital Footprints." *SSRN Electronic Journal*, 2018. https://doi.org/10.2139/ssrn.3259901.

[3] Buchak, Greg, Gregor Matvos, Tomasz Piskorski, and Amit Seru. "Fintech, Regulatory Arbitrage, and the Rise of Shadow Banks," n.d., 73.

[4] Fuster, Andreas, Matthew Plosser, Philipp Schnabl, and James Vickery. "The Role of Technology in Mortgage Lending." *The Review of Financial Studies* 32, no. 5 (May 1st, 2019): 1854–99. https://doi.org/10.1093/rfs/hhz018.

b. Banks do not assess the needs and conveniences of the customers who use their third-party products.

A significant challenge is that consumers are often not aware that they are using a bank when they receive a loan or make a deposit with a fintech through a third-party relationship. For example, 813 of the 2,183 complaints filed to the CFPB for Enova include a consumer narrative. Not one contains a reference to Republic Bank & Trust, even though Enova has a rent-a-bank scheme with Republic Bank & Trust in about 20 states. The same absence is the case with the 75 complaints about Personify loans issued by First Electronic Bank. [5] In each case, these banks have used their charter to help third parties provide high-cost credit to consumers, but without a corresponding community reinvestment plan.

Similarly, the bank has not taken any role in finding customers and may not oversee marketing to prevent targeting of struggling consumers and communities of color. While agreements stipulate that the banks should review the marketing materials used by the third party to communicate with customers, the banks do not acquire customers directly. Instead, the non-bank third parties create the materials, such as direct mail and online pre-approved offers, and deploy their marketing budgets to pay for the cost of customer acquisition. Ninety-two percent of Elevate Elastic line of credit borrowers responded to one of the company's prescreened credit offers. Elevate purchased those leads from credit bureaus.[6] OppFi[7] and Elevate[8] are examples of online non-bank lenders who use proprietary artificial intelligence to find customers. Third-party lenders are more likely to respond only to motives of profit – they have no obligation to meet community reinvestment needs.

c. Until the Community Reinvestment Act (CRA) is updated to account for the disconnect between the geographic reach of online fintechs and their branch networks, the business activities performed by banks in third-party relationships will not be subject to meaningfully commensurate community reinvestment obligations.

As third-party relationships usually govern activities that occur outside of the assessment area of the bank, they exist outside of the realm of community reinvestment obligations.

A third-party relationship necessarily permits a bank to expand its business activity outside of its assessment – not just outside of its home state – but potentially in all states.

Although an exception may exist, we are not aware of a case of an insured depository with a nationwide branch network that engages in third-party relationships to make loans or take deposits. Almost always, the opposite is true: a depository with an assessment area in one or a handful of MSAs uses a third-party relationship with a program manager to offer bank accounts in many states.

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[5] Consumer Financial Protection Bureau. "Consumer Complaint Database." Consumer Financial Protection Bureau. Accessed September 27th, 2021. https://www.consumerfinance.gov/data-research/consumer-complaints/.

[6] Elevate Credit, Inc. "2020 Annual Report," February 26th, 2021. https://investors.elevate.com/filings-financials/sec-filings/sec-filings-details/default.aspx?FilingId=14750383.

[7] OppFi. "OppFi Inc. IPO Investment Prospectus." S-1. Chicago, Illinois, August 11th, 2021. https://sec.report/Document/0001193125-21-242313/.

[8] Elevate Credit, Inc. "2020 Annual Report," February 26th, 2021. https://investors.elevate.com/filings-financials/sec-filings/sec-filings-details/default.aspx?FilingId=14750383.

In the category of digital bank accounts, a handful of small banks, usually with branches in a single assessment area, have partnerships with non-bank program managers who serve consumers nationally. For example, non-bank account program manager Chime now has twelve million active demand deposit accounts through Stride Bank after its customer account grew fifty percent during the pandemic.[9] Non-bank program manager Current, whose demand deposit account is issued by New York-based Metropolitan Commercial Bank, has enrolled three million consumers since its start in 2019.

These non-bank program managers conduct their business throughout the country, creating an inconsistency between the customers they serve and where they are obligated to meet their community reinvestment needs and conveniences. Some examples include the following:

- FinWise Bank has an assessment area in Salt Lake City, Utah but permits OppLoans and Elevate to use its charter to make high-cost loans in several states. Through third-party relationships in its Strategic Program division, FinWise facilitated $2.4 billion in loans in 2020.[10]
- First Electronic Bank, a Utah industrial loan company, has an assessment area in Salt Lake but facilitates loans for Personify in 19 states.[11]
- Republic Bank & Trust has assessment areas in Kentucky, southwestern Ohio, western Florida, and southeastern Tennessee[12] but facilitates lines of credit for Elevate Credit in 22 states and Easy Advance tax refund advances in all states. [13]

The lending facilitated through these partnerships is not included in the banks' CRA performance evaluations (PEs). Republic's PE only covers its home mortgage and small business loans. The PE states, "While the volume of loan originations by number through the Republic Processing Group is significant, RBTC's (Republic Bank & Trust Company) performance in extending loans in these areas was not reviewed, as it operates strategically outside the traditional retail banking operations and largely offered throughout the country (outside of the AAs)."[14]

Prudential regulators are not holding bank partners accountable for the misbehaviors of their demand deposit account program managers. Earlier this year Chime began to close accounts without the permission of account holders. Consumers filed complaints to the CFPB – not to the regulator of its partner bank.[15] No action against Stride Bank has been announced. When Chime referred to itself as a

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[9] Ron Shevlin. "Challenger Bank Chime Reaches The 12 Million Customer Mark." Forbes, February 1, 2021. https://www.forbes.com/sites/ronshevlin/2021/02/01/challenger-bank-chime-hits-12-million-customer-mark/.

[10] FinWise Bancorp. "FinWise Bancorp Registration Statement." Salt Lake City, Utah, July 15th, 2021. https://www.sec.gov/Archives/edgar/data/0001856365/000114036121024467/nt10024103x6_s1.htm#tB.

[11] National Consumer Law Center. "High-Cost Rent-a-Bank Loan Watch List." *National Consumer Law Center* (blog), March 17th, 2020. https://www.nclc.org/issues/high-cost-small-loans/rent-a-bank-loan-watch-list.html.

[12] Federal Deposit Insurance Corporation. "Republic Bank & Trust Company: Community Reinvestment Act Performance Evaluation." Louisville, Kentucky, January 6th, 2020. https://www7.fdic.gov/CRAPES/2020/23627_200107.PDF.

[13] Republic Bank & Trust. "Tax Refund Solutions - Republic Bank: Products." Accessed September 27th, 2021. https://www.republicrefund.com/Products/EasyAdvance.aspx.

[14] Federal Deposit Insurance Corporation. "Republic Bank & Trust Company: Community Reinvestment Act Performance Evaluation." Louisville, Kentucky, January 6th, 2020. https://www7.fdic.gov/CRAPES/2020/23627_200107.PDF.

[15] Kessler, Carson. "A Banking App Has Been Suddenly Closing Accounts, Sometimes Not Returning Customers' Money." ProPublica, July 6, 2021. https://www.propublica.org/article/chime.

bank, the California Department of Financial Protection and Innovation[16] and the Illinois Department of Financial and Professional Regulation[17] held Chime accountable for the misrepresentation. Stride Bank. In spite of existing guidance that placed responsibility on Stride Bank to monitor the actions of its partner, it did not – and Stride Bank was not penalized.

II. The third-party relationships governing rent-a-bank schemes are high-risk

Third-party relationships between banks and non-bank lenders deserve to be highlighted explicitly as "high-risk" The amount of activity is sizeable, interest rates can be very high, and many of the loans are not repaid. Non-bank lenders concentrate storefront payday loan stores in neighborhoods of color,[18] and are more likely to make high-cost internet payday loans to persons of color - [19] signaling that these partnerships may pose fair lending issues. Lending is a risky area with numerous compliance issues, and risks are high if the bank is not closely involved with all aspects of the loan program. These relationships should be defined as 'high-risk."

a) *When all loans made to consumers are considered in aggregate, banks engaged in rent-a-bank schemes distribute significant sums of money, usually at high interest rates.*

In the latest CRA performance evaluation for FinWise Bank, FDIC examiners estimated that FinWise Bank facilitated 360,000 loans worth a total of $1.9 billion in 2019.[20] Since then, FinWise has only expanded its rent-a-bank lending. In its S-1 Registration Statement offered to investors before an initial public offering of its stock, FinWise reported that it facilitated $2.4 billion in lending with third-party non-bank lenders in 2020.[21] Elevate uses FinWise Bank to originate Rise installment loans that can reach 149% APR.

OppFi, where interest rates may reach 160% APR, made $566 million in loans with bank partner FinWise in the two years ending in December 2020 and additional loans when it signed partnership agreements with two new partner banks during the latter half of 2020. During those years, 28.4 and 35.6 percent of OppFi loans were charged off.

In the same year, Republic Bank & Trust's Tax Refund Solutions division originated $95.7 million in loans to tax preparation providers. At the end of September 2019, it held $252 million in loans made

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[16] Smith, Mary Ann, Daniel P O'Donnell, and Paul Yee. The Commissioner of Financial Protection and Innovation v. Chime Financial, Inc. (March 2021).

[17] State of Illinois Department of Financial and Professional Regulation Division of Banking in the Matter of Chime Financial, No. 2021-DB-01 (March 25, 2021).

[18] Wei Li, Leslie Parrish, Keith Ernst, and Delvin Davis. "Predatory Profiling: The Role of Race and Ethnicity in the Location of Payday Lenders in California," March 26th, 2009. https://www.responsiblelending.org/california/ca-payday/research-analysis/predatory-profiling.pdf.

[19] Nick Bourke, Alex Horowitz, Walter Lake, and Tara Roche. "Fraud and Abuse Online: Harmful Practices in Internet Payday Lending." Pew Charitable Trusts, October 2014. https://www.pewtrusts.org/-/media/assets/2014/10/payday-lending-report/fraud_and_abuse_online_harmful_practices_in_internet_payday_lending.pdf.

[20] Federal Deposit Insurance Corporation. "FinWise Bank: Community Reinvestment Act Performance Evaluation." Murray, Utah, November 4th, 2019. https://www7.fdic.gov/CRAPES/2019/35323_191104.PDF.

[21] FinWise Bancorp. "FinWise Bancorp Registration Statement." Salt Lake City, Utah, July 15th, 2021. https://www.sec.gov/Archives/edgar/data/0001856365/000114036121024467/nt10024103x6_s1.htm#tB.

through Republic Processing Group, its online third-party consumer lending division – constituting 5.2 percent of its total portfolio at that moment. [22]

Republic Bank & Trust's agreement with Elevate requires it to hold ten percent of originated Elastic lines of credit (94 percent effective APR) on its balance sheet.[23] At the end of the 3rd quarter of 2019, Republic Credit Solutions had $99.15 million and $105.4 million in such loans on its balance sheet on September 30th, 2019[24] and December 31st, 2019,[25] inferring that the ten percent of loan participations held by Republic Bank & Trust as a part of its relationship with Elevate were a part of a moment-in-time portfolio of more than $990 million. Moreover, because this is only a snapshot in time of loans that have a duration of more than one month but no more than ten months,[26] the annual sums of facilitated loans are likely to be far more than $1 billion.

It is essential to clarify that bank partnerships do not uniformly facilitate high-cost lending. For example, many platform lenders that use the partnership model have procedures in place that cap interest rates to under 36 percent or below the applicable state interest rate cap, whichever is lower, and frequently at rates that are lower than risk-based credit card rates.[27]

b) *A high share of loans originated through bank partnerships are charged off – demonstrating that rent-a-charter structures often ignore the ability of many borrowers to repay their loans despite using a coercive repayment mechanism.*

OppFi has three bank partners: FinWise Bank, First Electronic Bank, and Capital Community Bank. In the first half of 2021, it used those partnerships to make approximately 86 percent of its originations.[28] . In 2019 and 2020, 42.2 percent and 35.6 percent of OppFi's loans (as a percentage of average net receivables) were charged off.[29] This poor performance has happened even though OppFi is an online lender that undoubtedly induces most of its borrowers to authorize automatic electronic repayment.

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[22] Federal Deposit Insurance Corporation. "Republic Bank & Trust Company: Community Reinvestment Act Performance Evaluation." Louisville, Kentucky, January 6th, 2020. https://www7.fdic.gov/CRAPES/2020/23627_200107.PDF.

[23] Elevate Credit, Inc. "2020 Annual Report," February 26th, 2021. https://investors.elevate.com/filings-financials/sec-filings/sec-filings-details/default.aspx?FilingId=14750383.

[24] Republic Bancorp. "Republic Bancorp, Inc. Form 10-Q." Quarterly Report. Louisville, Kentucky. Accessed October 7th, 2021. https://www.sec.gov/Archives/edgar/data/0000921557/000155837019010535/rbca-20190930x10q.htm#Item1FinancialStatements_384742.

[25] Republic Bancorp. "Republic Bancorp Annual Report for 2019." Annual Report. Louisville, Kentucky, March 13th, 2020. https://www.sec.gov/Archives/edgar/data/0000921557/000155837020002617/rbca-20191231x10k.htm.

[26] Elevate Credit, Inc. "Elevate Credit, Inc. Annual Report for 2019." Annual Report. Chicago, Illinois, February 14th, 2020. https://www.sec.gov/Archives/edgar/data/0001651094/000165109420000010/elevate10-kx2019.htm#sB10D30DD6CDACB98095C7F0C375B4669.

[27] Robert Adams. "Do Marketplace Lending Platforms Offer Lower Rates to Consumers?" Economic Research. FEDS Notes. Washington, DC: The Federal Reserve Board of Governors, October 22nd, 2018. https://www.federalreserve.gov/econres/notes/feds-notes/do-marketplace-lending-platforms-offer-lower-rates-to-consumers-20181022.htm.

[28] OppFi. "OppFi Inc. IPO Investment Prospectus." S-1. Chicago, Illinois, August 11th, 2021. https://sec.report/Document/0001193125-21-242313/.

[29] OppFi. "OppFi Inc. IPO Investment Prospectus." S-1. Chicago, Illinois, August 11th, 2021. https://sec.report/Document/0001193125-21-242313/.

Until it ended its bank partnership agreement earlier this year, CURO was using OCC-regulated Stride Bank as a partner to pilot its rent-a-bank loans that could reach 179% APR. More than 24 percent of CURO's unsecured installment loans were charged off in Q4 2020.[30]

Elevate relies on FinWise Bank for its Rise installment loan product and Republic Bank & Trust for its Elastic line of credit. Elevate does not report loan performance using charge-offs as a share of average loan receivables. Nonetheless, in using an alternative metric, the high-risk nature of the lending is revealed. In the last year, charge-off expenses were 52 and 41 percent of revenues for 2019 and 2020, respectively. Charge-offs are the highest expense items at Elevate. The cost of lending and the frequency of non-payment and defaults reflect the compromised nature of this lending -- a high-cost, high-default model that does not rely on consumers' ability to repay to be profitable. Echoing the similar nature of the lending, but from a second vantage point, Republic Bank's annual report for 2019 indicates that it has established a loan loss reserve allowance of 46 percent on the line of credit loans inside its Republic Processing Group division.[31] RPG is where it holds the loans it facilitates for Elevate Credit's Elastic Line of Credit product.

The charge-off rates demonstrate consumer harm and underscore our rationale for asking any future guidances to designate high-cost (above 36 percent or state rate caps, whichever threshold is lower) loans as "high-risk." The proposed guidance (page 26) asks banks to consider whether a third-party "has identified, and articulated a process to mitigate, areas of potential consumer harm, particularly in which the third-party will have direct contact with the bank's customers, develop customer-facing documents, or provide new, complex, or unique products." The relationships that facilitate the lending of the types referenced above are inherently harmful to consumers. Similarly, the proposed guidance (page 36) suggests that it might include benchmarks for risk management. If so, then the final guidance should have benchmarks for consumer harms.

c) *Safeguards to protect consumers from aggressive debt collectors should be strengthened. Some third-party non-bank lenders outsource their debt collection services to other third parties.*

Elevate, which services the loans it makes through its third-party relationships with FinWise Bank and Republic Bank, outsources its collections and customer service to a third party.[32] Enova uses bank partners to make its loans and acknowledges that it uses third-party debt collectors to cure some of its delinquencies.[33]

The Agencies should be skeptical about an agreement in which a non-bank third-party services loans originated by a bank but then outsources some of its debt collection practices to a third-party debt collection agency, as it suggests that the partner bank has little or no ability to exert influence over how customers who receive its loans are treated. Suppose the non-bank partner has a contractual relationship

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[30] CURO. "2020 Annual Report." 10-K. Wichita, Kansas, 2021. https://ir.curo.com/annual-reports.

[31] Republic Bancorp. "Republic Bancorp Annual Report for 2019." Annual Report. Louisville, Kentucky, March 13th, 2020. https://www.sec.gov/Archives/edgar/data/0000921557/000155837020002617/rbca-20191231x10k.htm.

[32] Elevate Credit, Inc. "2020 Annual Report." Chicago, Illinois, February 26th, 2021. https://investors.elevate.com/filings-financials/sec-filings/sec-filings-details/default.aspx?FilingId=14750383.

[33] Enova International. "Enova International, Inc. Annual Report for 2020." Annual Report. Chicago, Illinois, February 26th, 2021. https://ir.enova.com/annual-report-and-proxy-statement.

with a separate third party. In that case, the bank may have little or no ability to review and supervise the debt collection policies of the debt collector.

d) *The Agencies should prohibit bank partners from engaging in relationships with non-banks where they do not have complete control over all consumer-facing activities, regardless of whether the consumer-facing activities are the work of the non-bank partner or a contracted party to the non-bank partner.*

The guidance highlights that banks should be cautious about approving relationships where the third party lacks negotiating power.

While existing regulations place an expectation on banks to control underwriting, marketing, and other activities, the statements made by their non-bank lending partners underscore the inconsistency between that operating assumption and the on-the-ground reality. Consider, for example, how OppFi explains its business model to investors:

> *We are a leading financial technology platform that powers banks to offer accessible lending products through its proprietary technology and artificial intelligence ("AI") and a top-rated experience…Our bank partners benefit from our turnkey, outsourced marketing, data science, and proprietary technology to digitally acquire, underwrite and service these everyday consumers.*[34]

A turnkey service is just a service of such scope that there is minimal participation needed from the partner. Each partnership between a bank and a fintech creates a new set of supervisory challenges, as each fintech is likely to have a proprietary approach to analytics. The core value of many non-bank online lenders is their analytics – they do not look to bank partners to provide those services, and they are proprietary.

Moreover, regulators should view with skepticism the possibility that banks have the technological sophistication to adequately monitor the building, training, and optimization of artificial intelligence and machine learning systems. These systems are used in every step of the lending lifecycle, from marketing to underwriting and through to collections. The non-bank partners control every aspect of model creation and management, providing "turnkey" services and even the "analytics-as-a-service" systems used to improve the explainability of the AI itself.[35] The width (number of variables) and depth (number of cases) in data sets utilized to build and train these systems are becoming so substantial that it strains credulity to imagine that small banks can monitor the actions of their non-bank service partners. At the point in time when Upstart's model was operating under a no-action letter, its model had 1,600

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[34] OppFi. "OppFi Inc. IPO Investment Prospectus." S-1. Chicago, Illinois, August 11th, 2021. https://sec.report/Document/0001193125-21-242313/.

[35] Enova International. "Enova International, Inc. Annual Report for 2020." Annual Report. Chicago, Illinois, February 26th, 2021. https://ir.enova.com/annual-report-and-proxy-statement.

variables.[36] Enova's decision engine includes over 100 algorithms and more than 1,000 variables.[37] For years, Elevate Credit has reported that its model has more than ten thousand variables.[38]

e) *Banks must be sure that third-party non-bank partners do not violate the payment provisions in the CFPB's 2017 final rule on payday, vehicle title, and certain high-cost installment loans (the "payday rule").*

Under a court order issued in the Western District of Texas, the payment provisions in the 2017 final rule have been upheld and will go into effect on June 13th, 2022.[39]

Online installment lenders generally use commercial banks to collect pre-authorized payments through ACH networks. The payday rule prohibits payday lenders and installment and line-of-credit lenders where loans bear interest rates of greater than 36% APR from debiting a bank account after two earlier attempts have failed unless the lender has received reauthorization to do so from the borrower. Bank partners should be required to report on how they verify that non-bank partners are complying with this provision.

f) *These structures may undermine the reputation of partner banks.*

The provision of high-cost credit seems destined to provoke negative public opinion, as there are profound concerns held by many people and institutions about lending money at high interest rates. For centuries, institutions have raised concerns about the lending of money at unreasonably high rates of interest. The idea of usury – and the need to create laws to thwart it – reaches back to civilization's formative stages.

g) *They present risks associated with disparate impact and fair lending, including when lending is targeted at struggling consumers by non-bank third parties using artificial intelligence and machine learning.*

Non-bank partners provide the analytics to identify customers, collect applications, and determine the creditworthiness of potential borrowers.[40] They design the marketing strategies and decide whom to target.

Both the proposed guidance and prior Bulletins (e.g., OCC Bulletin 2020-10)[41] states that banks should conduct due diligence on the usage of alternative data for underwriting, fraud detection, loan pricing,

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[36] McCann, David. "Marketplace Lender Refines the Science of Underwriting." *CFO* (blog), December 2, 2019. https://www.cfo.com/applications/2019/12/online-lending-platform-refines-the-science-of-underwriting/.

[37] Enova International. "Enova International, Inc. Annual Report for 2020." Annual Report. Chicago, Illinois, February 26th, 2021. https://ir.enova.com/annual-report-and-proxy-statement.

[38] Elevate Credit, Inc. "2020 Annual Report." Chicago, Illinois, February 26th, 2021. https://investors.elevate.com/filings-financials/sec-filings/sec-filings-details/default.aspx?FilingId=14750383.

[39] Consumer Financial Protection Bureau. "Statement by CFPB Acting Director Uejio on CFPB Victory in Legal Challenge to Payday Lending Rule Protections," September 7th, 2021. https://www.consumerfinance.gov/about-us/newsroom/statement-cfpb-acting-director-uejio-cfpb-victory-in-legal-challenge-to-payday-lending-rule-protections/.

[40] Elevate Credit, Inc. "2020 Annual Report." Chicago, Illinois, February 26th, 2021. https://investors.elevate.com/filings-financials/sec-filings/sec-filings-details/default.aspx?FilingId=14750383.

[41] Office of the Comptroller of the Currency. "OCC Bulletin 2020-10." Third-Party Relationships: Frequently Asked Questions to Supplement OCC Bulletin 2013-29, March 5th, 2020. https://www.occ.gov/news-issuances/bulletins/2020/bulletin-2020-10.html.

servicing, marketing, and other aspects of account management. However, both that Bulletin and the prior Bulletin (2019-62) talked about the use of alternative data in a general context; the only empirical example was related to the use of cash flow data. As a result, content is absent to address the issues associated with the complexity and scope of alternative data used in online underwriting. As we noted earlier, marketplace techniques routinely use more than one thousand variables in an underwriting decision. These models break from traditional credit scoring in significant ways – for example, they are non-linear, rely on decision trees and dynamic variables, and are constantly in flux.

As a result, while the guidance's themes of bank accountability and rigorous assessment sound convincing, we think the proposal should be more skeptical of the ability of bank partners to supervise the AI and ML techniques being deployed in the marketplace.

It is also not clear that the banks will engage in rigorous fair lending testing of the lending program's marketing, underwriting, and other aspects. One non-bank lender says that it provides underwriting ("decision management platform as a service") and marketing services as well as analytics to optimize models and test for their explainability ("analytics as a service")[42] – suggesting that its bank partners no longer perform the functions required in existing guidance.

In describing its analytics, Elevate Credit provides evidence to support the view that managing a third party is not simple. In its most recent annual report, Elevate states:

> We have made substantial investments in our proven technology and analytics platforms to support rapid scaling and innovation, robust regulatory compliance, and ongoing improvements in underwriting. Our proven technology platform provides for nimble testing and optimization of our user interface and underwriting strategies, highly automated loan originations, cost-effective servicing, and robust compliance oversight. Our proprietary risk analytics infrastructure utilizes a massive (approximately 80+ terabytes) Hadoop database composed of more than ten thousand potential data variables related to each of the customers we have served. We are in the process of migrating our data stack to Snowflake, a next-generation cloud-based platform, which will provide us with improved scalability, reliability, and performance benefits to support our future growth. Our team of data scientists uses our proprietary technology to build and test scores and strategies across the entire underwriting process, including segmented credit scores, fraud scores, affordability scores, and former customer scores. We also use a variety of analytical techniques from traditional multivariate regression to machine learning and artificial intelligence to continue to enhance our underwriting accuracy while complying with applicable lending laws and regulations. As a result of our proprietary technology and risk analytics, more than 95% of loan applications are automatically decisioned in seconds with no manual review required.[43]

[42] Enova International. "Enova International, Inc. Annual Report for 2020." Annual Report. Chicago, Illinois, February 26th, 2021. https://ir.enova.com/annual-report-and-proxy-statement.

[43] Enova International. "Enova International, Inc. Annual Report for 2020." Annual Report. Chicago, Illinois, February 26th, 2021. https://ir.enova.com/annual-report-and-proxy-statement.

Elevate's analytics platform epitomizes the challenges that AI and ML create. The amount of information is vast, decision-making is not linear, weights are dynamic, and models change over time. To make it more difficult, decisions occur in seconds and without human review.

The guidance should state how bank partners will be held accountable to verify that these models are not biased against protected classes, that the models have been optimized not just for accuracy but also fairness, and that adverse action notices describe the reasons that resulted in an adverse decision. For example, the guidance could instruct banks on suitable pre and post-hoc methods for monitoring the systems used by their third-party relationships and standards for training methods and appropriate demographic makeups of training data sets.

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h) The guidance should state that models that are not explainable have heightened risks for discriminatory impacts.

Increasingly, third-party relationships involving lending are made through digital channels (online and mobile). The emerging models rely heavily on artificial intelligence (AI) and machine learning (ML) to provide instantaneous underwriting decisions and incorporate many variables, including alternative data. The guidance should include expectations for ensuring that decisions are explainable.

The Agencies should develop transparent systems for monitoring the use of algorithmic tools. Necessary steps include: Requiring lenders to use explainable models or to use explainability techniques that can accurately describe the reasons for a decision made by an AI model. The Agencies should staff and invest in testing models for explainability, including tests for explainability among different demographic groups.

- To fulfill the purpose of adverse-action notices, the CFPB should reconsider the content and form of adverse-action notices. The Agencies should require lenders only to use data elements that would give turned-down applicants the agency to improve their creditworthiness.
- The Agencies should address how consumers can resolve instances where lenders used incorrect data to evaluate applicants for creditworthiness.
- The Agencies should supervise and take enforcement action where lenders cannot demonstrate they have effectively performed disparate impact analysis of their use of AI and alternative data, including that provided by third parties. The Agencies should clarify that all financial institutions are accountable for ensuring a robust CMS that includes rigorous evaluations of their use of AI and alternative data.

i) Relationships that permit data aggregators to access customer information should be defined as a business arrangement, regardless of how it obtains the information.

Many banks have agreements with data aggregators. With the permission of a consumer, these companies can gain access to a consumer's bank account. Data aggregators may use automated programming interfaces (APIs) or screen scraping to access account information. Screen scraping is an older

technology, more susceptible to cyberattacks, and does not permit a consumer to place conditions on how his or her data is utilized.[44]

The proposed guidance would assign the "business arrangement" standard to contracts that permit a data aggregator to access consumer information through an API, but not when the information is obtained by screen scraping. The inconsistency creates a gap in consumer protection and has the counterintuitive effect of applying a lighter regulatory standard to a riskier technology. Screen scraping does not permit a consumer to apply gradations of permission. Moreover, the consumer is unlikely to perceive the difference when authorization is granted for screen scraping versus a system that uses an API. The guidance would not define screen scraping as grounds for a business arrangement but would only state that banks should "engage in appropriate risk management."

j. The guidance fails to alert banks to the risk that preemption authority may not apply, and the loan program may be found to be unlawful when it enables the issuance of credit at rates that exceed state laws.

Rent-a-charter relies on preemption power and undermines rate caps passed by states for payday and consumer installment lending. These partnerships have the effect of transferring preemption power to non-banks.

Rent-a-bank relationships exist to permit a non-bank high-cost lender to tap the preemptive immunity for a national bank or federal savings association from state usury laws (12 USC 85 or 1463 (g)). A lengthy litigation record exists to demonstrate that online lenders use bank partnerships to evade state laws and that states resent these evasions. The legal landscape is fluid, and banks that rent out their charters to non-bank entities run the risk that the lending programs will be deemed subject to state law and that the banks could be conspirators to usury evasions. The greater the disparity between a loan's interest rate and the legal state rate, and the more significant the role of the non-bank entity in designing, operating, and profiting from the loan program, the greater the likelihood that it will be viewed not as a bank lending program but as an unlawful evasion of state usury laws.

For example, the Attorney General of the District of Columbia filed a lawsuit against Elevate Credit for violating the District's Consumer Protection Procedures Act when it issued installment loans and lines of credit at interest rates of greater than 99 percent.[45] The complaint concerned loans issued through bank partnerships with FinWise Bank and Republic Bank & Trust. In remanding the case from federal to DC court, a federal court found that the AG's allegations are similar enough to older rent-a-bank schemes for the court to conclude that "the District has sufficiently alleged that Elevate is the true lender of the Rise and Elastic loans."[46]

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[44] Stephanie Wake. "A Short Prescription for Ensuring Responsible Open Banking in the United States." *Data Privacy, Security, Fintech & Innovation, and Fraud Reduction* (blog), September 9th, 2021. https://bpi.com/a-short-prescription-for-ensuring-responsible-open-banking-in-the-united-states/.

[45] Office of the Attorney General for the District of Columbia. "AG Racine Sues Predatory Online Lender For Illegal High-Interest Loans To District Consumers." June 5th, 2020. https://oag.dc.gov/release/ag-racine-sues-predatory-online-lender-illegal

[46] Distr. of Columbia v. Elevate, 2021 WL 2982143 at *9 (DDC July 15th, 2021).

III. Loans originated with interest rates of greater than 36 percent are especially high-risk and should be discouraged whether made directly or through a non-bank.

a) *The guidance should state that there is a heightened risk of violating the Military Lending Act* (MLA) *when loans are over 36%, especially when originated online through a third-party relationship.*

Lenders are prohibited from extending credit to service members and their families at rates that exceed 36 percent as calculated under the MLA. Any lending program above 36% runs the risk of violating the MLA.

b) *Heightened risk of providing national support for predatory lending, leading to consumer harm.*

When federal banking regulators permit national banks to originate high-cost credit, they encourage lending that is predatory, harmful to struggling consumers, and highly unpopular.

In poll after poll, the public has expressed its opposition to predatory lending,[47] [48]a preference for lower-cost small-dollar bank products as opposed to non-bank payday loans,[49] and support for a 36 percent annual interest rate cap on payday and consumer installment loans.[50]

By offering guidance on third-party lending without highlighting the risks of high-cost lending, especially lending that exceeds state interest rate caps, new guidance could be interpreted to permit predatory lending.

Conclusion

We applaud the Agencies for focusing on the critical questions of risk management of third-party relationships. Our comment calls attention to the particular problems posed by the subset of relationships that concern lending between banks and high-cost non-bank lenders.

We are concerned that the guidance does not include specific conditions associated with them, as they impact consumers, are achieving scale in the marketplace, and pose risks to harm consumers. They represent an example of innovation that may lead to financial inclusion of the wrong kind – giving consumers access to credit that they may not have the ability to repay.

Because third-party relationships naturally create a wall between banks and their customers, it undermines the ability of those banks to understand the needs and conveniences of underserved consumers.

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[47] GBA Strategies. "National Survey Results: Overwhelming Support for CFPB's Payday Lending Rule," June 10th, 2016. http://stopthedebttrap.org/wp-content/uploads/2016/06/Payday-Lending-Poll-Memo-June-2016.pdf.

[48] Lake Research Partners and Chesapeake Beach Consulting. "Bipartisan Support for Financial Regulation and Enforcement," January 22nd, 2015. https://www.responsiblelending.org/media-center/press-releases/Memo-CRL-Bipartisan-f-012215.pdf.

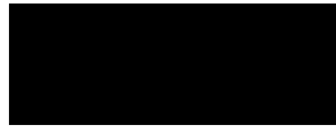
[49] Pew Charitable Trusts. "Americans Want Payday Loan Reform, Support Lower-Cost Bank Loans." *Issue Brief* (blog), April 19th, 2017. http://pew.org/2opyCMa.

[50] Center for Responsible Lending. "Bipartisan Support for Stopping Predatory High-Interest Loans," February 3rd, 2020. https://www.responsiblelending.org/es/research-publication/new-poll-bipartisan-support-stopping-predatory-high-interest-loans.

The third-party relationships governing rent-a-bank schemes are high-risk. Loans originated with interest rates of greater than 36 percent are especially high-risk and should be discouraged whether made directly or through a non-bank.

Thank you for the opportunity to provide input on the proposed guidance. Please reach out to me (jvantol@ncrc.org) or to Adam Rust (arust@ncrc.org) to answer additional questions or provide any clarifications.

Sincerely,



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