650 California Street, 12th Floor • San Francisco, CA 94108

February 4, 2020

Via Email: comments@fdic.gov

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

RE: Federal Interest Rate Authority – RIN 3064-AF21

Dear Chairman McWilliams:

Affirm, Inc. ("Affirm") is pleased to submit the following comments in strong support of the proposal by the Federal Deposit Insurance Corporation ("FDIC") that would clarify the interest permissible on state bank loans upon their transfer, sale, or assignment.[1]

As a partner to and a purchaser of loans from a state-chartered bank, as well as a seller of loans to banks and institutional investors, Affirm strongly supports the FDIC's proposal to address the market uncertainty created by the *Madden v. Midland Funding* decision.[2] Specifically, Affirm supports the codification of the longstanding legal principle that the legality and enforceability of a loan's interest rate terms are not affected by subsequent events such as the sale, assignment, or transfer of the loan.

We appreciate the FDIC taking steps to provide necessary clarity and certainty to this issue, which has only recently been called into question. For the reasons described below, we urge the FDIC to finalize the regulation and restore consistency to the market as soon as possible. We also encourage the FDIC to work closely with the Office of the Comptroller of Currency ("OCC") to ensure that the final language regarding the permissibility of interest rates is consistent, and, after promptly finalizing the regulation, we encourage the FDIC to continue to use its authority to ensure bank lending activities are safe and responsible.

About Affirm

Affirm is a financial technology company headquartered in San Francisco, CA that partners with a state-chartered, FDIC insured bank ("Bank Partner") to provide point-of-sale installment finance solutions at a variety of retailers from sectors including furniture and homewares, apparel, consumer electronics, and travel. When a consumer wants to make a purchase at a merchant partner, the consumer is

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[1] FDIC, "Federal Interest Rate Authority," 84 Fed. Reg. 66,845 (December 6, 2019).

[2] *Madden v. Midland Funding, LLC*, 786 F.3d 246 (2nd Cir. 2015).

given an option during the checkout process to apply for and, if approved, finance the purchase with a loan originated and funded by Bank Partner through the Affirm platform.

To expand access to responsible and affordable credit, banks have partnered with leading technology companies like Affirm to leverage their expertise in order to provide cost-efficient and consumer friendly products and services across the country. Pursuant to this model, Affirm performs services for loans originated by Bank Partner, including the use of technology to support the merchant integration, application processing, instant underwriting, and servicing of loans originated by Bank Partner.

The goal of this partnership is to offer consumers a quick, simple, and transparent alternative to credit cards. The consumer receives an instant credit decision during the checkout process. At that time, the consumer sees exactly what they will pay over the full loan term, including the total amount of interest, if they decide to take a loan. Loans made through the Affirm platform are closed-end installment loans with simple, daily accruing interest, APRs between 0-30%, and no fees charged to the consumer -- no origination fees, prepayment fees, late fees, or other fees are ever charged to the consumer. The consumer is never charged more than the amount disclosed up front and is not charged any additional interest such as deferred or compounding interest. Loan terms generally range from 3-48 months, with $800 as the average loan amount.

To date, Bank Partner has originated loans to over 4 million consumers through the Affirm platform, with more than $7 billion of loan volume.

Impact Of The Proposed Rule On Affirm And Innovation

This proposal will help foster responsible innovation in the banking system by providing clarity and stability to bank partnerships with financial technology companies and the loan market in general.

After Bank Partner originates a loan and issues the loan funds to a merchant on behalf of the consumer, Affirm may purchase the loan three to five days later. Affirm may then retain the loan, pledge the loan to a warehouse facility, or sell the loan to whole loan buyers, including banks and institutional investors.

As such, the ability of banks to partner with financial technology companies like Affirm and the transferability of the loans originated by banks are key components to the structure and viability of the partnership. More importantly, this structure allows for the provision of streamlined and cost-efficient products to consumers nationwide, pursuant to the bank's charter and supervision by the applicable federal and state regulators.

The ability of Affirm and Bank Partner to leverage the cost efficiencies and expertise of its partnership, and the ability of Affirm and Bank Partner to sell loans to loan buyers, has allowed for the provision of transparent point-of-sale loans to consumers at a significantly lower cost than traditional products in the small dollar loan space, such as rent-to-own, check cashing, and payday lending. However, in order for us to continue to offer these lower cost loans to consumers (below 30% APR with no fees), there must be clarity and consistency to the validity and enforceability of a loan after it is sold or transferred, whether to a bank or non-bank.

Impact Of The Madden Decision

Fallout from the *Madden* decision has created market uncertainty around partnerships between banks, financial technology companies, and loan purchasers and, in turn, the provision of more competitive and consumer-friendly products to all consumers. The result of this general uncertainty has been an inefficient and inconsistent market that threatens to spread, as we have seen in Colorado[3] as well as recent suits challenging securitization structures of performing credit card receivables originated by a national bank.[4] Such actions, without intervention from the FDIC, will continue to adversely affect credit availability as well as liquidity, which is ultimately detrimental to consumers.

In fact, there have been studies assessing the impact of the *Madden* decision on credit availability and a resulting rise in personal bankruptcy in the Second Circuit. For example, one study showed that after the *Madden* decision there was a 52% decline in credit availability in Second Circuit states for borrowers with FICO scores below 625, while outside the Second Circuit loans to these same borrowers increased by 124%.[5] Another study found not just a decline in credit availability caused by *Madden*, but also an observable rise in personal bankruptcies, particularly among low-income households in the Second Circuit states, as compared to other jurisdictions.[6]

The decision has also been met with a wide range of criticism as being wrongly decided as a legal matter, as well as unworkable as it undermines the smooth and logical functioning of our financial system. The Obama Administration's solicitor general, federal banking regulators, Members of Congress and outside commentators have all agreed that *Madden* was wrongly decided and has had a negative impact on credit availability.[7]

A 2018 Treasury Department report on fintech recognized that a broader adoption of *Madden* could restrict credit availability and recommended that the federal regulators address the challenges posed by *Madden*. The report also recognized the benefits bank and fintech partnerships can have, stating: "Treasury recognizes that partnerships between banks and marketplace lenders have been valuable to enhance the capabilities of mature financial firms. . . . Appropriately designed lending partnerships can

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[3] *See, e.g.*, *Meade v. Avant of Colo., LLC*, No. 17-CV-0620-WJM-STV, 2018 WL 1101672 (D. Colo. Mar. 1, 2018); *Meade v. Marlette Funding, LLC*, No. 17-CV-00575-PAB-MJW, 2018 WL 1417706 (D. Colo. Mar. 12, 2018).

[4] *See, e.g.*, *Cohen v. Capital One Funding, LLC*, No. 1:19-cv-03479-KAM-RLM (E.D.N.Y. 2019); *Petersen v. Chase Card Funding*, No. 1:19-cv-00741-LJV (W.D.N.Y. 2019).

[5] Honigsberg, Jackson, and Squire, *How Does Legal Enforceability Affect Consumer Lending? Evidence from a Natural Experiment*, 60 J. L. & Econ. 673, 709 (2017). Coauthor Robert J. Jackson, Jr., currently is a commissioner at the U.S. Securities and Exchange Commission. *See also* Charles Horn & Melissa Hall, *The Curious Case of* Madden v. Midland Funding *and the Survival of the Valid-When-Made Doctrine*, 21 N.C. Banking Inst. 1 (2017) at 22 (explaining that firms have started to exclude some Second Circuit states from lending programs and even removed loans to borrowers in the Second Circuit from securitization pools).

[6] *See* Piotr Danisewicz and Ilaf Elard, *The Real Effects of Financial Technology: Marketplace Lending and Personal Bankruptcy* (2018), available at https://ssrn.com/abstract =3208908.

[7] *See* Brief for the United States as Amicus Curiae, *Midland Funding, LLC v. Madden*, 2016 WL 2997343 (S. Ct. 2016) (jointly filed by the Solicitor General and the Office of the Comptroller of the Currency); H.R. 3299, 115th Cong. (2017); Rachel Witkowski, *Legislation Proposed to Counteract Court Ruling on State Usury Caps*, Wall St. J. (July 11, 2016), https://www.wsj.com/articles/legislation-proposed-to-counteract-court-ruling-on-state-usury-caps-1468278817; *and, e.g.,* Brief for the Clearing House Association L.L.C., Financial Services Roundtable, Consumer Bankers Association, Loan Syndications and Trading Association, and the Chamber of Commerce of the United States of America as *Amici Curiae* Supporting Petitioners, *Midland Funding, LLC v. Madden*, No. 15-610, 136 S. Ct. 2505 (2016).

leverage advantages from both banks and fintechs to improve upon the currently provided products. Treasury recognizes that these existing bank partnership arrangements have generally enhanced the provision of credit to consumers and small businesses."[8]

As the proposed rule astutely states, the ability of an assignee to rely on the enforceability and collectability of a loan that is validly made is central to the stability and liquidity of the domestic loan markets as well as important to safety and soundness. Denying an assignee the right to enforce a loan's terms would effectively prohibit assignment and render a bank's ability to make a loan at the rate provided by federal law illusory. The proposal provides a logical and fair rule that is necessary for the functioning and workability of our modern banking system and is consistent with longstanding market expectations as well as fundamental principles of contract law.

Further, not only is it imperative for the banking industry, but it is just as imperative that consumers know and understand the terms of the loan they enter into when the contract is signed, without the terms changing after the fact due to the bank's decision to sell or securitize the loan, which often occurs without the consumer's knowledge.

It is therefore vital the FDIC finalize this rule to ensure certainty for the markets and consumers, increase liquidity, and make credit more affordable for borrowers nationwide.

The FDIC's Authority

Consistent with existing law and authority, we agree that the proposal reasonably interprets the federal and state laws applicable to state-chartered banks in a way that is consistent with the grant of authorities under the Federal Deposit Insurance Act, including the inherent authority of state banks to assign loans and engage in banking activities similar to those listed in the National Bank Act as well as activities that are incidental to banking.[9] As such, the FDIC's reasonable interpretation of ambiguity should receive deference.

Request For Alignment Between FDIC And OCC Language

We request the FDIC work closely with the OCC to ensure that the final language regarding the permissibility of interest rates is as consistent as possible. Because these federal interest rate laws have been interpreted in the same manner historically, similarly worded provisions would be helpful for consistency and clarity. Particularly, we request both regulations reflect consistent language confirming

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[8] U.S. Dep't of Treas., Report, *A Financial System That Creates Economic Opportunities: Nonbank Financials, Fintech, and Innovation* (July 2018) at 11, 91-93.

[9] 84 Fed. Reg. at 66,848. *See also* Federal Deposit Insurance Corporation, Interpretive Letter No. 93-27, 1993 WL 853492, at *1 (July 12, 1993) ("We have stated consistently that [section 27 of the FDIA] was intended to give state-chartered FDIC-insured banks the same 'most favored lender' status and right to export interest enjoyed by national banks under . . . § 85 [of the NBA]."); Brief for the United States as Amicus Curiae, *Midland Funding, LLC v. Madden* at 7-8:

> A national bank's power to charge the interest rate authorized by Section 85 includes the power to transfer a loan, including the agreed-upon interest-rate term, to an entity other than a national bank. When Congress enacted Section 85's earliest statutory antecedent, it was already established that a bank's power to sell loans was a 'necessarily implied' corollary of the power to originate loans. *Planters' Bank of Miss. v. Sharp*, 47 U.S. (6 How.) 301, 322 (1848) (holding that state law that barred state bank from transferring a loan violates the constitutional prohibition on state impairment of contracts, U.S. Const. Art. I, § 10, Cl. 1).

that the interest on a loan is "determined as of the date the loan was made" and "shall not be affected by any subsequent events, including a change in State law, a change in the relevant commercial paper rate after the loan was made, or the sale, assignment, or other transfer of the loan." We recommend also including "or any interest in the loan" to the end of the provision. Alternatively, the agencies could make clear how the result effected by each rule is the same and therefore consistent with the *in pari materia* canon of construction.

The FDIC Should Continue To Use Its Authority To Ensure Bank Lending Activities Are Safe And Responsible

In addition to Affirm's strong support of the FDIC's expeditious action to address uncertainty triggered by the wrongly decided *Madden* case, Affirm continues to encourage that the FDIC use its regulatory and supervisory authority to set standards for bank lending programs and bank originated loans, including those that involve third-party service providers. The FDIC has set such standards and has successfully used its authority in the past to make clear that abusive or predatory lending programs and products were not welcome in the banking system.[10]

In the past, FDIC guidance and oversight over bank lending programs helped shut down irresponsible and abusive rent-a-bank schemes with payday lenders.[11] The FDIC can and should enhance and enforce such standards when appropriate to help protect consumers from predatory schemes and ensure that responsible bank programs and partnerships are encouraged, resulting in highly regulated and transparent consumer friendly financial products that can compete nationwide.

We appreciate the concern that the FDIC views unfavorably a state bank's partnership with a non-bank entity for the sole purpose of evading state law interest rates. To that end, we encourage the FDIC to continue to make clear to the banking industry its expectations regarding bank program standards and bank originated loans, including taking steps to finalize the proposed FIL-50-2016 Third Party Lending Guidance to help provide clarity to banks on how to manage appropriate and responsible third-party lending arrangements. Enforcing and enhancing such guidance will help protect consumers from predatory schemes and encouraging responsible bank lending in a safe and sound manner.

Conclusion

For the reasons stated above, Affirm urges the FDIC to quickly finalize the proposed regulation. As discussed, in the aftermath of *Madden* we have already seen an increase in litigation and negative consequences for consumers, especially for underserved, underbanked and low- and moderate-income ("LMI") borrowers in the Second Circuit. By codifying the longstanding legal principle that the legality

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[10] *See, e.g.*, FDIC, *Guidelines for Payday Lending* (2005 and revised Nov. 2015); FDIC, *Affordable Small-Dollar Loan Products Final Guidelines,* FIL-50-2007 (June 2007).

[11] *See, e.g.*, Democratic Staff Report Prepared for Democratic Members of the House Committee on Financial Services, *Skirting The Law: Five Tactics Payday Lenders Use To Evade State Consumer Protection Laws* (June 16, 2016) at 5 ("Similar to the rent-a-bank model that, before being shut-down by federal banking regulators, was previously embraced by lenders to avoid complying with state enacted payday bans"); Susanna Montezemolo, *Payday Lending Abuses and Predatory Practices: The State of Lending in America & its Impact on US Households*, Center for Responsible Lending (September 2013) at 11, 18, available at https://www.responsiblelending.org/sites/default/files/uploads/10-payday-loans.pdf (explaining that the FDIC "guidelines effectively ended the 'rent-a-bank' scheme in which payday lenders partnered with small banks in order to evade state laws").

of a loan's interest rate is determined at the time the loan is made and does not change due to a sale or assignment, the FDIC is ensuring there is clarity and consistency in our banking system and for consumers, and enforcing a logical, fair, and workable rule that is central to the stability and liquidity of the domestic loan markets. This certainty is imperative to ensure that banks may continue to collaborate with and responsibly utilize third-party service providers to expand access to financial services.

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We appreciate the opportunity to comment on this important rulemaking, and strongly encourage the FDIC to finalize the regulation as soon as possible.

Very truly yours,

AFFIRM, INC.

Sharda Caro-del-Castillo
Chief Legal Officer