<u>Via Electronic Mail</u>:
comments@fdic.gov

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, D.C. 20429
RIN 3064-AF21

Re: LendingClub Comment on Proposed Rulemaking Entitled "Federal Interest Rate Authority"

Ladies and Gentlemen:

LendingClub submits this comment letter regarding the notice of proposed rulemaking by the Federal Deposit Insurance Corporation (FDIC).[1] We agree that the Second Circuit's *Madden* v. *Midland Fundin*g decision misapplied federal law and erroneously undermined the valid-when-made doctrine by holding that a loan originated by a bank may become usurious when sold to a nonbank. LendingClub supports the FDIC's proposed rule and urges the FDIC to finalize it as soon as practicable.

LendingClub is a founding member of the Marketplace Lending Association (MLA)[2] and a member of the Structured Finance Association (SFA).[3] Both of these industry associations have submitted comment letters in support of the FDIC's proposal.[4] LendingClub provides this supplemental comment letter in order to offer additional perspective as the nation's largest facilitator of personal loans facilitating over $1 billion in loan volume per month. We also offer our perspective as the nation's largest online credit marketplace, selling responsible loan

[1] *See* FDIC, *Federal Interest Rate Authority*, 84 Fed. Reg. 66,845 (Dec. 6, 2019).

[2] MLA is the only trade association of marketplace lending companies, which generally use a two-sided marketplace and technology to provide better personal loan products for borrowers and investors. Marketplace lending is a subset category of fintech lending and online lending, in that all loans provided by MLA members must be under 36% APR and meet additional responsibility standards. *See* Marketplace Lending Association membership criteria, available at http://marketplacelendingassociation.org/about-us/; *see* also "Marketplace Lending Best Practices", available at http://marketplacelendingassociation.org/industry-practices/.

[3] SFA is a member-based, trade industry advocacy group focused on improving and strengthening the broader structured finance and securitization market.

[4] SFA's letter is written jointly with the Bank Policy Institute.

products to over 100 institutional investors including banks and asset managers, in addition to nearly two hundred thousand individual investors. The banks purchasing from our platform are predominantly community banks, including national and state-chartered institutions.

This letter outlines (A) the positive impact LendingClub's business has had on American borrowers, which this rulemaking would support, (B) the negative impact *Madden* has had on our efforts, on borrowers generally, and on the secondary market, and (C) additional action, beyond this rulemaking, the FDIC can take to protect consumers and the banking system from irresponsible lending partnerships.

We conclude that the proposed rule to fix *Madden* should be finalized. Furthermore, as part of Section C of this letter, we suggest that the FDIC next act to further support borrowers by protecting the banking system from a reemergence of bank-supported irresponsible lending partnerships. Just as the FDIC drove payday lenders out of the banking system when it issued Financial Institutions Letter 14-2005,[5] we urge the FDIC to use a similar method to address new types of potential borrower harm that has since emerged. Such guidance or regulation would prevent irresponsible lending partnerships, while promoting lower-cost access to credit for consumers, stability for banks and the secondary market, and innovation of better and lower cost credit products.

A. LendingClub's positive impact on American borrowers

LendingClub's mission is to empower our members on their path to financial health. We pursue this mission by encouraging responsible borrowing that lowers the cost of Americans' debt and reaches underserved populations. LendingClub accomplishes this by using technology to operate a lower cost and passing the savings on to customers, by employing machine learning and non-bureau data to improve pricing, through marketing that seeks borrowers with potentially high costs of credit, and by offering an enjoyable and positive customer experience. Most of the loans LendingClub facilitates are issued by WebBank, an FDIC-insured, Utah-chartered bank.

These loans feature fixed rates and fixed monthly payments, no balloon payments, no prepayment penalties, and no penalty interest rates, and APRs that never exceed 36%. We believe these types of personal loans offer Americans the best opportunity to achieve financial health, as compared to other sources of unsecured personal credit. To build industry standards around such lending, LendingClub co-founded the Marketplace Lending Association, which conditions membership on these responsible product features, including a 36% APR rate cap.[6]

Based on the findings of Federal Reserve researchers, it appears LendingClub has excelled in carrying out its mission. In a 2018 study these researchers concluded that "LendingClub's consumer lending activities have penetrated areas that may be underserved by traditional banks, such as in highly concentrated markets and in areas that have fewer bank branches per capita."[7]

[5] *See* FDIC, *Guidelines for Payday Lending*, FIL 14-2005 (March 2005, revised Nov. 2015), available at: https://www.fdic.gov/news/news/financial/2005/fil1405a.html.

[6] *See* note 2.

[7] Federal Reserve Bank of Philadelphia, Working Paper No. 18-13, *Do Fintech Lenders Penetrate Areas that are Underserved by Traditional Banks?*, pg. 1 (Mar. 2018), available at https://www.philadelphiafed.org/-/media/research-and-data/publications/working-papers/2018/wp18-13.pdf.

A later study by Federal Reserve researchers recognized that "consumers pay smaller spreads on loans from LendingClub than from credit card borrowing" and that the alternative data sources employed by LendingClub's technology have "allowed some borrowers who would have been classified as subprime by traditional criteria to be slotted into 'better' loan grades, which allowed them to get lower-priced credit."[8]

A third and most recent study, a joint effort by researchers at the Federal Reserve and Rutgers University, published in 2019, indicates that LendingClub-facilitated loans maintain exceptionally low default rates while extending access to credit to riskier borrowers.[9] The study defines a "best-practice ratio" which indicates "what ratio of nonperforming consumer loans to total consumer lending could a bank achieve if it were fully efficient at credit-risk evaluation and loan management?"[10] The research finds LendingClub among the best in the country, with defaults nearly at this best-practice margin – i.e., the defaults are largely the result of the inherent risk in the population served as opposed to inefficiency in underwriting.[11] In contrast, the study finds the underwriting efficiency of some major bank lenders to be 123x and 50x worse.[12]

This Federal Reserve and Rutgers University research has implications for financial inclusion. It indicates that LendingClub, relative to most banks, has "higher credit risk-taking and greater lending efficiency."[13] In other words, LendingClub is serving borrowers deemed by most banks to be too risky, while also maintaining extremely low default rates and the associated adverse outcomes for borrowers.

LendingClub is proud to facilitate these loans. They have a lower average cost than customers' credit cards, which is especially important today as credit card rates have hit record highs.[14] Average APRs for general purpose and private label credit cards have reached 20.3% and 26.4% percent, respectively.[15] These credit card APRs do not factor in the additional cost associated with fees charged in connection with card usage, which often make the cost associated with using credit cards even higher than the stated rates suggest, by as much as 3% according to the Consumer Financial Protection Bureau (CFPB).[16]

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[8] Federal Reserve Bank of Philadelphia, Working Paper No. 18-15, *The Roles of Alternative Data and Machine Learning in Fintech Lending: Evidence from the LendingClub Consumer Platform,* pg. 0 (April 2018, revised Jan. 2019), available at https://www.philadelphiafed.org/-/media/research-and-data/publications/working-papers/2018/wp18-15r.pdf.; ***see also*** Federal Reserve Banks of Philadelphia & Chicago, Working Paper No. 17-17, *Fintech Lending: Financial Inclusion, Risk Pricing, and Alternative Information* (Jul. 2017), available at https://www.fdic.gov/bank/analytical/cfr/bank-research-conference/annual-17th/papers/14-jagtiani.pdf.

[9] *See* Federal Reserve Bank of Philadelphia, Working Paper No. 19-22, *Consumer Lending Efficiency: Commercial Banks Versus A Fintech Lender* (April 2019), available at https://philadelphiafed.org/-/media/research-and-data/publications/working-papers/2019/wp19-22.pdf.

[10] *Id*. at pg. 16.

[11] *See id*. at pg. 21.

[12] *See id.* at pgs. 21-22.

[13] *See id*. at pgs. 16-17.

[14] *See* Consumer Financial Protection Bureau, *The Consumer Credit Card Market,* pg. 12 *(*Aug. 2019), available at https://files.consumerfinance.gov/f/documents/cfpb_consumer-credit-card-market-report_2019.pdf.

[15] *See id.* at pg. 12.

[16] *See* Consumer Financial Protection Bureau, *The Consumer Credit Card Market*, pgs. 60-61, (Dec. 2015), available at https://files.consumerfinance.gov/f/201512_cfpb_report-the-consumer-credit-card-market.pdf.

Our borrowers tell us that approximately 3 out of 4 personal loans received through LendingClub's platform are for refinancing or consolidating credit card debt. Although exact savings vary by consumer, such a borrower can save hundreds or thousands of dollars via a personal loan through LendingClub. These borrowers reduce the interest rate on their debt by about five percentage points and are placed on a responsible paydown plan due to the installment structure of the loan.

Similarly, LendingClub's auto loan program, which also facilitates WebBank loans, helps the average consumer save thousands of dollars over the life of the loan versus the loans they obtained at car dealerships, often by eliminating hidden dealer markups. Numerous studies have shown these markups to have a disparate impact on women and minorities.[17]

Finally, LendingClub's small business lending program reaches borrowers underserved by traditional banks, often in partnership with the nonprofit community development financial institution (CDFI) Opportunity Fund. The program has seen five times the representation of minority-owned businesses, and four times the representation of women-owned businesses, as compared to conventional bank lending. The small businesses LendingClub has served have created or sustained over 100,000 jobs.

Unfortunately, LendingClub's ability to provide these benefits has been negatively impacted by the *Madden* decision.

B. *Madden*'s negative impact on the secondary market and the American economy

Madden v. Midland Funding[18] is a textbook example of the old legal adage that "bad facts make bad law." Until *Madden*, the valid-when-made doctrine had been precedent for nearly two centuries.[19] As the Supreme Court described the doctrine in 1833, "the rule of law is everywhere acknowledged, that a contract free from usury in its inception, shall not be invalidated by any subsequent transactions."[20] Simply put, a bank loan's terms should not change merely because the loan is sold.

Madden began a domino effect in 2015 toward undermining this important proposition. At first, its ruling appeared restricted to unsympathetic debt collectors. The ruling prevented a debt collector from collecting on a bank loan at its original interest rate, due to a loan sale. But two years later, in 2017, the Colorado state attorney general sought to formally expand the decision to additional types of nonbanks by filing a suit that called into question rates when a bank loan is sold to nonbank loan facilitators.[21] The case also sought to expand *Madden* geographically by exporting a Second Circuit decision governing New York, Connecticut and Vermont to Colorado

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[17] According to research by the National Consumer Law Center, auto dealers are twice as likely to add markups to loans of African Americans than to white borrowers, and those markups are routinely two-to-four times higher for African Americans. *See* Stuart Rossman, *The Data Is Clear: Auto Lenders Discriminate*, US News & World Report (Nov. 2015), available at http://www.usnews.com/opinion/economic-intelligence/2015/11/17/dont-let-congress-weaken-oversight-of-discriminatory-auto-financing.

[18] 786 F.3d 246 (2nd Cir. 2015).

[19] *See, e.g., Nichols v. Fearson*, 32 U.S. (7 Pet.) 103 (1833).

[20] *Id.*

[21] *See Meade v. Marlette Funding LLC*, No. 17CV30376 (D.Colo. 2017); *Meade v. Avant of Colorado LLC*, No. 17CV30377 (D.Colo. 2017).

and the Tenth Circuit. The expansion continued when, in 2019, New York plaintiffs brought cases against additional types of nonbanks – this time securitization trusts – calling into question the rates on bank loans that had been transferred to trusts.[22]

The FDIC is correct to propose this rulemaking. The timing is right, before *Madden* expands to further types of institutions and geographies. We advocate the rulemaking's urgent finalization.

1. Harm to secondary market

As the nation's largest marketplace for personal loans, LendingClub has been on the front line of how *Madden* has affected the secondary markets, hearing investors' concern regarding buying marketplace loans ever since the case was decided. These concerns are critical. The US secondary market is the envy of the world and bedrock to the American financial system. Securitizations alone are the source of over $11.3 trillion in funding, over half the value of the US's $20 trillion economy.[23] The overall secondary market is a multiple of that, by definition.

LendingClub's success in facilitating responsible, lower-cost loans to borrowers depends on our ability to sell these loans to investors. We do not hold loans on our balance sheet except for very short durations.[24] Therefore, it is the varying risk appetites of our many loan buyers that enables us to confidently facilitate loans to borrowers at various FICO scores, without concentrating risk on ours or others' balance sheets. Our marketplace for purchasing these loans creates a virtuous cycle: the more investors demand loans of a certain credit quality, the less they require in interest payments for those loans, and the more interest rate savings we can pass on to borrowers.[25]

We noticed the impact of *Madden* almost immediately after it was decided. We observed and were told by loan buyers that the secondary market of marketplace loans was being disrupted as loan buyers began demanding higher yields on LendingClub-facilitated loans to certain Second Circuit borrowers. This development indicated that the buyers of these loans suddenly viewed these loans as less likely to be collectable. In other words, investors were less willing to pay for these loans because the loans suddenly became infused with new legal risk.

Indeed, this result was predicted in an *Amicus* brief to the Second Circuit panel deciding *Madden*, jointly submitted by the Obama Administration's Solicitor General and OCC. Their brief stated, "the marketability (and therefore the value) of a national bank's loan portfolio could be significantly diminished if the national bank could not transfer to assignees the right to charge the rate of interest that the national bank itself could charge" in arguing that the valid-when-made doctrine be fully upheld.[26]

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[22] *See Petersen, et al. v. Chase Card Funding, LLC, et al.*, No. 1:19-cv-00741-LJV (WDNY 2019); *Cohen, et al. v. Capital One Funding, LLC, et al*., No. 19-03479 (EDNY 2019).

[23] *See* Sec. Indus. & Fin. Mkts. Ass'n, *US ABS Issuance and Outstanding* (July 2019), available at https://www.sifma.org/resources/research/us-abs-issuance-and-outstanding; Sec. Indus. & Fin. Mkts. Ass'n, *US Mortgage-Related Issuance and Outstanding* (July 1, 2019), available at https://www.sifma.org/resources/research/us-mortgage-related-issuance-and-outstanding.

[24] For example, while loans are accumulated for bulk sales such as for securitizations.

[25] LendingClub does not earn spread.

[26] Brief for the United States as *Amicus Curiae*, *Midland Funding v. Madden*, No. 15-610, 2016 WL 2997343 at *9 (2016).

Numerous statements had been previously made by regulators warning of an adverse outcome if state usury rates could be suddenly applied to bank transactions with nonbanks.[27] Further, this result was also documented in a study by professors at Stanford, Columbia and Fordham Universities, including currently sitting Democratic SEC Commissioner, Robert Jackson.[28] That study concluded that "*Madden* reduced the price of notes backed by above-usury loans to borrowers in Connecticut and New York".[29]

Distorted demand for loans to Second Circuit borrowers has also been confirmed by conversations with institutional buyers of marketplace loans, including loans facilitated by LendingClub. Several tell us that they fear buying marketplace loans made to borrowers in the Second Circuit that are above state usury rates out of fear of the possible application of *Madden*. Additionally, more conservative institutions tell us they fear buying marketplace loans made to borrowers *outside* of the Second Circuit because they fear geographical expansion of *Madden*.

We hear similar concerns related to warehouse financing and the securitization markets. Several large financial institutions have offered to provide warehouse financing to us, but some indicate that they will not accept as eligible collateral marketplace loans in excess of Second Circuit usury rates for us or for our loan buyers. We do not just observe these sentiments, but industry literature supports them.[30] Similarly, we see that some large financial institutions have not been willing to underwrite securitizations that include loans with rates above Second Circuit usury limits, another observation that has been supported by literature.[31] Finally, there is at least one major credit rating agency that extrapolates the Second Circuit's *Madden* decision to other jurisdictions and expresses concern about the validity of any loan with a rate above the usury limit of any state.

With these concerns overhanging players in the markets for marketplace loans, a well-established and deep source of financing is not fully accessible. Without full access to financing, backed by confidence in the legal framework for the loans underlying the transactions, investor demand is muted and the cost of funding is unnecessarily high compared to other assets.

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[27] *See, e.g.,* John Hawke, Jr., Comptroller of the Currency, *Hearing of Housing and Urban Affairs Subcommittee on Banking* (2004) (stating "the continuing uncertainty about the applicability of state laws has already negatively affected national banks' ability to lend in certain markets and to access the secondary market"); Julie Williams, Senior Deputy Comptroller and Chief Counsel, OCC, *Hearing of Subcommittee on Oversight and Investigations of the House Financial Services Committee* (2004) (stating "[s]tate-based restrictions on loan terms substantially affect the marketability of such loans").

[28] *See* Colleen Honigsberg, Robert J. Jackson, Jr. and Richard Squire, *How Does Legal Enforceability Affect Consumer lending? Evidence from a Natural Experiment*, Journal of Law and Economics (Nov. 2017), available at https://pdfs.semanticscholar.org/b68b/39250f72d723e85d480e3927f4957afdc584.pdf. We understand this study has been submitted as a formal comment to the FDIC's proposed rulemaking.

[29] *Id*. at pg. 675.

[30] *See* Joy Wiltermuth, *Usury worries hit Avant collateral*, International Financing Review (Aug. 2015).

[31] *See* Will Caiger-Smith, *Prospect Capital may rejig ABS deals amid usury worries*, International Financing Review (Sept. 2015).

2. Harm to Americans

This problem in the secondary market has reverberated into the American economy in ways that have harmed borrowers. This proposition has been evidenced in at least three studies.

The first such study found that *Madden* "reduced credit availability for higher-risk borrowers in affected states" as people with FICO scores below 625 FICO lost over half their access to credit post-*Madden* in the Second Circuit.[32] But at the same, borrowers who are less in need of credit options (i.e. those with FICO scores above 700) received no decline in loan volume. Meanwhile, outside of the Second Circuit, credit flowed to borrowers who most needed it, as loan volume to sub 625 FICO borrowers increased by 124%.[33]

The second study, performed in 2018, found that *Madden* caused personal bankruptcy to spike due to a decline in marketplace lending in the Second Circuit, again negatively impacting the neediest borrowers.[34] The researchers found an 8% increase in bankruptcies in the *Madden*-affected states, and reasoned that "marketplace lending may help households, particularly those on low incomes, avoid bankruptcy and … the screening and lending technology behind marketplace credit may have some positive welfare effects compared with other forms of costly credit, such as payday loans and credit card debt, associated with worsening personal bankruptcy."[35] The study also found that lending to borrowers with incomes under $25,000 fell by 64%, as compared to non-*Madden* states, while lending to borrowers with incomes above $100,000 remained unchanged.[36] It concluded that *Madden* caused "a pullback of marketplace lending… persistently raising personal bankruptcy filings, particularly among low-income households."[37]

A third report by the Brookings Institution's Center on Regulation and Markets again considered *Madden* in 2019 and, aligned with the previous two studies, concluded that "[t]he economic consequences of *Madden*… are not good for the cause of financial inclusion." The report agreed that "the average citizen is the one who will have to pay more when those investors leave the field."[38]

Brookings made an additional point about the impediment *Madden* represents to the development of more consumer-friendly financial products. It stated, "[s]ome of the most important innovations in finance are aimed at making credit intermediation fairer and more efficient. *Madden* stands in the way." The report explains that *Madden* is reducing firms' abilities to originate and distribute loans without the balance sheet of a large financial institution, including the ability to accept the regulatory and supervisory burdens of national banks." As a

[32] *See* note 28 at pg. 673.

[33] *See id.*

[34] *See* Piotr Danisewicz and Ilaf Elard, *The Real Effects of Financial Technology: Marketplace Lending and Personal Bankruptcy* (July 2018), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3208908. We understand this study has been submitted as a formal comment to the FDIC's proposed rulemaking.

[35] *Id.* at pg. 28.

[36] *See id.*

[37] *Id.* at pg. 33.

[38] Peter Conti-Brown, *Can fintech increase lending? How courts are undermining financial inclusion*, Brookings Institution (April 2019), available at https://www.brookings.edu/research/can-fintech-increase-lending-how-courts-are-undermining-financial-inclusion/.

result, competition and innovation are impaired. "To put the point bluntly," the report concludes, "those who want to see more diversity in business models to support the least well off in our financial system should wince at the way that *Madden* puts megabanks at the center of borrowing and lending."[39]

Contributing to the results of these studies are the wide differences between state usury rates and the consumer products used in the modern economy. For example, the state of Connecticut in the Second Circuit has a rate cap of 12% for loan amounts above $15,000.[40] Vermont has a rate cap of as low as 12% or 18% for loan amounts above $1,000, depending on ultimate loan size.[41] When considering these rate caps against the most common unsecured consumer credit product – the credit card[42] – wide disparities emerge. The APR for general purpose and private label credit cards, which does not include credit card fees, has reached 20.3% and 26.4% percent respectively, with some cards exhibiting a fee-inclusive total cost of credit near 40%.[43] This contrast between credit cards and state rate caps suggests that borrowers' use of credit in the modern economy has grown since the contemplation of some states' laws in this area. For this reason, LendingClub and others advocated for establishment of a 36% usury rate in California, which was recently enacted, aligning credit needs with the modern economy while protecting consumers.

Given the above studies and points, we are concerned that the benefits LendingClub provides American borrowers will be greatly reduced if *Madden* is allowed to expand and is not corrected. Credit will continue to contract and bankruptcies will needlessly rise, as the studies indicate.

There is another pernicious impact to the American economy as a result of *Madden*, alluded to in the Brookings report. Current market participants and new entrants seeking to provide responsible credit are discouraged from entering the market because of the lack of legal certainty, particularly when related to fundamental concerns such as geographic market size. In order to assess revenues and potential costs, innovators today have to ask basic questions such as (a) "which circuit will adopt *Madden* next?"; (b) "to what type of nonbank will *Madden* next apply?"; (c) "would these potential expansions of *Madden* void the entire loan or just limit the amount of interest that could be collected?" As the current credit card rates and the current personal loan rates offered via marketplace lending companies (among others) reflect, the risk-based price of offering credit to many new and existing borrowers exceeds many states' usury rates. And these questions do not address further analysis that could ultimately be required, including consideration of how many people who could be served below the 36% APR standard of the marketplace lending industry could no longer be offered loans if *Madden* expanded to a given state.[44]

Using LendingClub as an example, we can attest that the technology and marketing expertise we provide WebBank has been a significant investment. Similarly novel technological investments would be very challenging to embark on, for us and for others, given the

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[39] *See id.*

[40] Conn. Gen. Stat. Ann., §§ 36a-558 and 36a-555.

[41] Vt. Stat. Ann. tit. 9, § 41a.

[42] The credit card market has reached $900 billion (dwarfing all other forms of unsecured personal credit), continues to grow, and is exempt from state usury rates. *See* note 14 at pg. 11.

[43] *See id*. at pgs. 12, 57.

[44] See note 2.

fundamental outstanding questions. These concerns are only getting more complicated as *Madden* expands. Meanwhile, the balances of the credit cards Americans could refinance through a marketplace lending company continue to increase to record highs with costs to borrowers reaching "the highest overall level observed."[45] Without FDIC intervention, businesses that seek to invest in complex underwriting technology to provide credit to such borrowers will be disincentivized and inhibited by *Madden*.

We are therefore far from alone in our view that *Madden* must be fixed. Not only is the FDIC joined by the OCC in this proposed regulation, but also the OCC and Solicitor General under President Obama similarly called the *Madden* decision "incorrect."[46] Raj Date, the first Deputy Director to the CFPB, agreed and recently wrote "Madden achieved nothing to advance a sensible consumer protection agenda, but instead set back the financial system's long-overdue progress toward efficiency and inclusion."[47] Furthermore, the Republican members of the House Financial Services Committee urged the OCC to mitigate the consequences of the *Madden* decision and that "this issue be made a priority."[48] Associations representing the banking industry, small business, and fintech urged Congress to codify the valid-when-made doctrine.[49] The Financial Health Network, then known as the Center for Financial Services for Innovation, wrote that fixing *Madden* would "bring competition and choice into the marketplace, improving affordable, high-quality credit products for consumers and small businesses."[50] The Treasury Department even recommend the regulatory solution proposed here, stating that federal regulators should "use their available authorities to address challenges posed by *Madden.*"[51]

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[45] Credit card balances at the end of 2018 were "well above their pre-recession peak of $792 billion." See note 14 at pg. 9-10.

[46] See note 26 at *5-6 (further stating that "[t]he court of appeals erred in holding that state usury laws may validly prohibit a national bank's assignee from enforcing the interest-rate term of a debt agreement that was valid under the law of the state in which the national bank is located.").

[47] Raj Date, *Madden ruling was a step backward. Congress should fix it*, American Banker (Dec. 4, 2017), available at https://www.americanbanker.com/opinion/madden-ruling-was-a-step-backward-congress-should-fix-it.

[48] House Financial Services Committee Republican Members, *Letter to Comptroller Otting* (Sept. 19, 2019), available at https://buckleyfirm.com/sites/default/files/Buckley%20InfoBytes-%20House%20Republican%20letter%20to%20OCC%20re.%20Madden%20-%202019.09.19.pdf.

[49] *See* National Federation of Independent Business, National Small Business Association, Small Business Entrepreneurship Council, Innovative Lending Platform Association, Marketplace Lending Association, Financial Innovation Now, Financial Services Roundtable, Independent Community Bankers of America, American Bankers Association, The Consumer Bankers Association, The Clearing House Association, and U.S. Chamber of Commerce, ***Letter to Senators Warner and Toomey and Representatives McHenry and Meeks***, (Oct. 2017), available at: https://financialinnovationnow.org/2017/10/05/fin-joins-broad-industry-coalition-supporting-mchenry-warner-legislation-to-ensure-access-to-credit/.

[50] Center for Financial Services Innovation, *Letter to Chairman Crapo and Ranking Member Brown* (Feb. 2018).

[51] *See* United States Treasury Department, *A Financial System That Creates Economic Opportunities: Nonbank Financials, Fintech, and Innovation,* pg. 93 (July 2018).

C. Beyond fixing *Madden*, the FDIC can further support borrowers

During the debates over *Madden*, an important concern has been a re-emergence of high-rate, irresponsible lending partnerships sponsored by banks. Some commentators argue forcefully that irresponsible partnerships must be regulated and curtailed. We strongly agree.

In our view, not only would such regulation or guidance help in its primary purpose of protecting borrowers from high-priced cycles of debt and stress – something we see and hear all too often from borrowers who come to our platform – such regulation would also be good for the economy. Responsible, lower-priced credit allows borrowers to spend more on goods and services, to experience less stress to be more productive workers, and to avoid defaults and bankruptcies that can adversely ripple through economic sectors.

However, although we agree on this point, we disagree with these commentators that fixing *Madden* empowers irresponsible lending partnerships. In fact, in our view, the opposite is true.

First, in the personal loan space, the credit providers that *Madden* most hinders are not high-rate lenders but are marketplace lending companies like LendingClub. As described above, these companies provide responsible products with APRs that are always under 36%,[52] in contrast to many lenders who offer borrowers APRs in excess of 100% and without affordably-structured installment plans. It is precisely because of our responsible product structures that we can host robust marketplaces for the purchase of these loans, which irresponsible lenders cannot. Investors prefer products that are void of the safety-and-soundness and reputational risks that are associated with irresponsible products. For example, we do not believe LendingClub would be able to attract dozens of regulated banks who purchase a significant portion of the loans we facilitate, if our products were not responsible.

Second, fixing *Madden* empowers responsible firms like LendingClub to compete with firms that offer higher prices. As described above, it is the valid-when-made doctrine that helps LendingClub lower prices for borrowers as we seek to provide a path to financial health. We actively compete with higher-priced personal credit, and this competition places downward pressure on prices. For example, the Wall Street Journal has credited LendingClub and other marketplace lending companies for the competitive pressure that has led major credit card banks to begin offering lower-rate personal loans to their own credit card customers.[53]

Finally, fixing *Madden* will remove the distraction that has impeded solving the most important consumer protection issue raised by online lending – namely, abusive bank partnerships that offer irresponsible products. For the same reasons laid out in the beginning of this section, we believe regulatory action is needed to address irresponsible bank partnerships in order to support borrowers and promote economic growth.

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[52] See note 2.

[53] *See, e.g.*, AnnaMaria Andriotis and Peter Rudegeair, *AmEx's Lending Push Goes Beyond Cards: The iconic card company is expanding into personal loans for the first time*, Wall Street Journal (March 9, 2017), available at https://www.wsj.com/articles/amexs-lending-push-goes-beyond-cards-1489084412. (stating "AmEx's foray into personal loans is happening as the company is under pressure to maintain market share in the card market while also fending off growing competition from a host of lending rivals … British bank Barclays PLC has also joined in … Discover Financial Services, too, is ramping up in personal loans …" and further stating "[i]n the wake of the financial crisis, many banks cut back on these loans … [t]his left an opening for online lenders such as LendingClub Corp. and Prosper Marketplace Inc … [w]hile personal loan rates often range from roughly 6% to 20%, credit-card charges often exceed 20%.").

The Financial Health Network, then known as the Center for Financial Services Innovation, suggested in 2018 that regulatory action can protect consumers and the banking system from irresponsible lending, without withholding the benefits of affirming valid-when-made. "We understand that some groups are concerned that codifying valid-when-made would simply facilitate "rent-a-bank" schemes that rely on the preemption of state usury laws to charge high (in many cases, triple-digit) interest rates well in excess of state rate caps," they wrote. "However, we note that the Office of the Comptroller of the Currency (OCC) issued guidance in 2000, stating that 'Payday lenders entering into such arrangements [*that is, third party arrangements*] with national banks should not assume that the benefits of a bank charter, particularly with respect to the application of state and local law, would be available to them.' We believe the prudential supervisors can effectively enforce this guidance and mitigate against the rent-a-bank and interest-rate export risks."[54]

Therefore, there is no need to look far for regulatory precedent in order to tackle this issue. Similar to the OCC advisory letter noted by the Financial Health Network,[55] the FDIC issued FIL 14-2005 fifteen years ago, entitled "Guidelines for Payday Lending," which received wide acclaim for similarly ending abusive relationships between payday lenders and banks.[56] In it, the FDIC warned banks against "the significant credit, operational, legal, and reputation risks inherent in payday lending."[57] This guidance has since been broadly recognized for its efficacy in ending abusive partnerships between banks and payday lenders.[58]

Our view is that the FDIC could modernize this guidance by incorporating changes that have occurred in the small dollar market over the past 15 years. Although payday lenders (i.e., providers of "small-dollar, short-term, unsecured loans that borrowers promise to repay out of their next paycheck" as defined by the FDIC[59]) are still restricted from partnering with banks under current guidance, it is well documented that over the intervening years many payday lending companies have migrated to offering high cost installment lending.[60] These providers

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[54] *See* note 50.

[55] OCC, *Payday Lending,* Advisory Letter 2000-10 (Nov. 27, 2000).

[56] *See* note 5.

[57] *See id.* at pg. 1.

[58] The FDIC "guidelines effectively ended the 'rent-a-bank' scheme in which payday lenders partnered with small banks in order to evade state laws." Center for Responsible Lending, *Payday Lending Abuses and Predatory Practices,* pg. 11, fn. 21 (Sept. 2013), available at https://www.responsiblelending.org/sites/default/files/uploads/10-payday-loans.pdf; "[T]he rent-a-bank model … before being shut-down by federal banking regulators, was previously embraced by lenders to avoid complying with state enacted payday bans…" Democratic Staff Report prepared for House Financial Services Committee, *Skirting The Law: Five Tactics Payday Lenders Use to Evade State Consumer Protection Laws*, pg. 5 (June 2016), available at https://financialservices.house.gov/uploadedfiles/06.15.2016_committee_report_skirtingthelaw_final.pdf; "In the early 2000s, the federal bank regulators shut down rent-a-bank arrangements like these..." Americans for Financial Reform, *News Release: FDIC/OCC Proposal Would Encourage Rent-a-Bank High-Cost Predatory Lending* (Nov. 2019), available at http://ourfinancialsecurity.org/2019/11/fdicocc-proposal-encourage-rent-bank-high-cost-predatory-lending.

[59] *See* note 5 at pg. 1.

[60] *See, e.g.,* Paul Kiel, *Whack-a-Mole: How Payday Lenders Bounce Back When States Crack Down,* ProPublica (Aug. 6, 2013), available at https://human.libretexts.org/Bookshelves/Literature_and_Literacy/Book%3A_Thematic_Reading_Anthology_(Lumen)/09%3A_Consumer_Debt/09.4%3A_%E2%80%9CWhack-a-Mole%3A_How_Payday_Lenders_Bounce_Back_When_States_Crack_Down%E2%80%9D_by_Paul_Kiel.

are no longer "payday" lenders: their terms are longer than one pay period, amounts may be higher, and different repayment structures are employed. But some of them can be just as irresponsible.

Just as the MLA wrote in a comment letter to the FDIC regarding regulating small dollar lending,[61] we suggest that FDIC guidance on bank partnerships consider the nature and quality of the emerging loan products for their implications to credit, operational and reputational risk, as the FDIC did in FIL 14-2005. Lending services that are priced at greater than 36%[62] or result in expensive debt-trap cycles of reborrowing may pose increased risks to the banks, according to the MLA letter. We believe modernizing the FDIC's guidance in this way, once the proposed *Madden* fix regulation is finalized, would mimic the success the FDIC achieved in 2005 before the small dollar market changed.

[61] The MLA encouraged the FDIC to "[c]onsider how the nature and quality of the loan products themselves should be highlighted in the Guidance for their implications to reputational and safety-and-soundness risks. Lending products with APRs greater than 36% can at times result in expensive 'debt-trap' cycles of re-borrowing and may pose longer-term but nevertheless important risks to the banks, including risks of reputational harm and customer attrition. In a risk-based vendor management framework, such longer-term risks are important considerations. We suggest they be discussed in the Guidance." Marketplace Lending Association, *Re: Request for Information on Small-Dollar Lending – FIL 71-2018*, pg. 10 (Jan. 2019), available at https://www.fdic.gov/regulations/laws/federal/2018/2018-small-dollar-lending-3064-za04-c-061.pdf.

[62] We suggest 36% because of the extensive federal precedent for considering 36% as a rate that appropriately demarks increased risk:

First, in 2006, the US Congress passed the Military Lending Act, protecting active duty servicemembers from being charged more than a 36% APR for unsecured installment loans, overdraft lines of credit, short-term loans (e.g., payday loans, deposit advance products), and vehicle title loans. *See* 10 U.S.C. 987 (2006).

Second, FDIC Small-Dollar Loan Guidance states, "we encourage lenders to offer small-dollar credit with APRs no greater than 36 percent." FDIC, *Affordable Small-Dollar Loan Products Final Guidelines,* FIL 50-2007 (June 2007), available at https://www.fdic.gov/news/news/financial/2007/fil07050.html.

Third, the CFPB Rule on Payday and High-Cost Installment Loans issued in 2017 banned lenders of high-cost installment loans (with 36%+ APRs), among others, from making multiple attempts to withdraw payments from borrowers' checking accounts. Although portions of this rule are subject to repeal, this 36%+ provision for installment loans remains. *See* 12 C.F.R. § 1041.

Conclusion

For the above reasons, the urgent finalization of the FDIC's proposed rulemaking is essential, and its power to do so is supported by substantial Supreme Court precedent.[63]

LendingClub is pleased to support the *Madden* fix proposal and appreciates the opportunity to provide our comment letter. Please do not hesitate to contact us at rneiman@lendingclub.com or ameyer@lendingclub.com.

Respectfully submitted,

[redacted]

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[63] Section 27 of the FDIA is interpreted *in pari materia* with section 85 of the National Banking Act, and previous OCC interpretations of section 85 have been upheld by the Supreme Court. *See Greenwood Trust Co. v. Massachusetts,* 971 F.2d 818, 827; *see also Marquette Nat'l Bank v. First of Omaha Svc. Corp.*, 439 U.S. 299, 313-19 (1978) (affirming that a national bank may charge interest permitted by the state of its location to borrowers outside that state even when the borrower's state prescribes a lower rate); *Smiley v. Citibank*, 517 U.S. 735 (1996) (affirming the OCC's definition of the term "interest"). Furthermore, courts have consistently held that the FDIC's reasonable interpretations of the FDIA receives substantial deference given that the FDIC has specialized expertise regarding the country's complex banking laws. *See, e.g.*, *FDIC v. Philadelphia Gear Corp.*, 476 U.S. 426, 436-38 (1986) (indicating that FDIC interpretations of the FDIA are entitled to substantial deference, especially because of the "complex statutory scheme that the FDIC administers"); *Investment Company Institute v. FDIC*, 815 F.2d 1540, 1550 (D.C. Cir. 1987) (explaining that courts defer to the FDIC given its expertise on the banking laws).