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VIA EMAIL: thirdparty lending@fdic.gov

Martin J. Gruenberg
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Re: *Comments to Proposed Examination Guidance for Third-Party Lending, FIL-50-2016*

Dear Chairman Gruenberg:

The Massachusetts Attorney General's Office submits these comments regarding the FDIC's Proposed Examination Guidance for Third-Party Lending ("Proposed Guidance").

We applaud the Proposed Guidance and the FDIC for applying increased scrutiny to third-party lending arrangements between non-bank online lenders and FDIC-insured institutions. As the Proposed Guidance acknowledges, non-bank lenders often seek relationships with insured institutions because these lenders "lack[] the necessary licenses or charter to lend on [their] own behalf or seek[] to take advantage of the institution's ability to export interest rates."¹ Given the history of predatory lending associated with these "rent-a-bank" and "rent-a-charter" arrangements, we are skeptical that the benefits to consumers outweigh the harm in third-party lending arrangements where insured institutions act as mere originators of record. Moreover, in the majority of cases, insured institutions will not have sufficient resources or ability to effectively monitor third-party lenders. Thus, as the FDIC undertakes the supervisions and enforcement actions envisioned by the Proposed Guidance, we urge you to apply heightened scrutiny to those cases involving "rent-a-bank" and "rent-a-charter" activity with the goal of significantly limiting or ending risky and abusive third-party lending.

¹ As the Proposed Guidance acknowledges, multiple courts have recently concluded that a "rent-a-bank" arrangement does not entitle the participant to export home state interest rates. *CashCall, Inc. v. Morrissey*, No. 12-1274, 2014 WL 2404300, at *1 (W. Va. May 30, 2014), *cert. denied sub nom. CashCall, Inc. v. Morrissey*, 135 S. Ct. 2050 (2015). This Office is committed to taking appropriate enforcement action against third-party lenders that violate Massachusetts' consumer protection laws. *See Commonwealth v. Western Sky Financial, LLC, et al.*, Suffolk Sup. Ct. Civ. A. No. 15-3044D (2015).



Online marketplace lending has experienced exponential growth in recent years.² While potentially expanding access to credit to underserved market segments, online lending poses significant risk of consumer harm. Online lenders increasingly target sub-prime consumers³ and are moving from traditional balance-sheet “lend and hold” business models to hedge fund and venture capital backed “lend and securitize” models like those that facilitated the risky practices leading up to the sub-prime mortgage crisis.⁴ In May 2016, the U.S. Department of the Treasury released a report highlighting a number of dangers for consumers in online lending, including:

- The misuse of consumer data from credit underwriting;
- The risk of disparate impact in credit outcomes;
- The potential for fair lending violations and the inability of consumers to check and correct data used in underwriting decisions; and
- Bank liquidity risk due to undeveloped securitization markets and untested credit models based upon consumer loans with high charge off and delinquency rates.⁵

Additionally, the credit extended by online lenders comes at a high cost, often far exceeding the usury limits set by state legislatures in the borrower’s state of residence. The risk of consumer default is further exacerbated by a failure by lenders to underwrite based upon a consumer’s ability to pay. For example, in one recent court case involving a non-bank lender that purported to partner with an insured institution, the Court found the following egregious consumer abuse:

Between August of 2006 and February of 2007, CashCall purchased loans made by FB & T to 292 West Virginia residents. Of those loans, ten were for \$1,075.00 at an eighty-nine percent annual interest rate; 214 were for \$2,600.00 at a ninety-six percent annual interest rate; and the remaining sixty-three loans were for \$5,000.00 at a fifty-nine percent annual interest rate. Eventually, 212 of CashCall’s 292 West

² Kevin Wack, *Marketplace Lending Grew by 700% in Four Years: Report*, American Banker: Marketplace Lending, Apr. 8, 2016, available at <http://www.americanbanker.com/news/marketplace-lending/marketplace-lending-grew-by-700-in-four-years-report-1080341-1.html>.

³ See Kroll Bond Rating Agency, “Kroll Bond Rating Agency Assigns Preliminary Ratings to Avant Loans Funding Trust 2016-B,” April 20, 2016 (online lender extending credit to borrowers with 580 FICO score). See also Earnest company website, <https://www.earnest.com> (online lender extending credit to borrowers without FICO scores).

⁴ U.S. Department of the Treasury, *Opportunities and Challenges in Online Marketplace Lending*, May 10, 2016, at 25.

⁵ *Id* at 1.

Virginia consumers defaulted on these loans.⁶

The consumer abuses in the online lending industry are not new. Indeed, they echo many of the more problematic aspects of the predatory mortgage and payday lending markets. Similarly, predatory lenders have repeatedly sought to evade state usury and other consumer protection laws through the pretext of partnerships with state and national banks, even though such attempts have been rightly disapproved of by courts and regulators alike. In 2002, the Comptroller of the Currency, John D. Hawke, Jr., made the following observations regarding “rent-a-bank” schemes by payday lenders:

We have recently seen several instances in which nonbank lenders who would otherwise have been fully subject to various state regulatory laws have sought to rent out the preemption privileges of a national bank to evade such laws. Indeed, the payday lending industry has expressly promoted such a ‘national bank strategy’ as a way of evading state and local laws. Typically, these arrangements are originated by the payday lender, which attempts to clothe itself with the status of an ‘agent’ of the national bank. Yet the predominant economic interest in the typical arrangement belongs to the payday lender, not the bank.⁷

Soon thereafter, the OCC took a series of enforcement actions that targeted “rent-a-bank” arrangements with national banks.⁸ The FDIC also issued guidance limiting partnerships between payday lenders and FDIC-supervised institutions, and initiated an enforcement action against a rent-a-bank partnership.⁹ Similarly, courts in multiple jurisdictions have rejected attempts by non-bank lenders and debt buyers to take advantage of the regulatory status of national bank partners.¹⁰ We view the Proposed Guidance as a continuation of federal and judicial disapproval of efforts by non-bank lenders to exploit the charters of state and national banks in order to avoid state consumer protection laws.

Finally, we question whether most state-chartered institutions will have the resources to effectively and vigorously monitor their third-party marketplace lending partners. In many instances, state-chartered banks partner with online lending platforms precisely because they lack the institutional reach and technological sophistication to successfully enter the online lending

⁶ *CashCall, Inc. v. Morrissey*, No. 12-1274, 2014 WL 2404300, at *1 (W. Va. May 30, 2014), *cert. denied sub nom. CashCall, Inc. v. Morrissey*, 135 S. Ct. 2050 (2015).

⁷ Remarks by John D. Hawke, Jr. Comptroller of the Currency Before the Women in Housing and Finance Washington, D.C., Feb. 12, 2002, available at <https://occ.gov/static/news-issuances/speeches/2002/pub-speech-2002-10.pdf>

⁸ See <https://occ.gov/topics/consumer-protection/payday-lending/index-payday-lending.html>. See also <http://www.occ.gov/static/news-issuances/news-releases/2003/nr-occ-2003-3.pdf>.

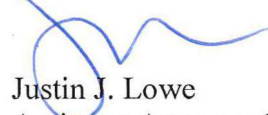
⁹ See https://www.fdic.gov/news/news/press/2008/fbd_notice_of_charges.pdf.

¹⁰ *Madden v. Midland Funding, LLC*, 786 F.3d 246, 253 (2d Cir. 2015); *Commonwealth of Pennsylvania v. Think Fin., Inc.*, No. 14-CV-7139, 2016 WL 183289, at *13 (E.D. Pa. Jan. 14, 2016); *Maryland Com’r of Financial Regulation v. CashCall, Inc.*, 225 Md.App. 313 (2015).

sector. As the Proposed Guidance itself notes, in some cases, “the loan volumes passing through insured institutions exceed by many multiples the bank’s balance sheet.”¹¹ Indeed, in the words of a depository institution that has submitted comments on the Proposed Guidance, small banks simply “don’t have the staff internally to perform the analysis required.”¹² Accordingly, the FDIC should vigorously deploy its supervisory and enforcement resources to discourage problematic “rent-a-bank” and “rent-a-charter” arrangements that insured institutions cannot realistically monitor and police.

Thank you for your consideration and the opportunity to submit this comment.

Sincerely,



Justin J. Lowe
Assistant Attorney General
Consumer Protection Division

¹¹ Proposed Guidance, at 2.

¹² People’s Intermountain Bank Comment, September 23, 2016, at 1.