Global Debt Registry℠

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Via Electronic Mail (thirdpartylending@fdic.gov)

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

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

Global Debt Registry℠ ("GDR"℠) respectfully submits this Comment to the Federal Deposit Insurance Corporation ("FDIC") in response to the FDIC's above-referenced request for comments, released on July 29, 2016, entitled *"Proposed Guidance for Third Party Lending"* (the "Guidance"). GDR is pleased with the FDIC's receptive approach to ensuring that platform lending arrangements assist with the goal of increasing consumer access to credit in a safe and sound banking climate for investors. Our Comment will focus exclusively on how the promise of platform lending can be achieved by implementing infrastructure designed to improve transparency for consumers and investors, and by establishing a registry tracking solution for confirming ownership and servicing rights throughout the lending and securitization process. Our Comment is designed to share our observations of how the online lending markets can avoid some of the problems that have arisen in other markets (e.g. mortgage-backed securities, consumer credit card debt sales) by utilizing a centralized platform for the secure storage and transfer of loan-related information, and by requiring the use of third party validation of loan-related data when loans are securitized and/or sold to institutional investors. We specifically recommend the establishment and use of (1) banking standards that require independent, third party loan validation to prevent fraud and ensure loan enforceability, and (2) a central registry process for titling ownership and servicing rights related to platform loans.

A. *The FDIC Should Establish Guidelines That Require Independent Validation of All Loans Generated on MPL Platforms*

The FDIC identified several potential risks that may arise from the use of third parties, particularly in arrangements common in marketplace lending ("MPL") arrangements. Particularly noteworthy among the risks identified in the Guidance were "transaction risk" (arising from problems with service or product delivery, caused by weak controls, human error or fraud); "pipeline and liquidity risk" (the risk that transactions will not be consummated because the third party responsible for purchasing the loan production cannot perform), and "credit risk" (the risk that any creditor necessary to the third-party relationship does not meet contractual requirements due to a misalignment in incentives). The misalignment in incentives produces the possibility that MPL platforms or associated entities might misrepresent information about the loans or increase credit risk by failing to adhere to established underwriting guidelines.

Among the list of risks already identified as endemic to the misalignment of incentives, we would add these additional risks faced by entities insured by the FDIC:

Reputational Risk: Original creditors also face the risk of adverse publicity if a bank partners with a platform that engages in abusive sales or collection practices. The bank faces similar risks if the platform fails to service the loans properly. This risk is often associated with potential abuse of consumers. But it also extends to the risk that platforms have double sold loans, or have failed to maintain adequate custody of loan documents – servicing failures that ultimately lead to losses for investors.

Litigation Risk: If investors lose money because of platform failure, they will look to the originating bank as a deep pocket to cover their losses. Jilted investors are likely to allege that the bank acted as a joint venture with the platform, and therefore assumed responsibility for inadequate disclosures or other forms of negligence arising in the origination, transfer or servicing of marketplace lending loans.

Risk Retention: In the securitization context, banks face the risk that the Securities and Exchange Commission will regard the bank as the "sponsor" of the securitization because it sold the loans to the platform which in turn sold them to the securitizer with the expectation that the securitization would occur.

The speed and convenience of lending through marketplace lending platforms should be supported with sound risk management guidelines requiring independent validation that: (a) the borrowers actually exist, and (b) that the loans are supported with consistent and accurate data. It is not enough to rely on the representations and warranties of loan originators about the soundness of loan data – independent validation is a practice that will protect consumers and investors, while benefitting loan originators by creating more certainty in this new generation of lending.

We recommend that the FDIC provide guidance that will ensure full transparency between parties in the lending process. Full transparency is best achieved through independent, third party due diligence to validate the accuracy of information associated with each loan included in a pool for securitization or funded through a warehouse lending arrangement. Currently, the marketplace lending industry lacks automated, "real" independent third party complete review and certification for investors to have confidence in the assets that they are purchasing. Investors are unable to compare loan level data reported by the lender against trusted third party sources. This significant gap in the market has prevented more traditional institutional capital sources from entering. In order for the MPL market to complete its evolution from its roots in peer-to-peer lending to attracting "permanent" institutional capital, it needs to ensure that investors have the tools to verify each and every loan they purchase. This is accomplished by use of a third party to interface with the credit bureaus to provide an independent validation that information concerning borrower identity and credit score has been accurately conveyed by an MPL platform to institutional investors acquiring the loans.

A regime of independent validation should have the following attributes:

1. <u>Complete Validation:</u> Every single MPL loan should be validated by a third party by comparing each loan to trusted third party data sources at multiple points in an account's life cycle: a) when a loan is first sold to an investor; b) when a loan is securitized and 3) on an on-going basis for the purpose of account monitoring.

2. <u>True Independence:</u> This service needs to be done by an independent party that has expertise in handling and protecting consumer data and that is not a back-up servicer or other direct servicing vendor. The independent validation provider should have no financial interest in the loan's origination or performance. The validation

service needs to confirm loans by using trusted third party databases that provide loan level borrower identification and credit information.

3. Specificity: Validation should include ensuring a borrower actually exists, that his/her credit profile is consistent with what has been presented by the platform and that funds have been disbursed to the borrower.

4. Collateral Protection: There should also be an independent mechanism to track collateral pledges by platforms. Entities that fall under the FDIC's jurisdiction and that are engaged in warehouse lending, in particular, would benefit from independent assurance that MPL loans have not been double-pledged.

5. On-going Compliance Validation: Independent validation should be on-going even in periods when loans are not being transferred so as to ensure borrowers do not end up on terrorist or money laundering watch lists, or that loans do not exceed state usury laws where applicable.

B. The FDIC Should Establish a Central Registry for Titling MPL Loans

The marketplace lending industry provides an opportunity to merge the ingenuity of FinTech with time-honored safe and sound principles for validating the titling and documentary support of loans in the secondary market. Markets for assets have traditionally been facilitated by the adoption of centralized registries to track the title and supporting documentation associated with the asset. This solution is essential for a new industry offering swift automation of new loans that ideally will travel freely in a marketplace that is both liquid and sound for investors.

Marketplace lending is an extremely efficient alternative to traditional borrowing for consumers and small businesses, and the market is likely to continue its rapid expansion into new and larger market segments. The digital nature of these loan transactions offers significant advantages over traditional, often paper-based, applications in which various documents can become disconnected from the account over time.

For most of the current firms operating in the marketplace, compliance with information requirements necessary to substantiate a debt is simplified by the nature of the loans themselves that are being offered today. For example, most loans are fixed installment loans paid over time, as opposed to revolving loans involving frequent transactions and variable balance levels. Historically, most consumers of MPL loans are prime or "super prime" risk levels and require automatic payment of the balance each month resulting in low delinquency rates and low credit losses. Most firms rely on one or a small number of service agencies. Moreover, the sale of accounts, particularly charged-off accounts, is still relatively limited compared to other types of consumer debt.

But as the market evolves and firms pursue different types of loans and different risk profiles, the ability to ensure compliance will be tested. The credit underwriting models, funding structures and the use of mostly outsourced collection services have not yet experienced challenging market conditions, such as a sharp rise in regional or national unemployment. As seen in other markets, a significant downturn in economic conditions can create challenges for debt owners when account information moves between parties. This has proven to be

true historically when markets have been subject to liquidations and takeovers. In these circumstances, it can be difficult to substantiate a collector's or debt owner's right to collect the debt. Incomplete, untimely or incorrect data can lead to harmful consumer practices in collection of past due accounts. For marketplace firms, the unique ownership and legal structures between investors and servicers create an additional need to ensure that account information remains updated and intact as accounts flow between various parties in the marketplace. Risk strategies need to incorporate plans for legal collection that are consistent with recent federal rulemaking and enforcement actions involving continuity in servicing, and required documentation and recordkeeping.

Fortunately, the digital nature of this marketplace can support processes to ensure long-term transportability of account information. If the market adopts a consistent process to independently validate and track account data and documents for its loans, it can ensure consistent ready-access to the full account profile of both original and new account data and documentation as accounts move between parties. This can be best implemented through an industry-wide process independent of any individual market participant. This process not only protects consumers downstream in the collections process, but also serves as a valuable point of validation for investors seeking independent and ongoing validation of the accounts in a pool of loans.

The FDIC could facilitate both innovation and stability in the online marketplace for lending by mandating or incentivizing the use of an independent centralized registry for tracking lending transactions and storing the account-level data and documents associated with such loans. A similar framework for marketplace lending would help protect investors by ensuring transparency and coherency regardless of how deals are structured.

Conclusion

In sum, we encourage the FDIC to offer guidance directing the use of independent validation of each loan originated and transferred through a marketplace lending platform. We also urge the FDIC to consider how the centralization of account data and documentation associated with marketplace lending for tracking in an industry registry will result in a safer and more robust future for this innovation in consumer lending. Finally, we recommend that the FDIC include these solutions as part of an adequate risk management framework that will satisfy the FDIC when it examines insured institutions. These reforms would improve transparency for investors, reduce costs associated with disputes and litigation, and increase investment and liquidity in the market.

Respectfully submitted,

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