April 14, 2017

Chairman Mike Crapo and Ranking Member Sherrod Brown
United States Senate Committee on Banking, Housing and Urban Affairs
534 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Crapo and Ranking Member Brown:

On behalf of WebBank, thank you for the invitation to share some legislative ideas to promote economic growth. It is our hope that you will find that these proposals will enable consumers, market participants and financial companies to better participate in the economy.

WebBank, a Federal Deposit Insurance Company ("FDIC")-insured, Utah-chartered bank located in Salt Lake City, is a leader in the online lending industry. We use convenient and innovative online platforms to deliver financial products: fair and transparent loans for individuals and small businesses. Our core business involves partnering with non-bank financial companies, financial technology platforms, retailers, and manufacturers to offer revolving and closed-end credit to consumers and small businesses nationwide.

Current federal law provides a good way for offering loans on a nationwide basis. However, the online lending industry is facing unnecessary and unwarranted challenges because some courts have misinterpreted longstanding rules and common understandings. Congress can promote the potential of financial technology by eliminating this uncertainty created by these courts. A legislative fix of *Madden v. Midland*[1] and "True Lender" issues, to confirm the proper application of existing law, would remove the cloud that covers the lending industry. New charters are not necessary. The existing bank model works well.

What follows is a discussion of three targeted legislative proposals–simple, technical fixes that will encourage innovation, spur economic growth, and promote broader financial inclusion.

I. Eliminate the Uncertainty of the *Madden v. Midland* Decision

The United States Court of Appeals for the Second Circuit upended the secondary market for consumer loans – including online lending but also the broader securitization and financing market – by failing even to recognize let alone enforce the longstanding "valid-when-made" rule, which that states a loan that is valid when made cannot become usurious by virtue of a subsequent transaction.[2] Specifically, the court in *Madden* held that the National Bank Act ("NBA") did not preempt a state law

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

[2] *See, e.g., Nicholas v. Fearson*, 32 U.S. 103, 109 (1833); *FDIC v. Lattimore Land Corp.*, 656 F.2d 139, 148-49 (stating that the "non-usurious character of a note should not change when the note changes hands").

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usury claim brought against a non-national bank entity because the national bank was no longer involved with the loan that it had originated.

President Obama's Solicitor General and the Office of the Comptroller of the Currency ("OCC") argued to the U.S. Supreme Court that the Second Circuit wrongly decided the case, explaining that the valid-when-made rule has been a fundamental rule of national banking law for more than 100 years, but the Supreme Court denied certiorari.[3] This means that the Second Circuit's decision remains in effect, even though it incorrectly interpreted federal law, and thus casts into doubt what previously had been a fundamental understanding of the common-law principles that the NBA incorporated upon its enactment in 1863. Because the Second Circuit essentially held that a non-bank purchaser of a loan from a national bank was not entitled to federal preemption, marketplace platforms and loan purchasers are now vulnerable to further legal challenges in the Second Circuit (New York, Connecticut, and Vermont). If other courts decide to follow the *Madden* precedent the impact would be even greater. Already, plaintiffs' lawyers and state regulators are seeking to expand *Madden*.

Specifically, the misguided uncertainty that *Madden* created makes it harder for depository institutions to make loans in partnership with the services of non-bank entities, which in turn impacts loan origination and curtails credit to borrowers in certain states, ultimately slowing economic growth. *Madden* limits access to credit, lender choice, and innovation in a promising growth sector of the financial marketplace.[4]

The Supreme Court is unlikely to hear a dispositive case on the issue until there is a formal split at the Circuit Court level. This could take years. Congress can quickly fix the problem that *Madden* created and eliminate this uncertainty through a straightforward amendment that clarifies that the centuries-old valid-when-made rule continues to be incorporated into federal banking law. We echo the view of both the OCC and the Solicitor General[5] and support legislation to restore the pre-*Madden* status quo in line with Congressional intent and the valid-when-made rule. Attached as Appendix 1 is the "Protecting Consumers' Access to Credit Act of 2017," which explicitly confirms that the interest rate of a loan that is valid when made may be enforced by any third-party assignee to the same extent as the bank itself.

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[3] *See* Brief for the United States as Amicus Curiae, p. 6, *Midland Funding, LLC v. Madden*, No. 15-610, *cert denied* (2016) "The court of appeals' decision is incorrect. Properly understood, a national bank's … authority to charge interest up to the maximum permitted by its home State encompasses the power to convey to an assignee the right to enforce the interest-rate term of the agreement."

[4] *See, e.g., Public Input on Expanding Access to Credit Through Online Marketplace Lending,* Office of the Undersecretary for Domestic Finance, Department of the Treasury, 80 Fed. Reg. 42866 (July 20, 2015).

[5] *See* Brief for the United States as Amicus Curiae, p. 7-8, *Midland Funding, LLC v. Madden*, No. 15-610, *cert denied* (2016) "Under the long established 'valid-when-made' rule, if the interest rate term in a bank's original loan agreement was non-usurious, the loan does not become usurious upon assignment, and so the assignee may lawfully charge interest at the original rate … The power explicitly conferred on national banks by Section 85 [of the NBA]—i.e., the power to originate loans at the maximum interest rate allowed by the national bank's home State—therefore carries with it the power to use the loans once originated for their usual commercial purposes, which include assignment of such loans to others."

II. Maintain Bank "True Lender" Status

Many marketplace lending platforms depend on partnerships with banks to originate loans. Relying on established federal law, these arrangements have been structured in order to use a bank's authority under the existing banking laws to "export" the interest rate permitted in the state where the bank is located. True lender cases seek to recharacterize a bank's partner as the "true lender," and thus to negate protection of the banking laws.[6] However, the plaintiffs in these cases fail to recognize the extensive compliance requirements and regulatory oversight that apply to the loans solely because a bank is involved in the lending process. Recently, federal and state courts evaluating true lender claims have adopted varying standards to determine whether the "true lender" is the bank or the non-bank partner, again incorrectly injecting uncertainty into the market. Some of these decisions look to multi-factor state law tests for the "predominate economic interest" in a loan, but any such test is unworkable for secondary market transactions on which U.S. financial markets depend, because it is wholly unpredictable in outcome.

Similar to the *Madden* discussion above, the consequences of this uncertainty are significant, creating foundational concerns about loan sales, limiting originations, and hindering economic growth. When a court ignores Congressional intent and the originating bank is deemed not to be the true lender, the third party risks losing the exportation rights that the bank has, and could be subject to substantial penalties and fines for violating a state's usury laws.

Here, too, we believe federal law already provides a clear answer to this question. For example, the scope of preemption in Section 27(a) of the Federal Deposit Insurance Act applies not just to banks, but to "any loan" that a bank originates. Notwithstanding this plain language, however, some (though not all) courts persist in applying state law tests to decide if the originating bank is truly the lender. While we are confident that the U.S. Supreme Court will vindicate the plain meaning of federal law, realistically it could take years before this issue reaches the Supreme Court, and the uncertainty and proliferation of litigation in the meantime is damaging to the interests of consumers and marketplace lenders alike. Rather than awaiting an eventual Supreme Court decision, we believe that legislation provides the best opportunity to clear the cloud of true lender uncertainty. Attached as Appendix 2 is another straightforward legislative proposal that would supplement the relevant provisions of the National Bank Act, the Home Owners' Loan Act, the Federal Credit Union Act and the Federal Deposit Insurance Act to confirm that, under federal law, the originating bank is the true lender.

III. Ensure Congressional Leadership Over "Fintech" Regulation

As you know, the OCC is seeking comments until April 14, 2017, on its March 15, 2017 proposal, included in a supplement to its Licensing Manual, to grant limited-purpose national bank

[6] *See, e.g., CashCall v. Morrisey*, 2014 W. Va. LEXIS 587 (2014).

charters to "fintech" companies that engage in the business of banking. A new charter does not help solve the problems of economic growth or financial inclusion that the Committee is trying to address.

Simply, we believe it best to follow the advice of Ranking Member Brown and Sen. Jeff Merkley who have "urge[d] the OCC to refrain from offering any alternative or special purpose charters."[7] Every Republican member of the House Financial Services Committee has also made clear that they "will work with [their] colleagues to ensure that Congress will examine the OCC's actions and, if appropriate, overturn them."[8]

The existing bank model already provides an entry point for fintech companies and other emerging platforms to offer national services. It promotes a superior environment for innovation too. Banks are increasingly working alongside financial technology companies to diversify their revenues, serve a wider array of customers, and potentially lessen the concentration of available credit products at the largest banks.[9] Additionally, this bank model ensures essential consumer protection because these activities by definition fall under the supervision of the FDIC and state regulators. At issue is not whether the OCC has the authority to charter fintech companies, but whether it should. Congress – not unelected, independent regulators – should set the policies that could reshape the financial services industry.

We are concerned that the fintech charter could erode the dual banking system and favor large, established technology companies at the expense of the emerging innovators it ostensibly seeks to assist. Perversely, the fintech charter may indeed have the effect of stifling innovation and consequently harming consumers through the selection of winners and losers in what is now a highly competitive marketplace.

Moreover, this approach is not in line with the regulatory architecture Congress established. Financial technology companies already have a regulator, the FDIC, that has been regulating the "fintech" space for years because of these companies' relationships with banks.[10] The FDIC has sought

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[7] Letter to Comptroller Thomas J. Curry, Sens. Sherrod Brown and Jeffrey A. Merkley (Jan. 9, 2017); *available at* http://brown.senate.gov/download/occ-fintech.

[8] Letter to Comptroller Thomas J. Curry, House Financial Services Committee Chairman Jeb Hensarling, Rep. Randy Hultgren, Vice Chairman Patrick McHenry, et. al (Mar. 10, 2017); *available at* http://s3.amazonaws.com/cdn.orrick.com/files/03102017LetterComptrollerCurry.pdf. Non-Financial Services Committee members Warren Davidson (R-OH) and Thomas MacArthur (R-NJ) also signed the letter.

[9] *See* PwC Global FinTech Report 2017 (April 2017) at 3-4, *available at* http://www.pwc.com/gx/en/industries/financial-services/assets/pwc-global-fintech-report-2017.pdf. "Mainstream financial institutions are rapidly embracing the disruptive nature of fintech and forging partnerships in efforts to sharpen operational efficiency and respond to customer demands for more innovative services… FinTech has evolved from startups that want to take on and beat incumbents, to a broader ecosystem of different businesses looking in many cases for partnerships." PwC's study included a survey of 1,308 financial and technology executives that found "63% of bankers see the rise of FinTech as an opportunity to expand products and services." *Id.* at 11.

[10] *See* "Marketplace Lending," FDIC Supervisory Insights (Winter 2015), available at https://www.fdic.gov/regulations/examinations/supervisory/insights/siwin15/SI_Winter2015.pdf; FDIC Guidance for Managing Third-Party Risk, FIL-44-2008 (June 6, 2008); *available at* https://www.fdic.gov/news/news/financial/2008/fil08044a.pdf

input from the public on proposed additional guidance specifically to "set forth safety and soundness and consumer compliance measures FDIC-supervised institutions should follow when lending through a business relationship with a third party."[11] Thus, the FDIC is active in its role to monitor "lending activities conducted through third party relationships" to ensure that risks are sufficiently monitored and controlled. In doing so, the legislative architecture is preserved with the FDIC fulfilling its statutory mandate in concert with the other financial regulatory agencies.

Conclusion

The current model that encourages banks and non-bank entities to partner to provide innovative credit solutions to consumers and small businesses is thriving. The result of these partnerships is greater financial inclusion through superior, constantly improving products efficiently delivered in ways consumers and small businesses desire. Simultaneously, federal and state regulator involvement ensures these innovations do not come at the expense of high levels of consumer protection. Additionally, the growth of marketplace lending allows smaller banks the opportunity to leverage technological innovation and partnerships with fintech firms to both expand the credit available to consumers and create new sources of revenue, fostering overall economic growth along the way.

Congress has the opportunity to help ensure that this innovation continues and credit remains accessible to qualified borrowers at reasonable costs by eliminating the unwarranted uncertainty courts, through misapplication of existing law, have imposed around these business models and partnerships. The legislative proposals described herein will help remove this uncertainty and preserve the viability of online lending partnerships between banks and technology companies.

Again, thank you for this opportunity to share our views. We look forward to working with you.

Sincerely,

John McNamara
Executive Chairman
WebBank

[11] *See* FDIC Examination Guidance for Third-Party Lending, FIL-50-2016 (July 29, 2016); *available at* https://www.fdic.gov/news/news/financial/2016/fil16050a.pdf. The FDIC extended the comment period until October 27, 2016.

Appendix 1: Proposed Legislation to End *Madden* Uncertainty

To amend the Revised Statutes of the United States, the Home Owners' Loan Act, the Federal Credit Union Act and the Federal Deposit Insurance Act to require the rate of interest on certain loans remain unchanged after transfer of the loan, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE. This Act may be cited as the "Protecting Consumers' Access to Credit Act of 2017".

SEC. 2. RATE OF INTEREST AFTER TRANSFER OF LOAN.

(a) AMENDMENT TO THE REVISED STATUTES.—Section 5197 of the Revised Statutes of the United States (12 U.S.C. 85) is amended by adding at the end the following new sentence: "A loan that is valid when made as to its maximum rate of interest in accordance with this section shall remain valid with respect to such rate regardless of whether the loan is subsequently sold, assigned, or otherwise transferred to a third party, and may be enforced by such third party notwithstanding any state law to the contrary."

(b) AMENDMENT TO THE HOME OWNERS' LOAN ACT.—Section 4(g)(1) of the Home Owners' Loan Act (12 U.S.C. 1463(g)(1)) is amended by adding at the end the following new sentence: "A loan that is valid when made as to its maximum rate of interest in accordance with this section shall remain valid with respect to such rate regardless of whether the loan is subsequently sold, assigned, or otherwise transferred to a third party, and may be enforced by such third party notwithstanding any state law to the contrary."

(c) AMENDMENT TO THE FEDERAL CREDIT UNION ACT.—Section 205(g)(1) of the Federal Credit Union Act (12 U.S.C. 1785(g)(1)) is amended by adding at the end the following new sentence: "A loan that is valid when made as to its maximum rate of interest in accordance with this section shall remain valid with respect to such rate regardless of whether the loan is subsequently sold, assigned, or otherwise transferred to a third party, and may be enforced by such third party notwithstanding any state law to the contrary."

(d) AMENDMENT TO THE FEDERAL DEPOSIT INSURANCE ACT.—Section 27(a) of the Federal Deposit Insurance Act (12 U.S.C. 1831d(a)) is amended by adding at the end the following new sentence: "A loan that is valid when made as to its maximum rate of interest in accordance with this section shall remain valid with respect to such rate regardless of whether the loan is subsequently sold, assigned, or otherwise transferred to a third party, and may be enforced by such third party notwithstanding any state law to the contrary."

Appendix 2: Proposed Language for True Creditor Fix

To amend the Revised Statutes of the United States, the Home Owners' Loan Act, the Federal Credit Union Act and the Federal Deposit Insurance Act to determine the applicable interest rate for loans originated by national banks, federal savings associations, and insured state banks, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE. This Act may be cited as the "_____________ Act of 2017".

SEC. 2. RATE OF INTEREST APPLICABLE TO LOAN.

(a) AMENDMENT TO THE REVISED STATUTES.—Section 5197 of the Revised Statutes of the United States (12 U.S.C. 85) is amended by adding at the end the following new sentence: "A loan shall be conclusively presumed a loan made by an association for purposes of this section if both (a) the loan is made in the name of that association and (b) the loan is funded by that association, irrespective of any other circumstances including whether any other person provides any services in connection with such loan or purchases such loan after it is made.".

(b) AMENDMENT TO THE HOME OWNERS' LOAN ACT.—Section 4(g)(1) of the Home Owners' Loan Act (12 U.S.C. 1463(g)(1)) is amended by adding at the end the following new sentence: "A loan shall be conclusively presumed a loan made by a savings association for purposes of this section if both (i) the loan is made in the name of that savings association and (ii) the loan is funded by that savings association, irrespective of any other circumstances including whether any other person provides any services in connection with such loan or purchases such loan after it is made.".

(c) AMENDMENT TO THE FEDERAL CREDIT UNION ACT.—Section 205(g)(1) of the Federal Credit Union Act (12 U.S.C. 1785(g)(1)) is amended by adding at the end the following new sentence: "A loan shall be conclusively presumed a loan made by an insured credit union for purposes of this section if both (i) the loan is made in the name of that insured credit union and (ii) the loan is funded by that insured credit union, irrespective of any other circumstances including whether any other person provides any services in connection with such loan or purchases such loan after it is made.".

(d) AMENDMENT TO THE FEDERAL DEPOSIT INSURANCE ACT.—Section 27(a) of the Federal Deposit Insurance Act (12 U.S.C. 1831d(a)) is amended by adding at the end the following new sentence: "A loan shall be conclusively presumed a loan made by a State bank or insured branch of a foreign bank for purposes of this section if both (1) the loan is made in the name of that State bank or insured branch of a foreign bank and (2) the loan is funded by that State bank or insured branch of a foreign bank, irrespective of any other circumstances including whether any other person provides any services in connection with such loan or purchases such loan after it is made.".