



May 11, 2016

TREASURY ISSUES WHITE PAPER ON ONLINE MARKETPLACE LENDING

On May 10, 2016, the United States Department of the Treasury issued a white paper that provides (i) an overview of the online marketplace lending industry, (ii) a summary of the responses that the Treasury received to its 2015 Request for Information on the industry (RFI), (iii) policy recommendations for private sector participants and the federal government and (iv) identification of trends that the Treasury believes require ongoing observation. The Treasury defines "online marketplace lending" as the segment of the financial services industry that uses investment capital and data-driven online platforms to lend either directly or indirectly to consumers and small businesses. According to the Treasury, online marketplace lenders share certain key characteristics. Most notably, they (i) provide faster access to credit than traditional lenders, (ii) often offer small loans with short-term maturities that may be collected on a daily basis from linked bank accounts, (iii) use automated online loan applications without retail branches, (iv) rely on a variety of funding sources and (v) use electronic data sources and technology-driven underwriting models to automate processes. While the Treasury recognizes that online marketplace lenders are subject to many of the same federal laws that apply to traditional lenders, the Treasury expressed a concern that certain federal consumer protection laws apply only to consumer loans and not small business loans. However, in expressing this concern, the Treasury did not acknowledge the potential for adverse effects on the costs and availability of credit in extending consumer protection laws to small business lending as recognized by the Board of Governors of the Federal Reserve System in its report to Congress in accordance with Section 506 of the Credit Card Accountability Responsibility and Disclosure Act of 2009 (Credit CARD Act).

Based on the Treasury's market research and the responses that it received to the RFI, the Treasury has provided the following recommendations with the stated purpose of fostering safe and affordable access to credit for consumers and businesses:

- **Support More Robust Small Business Borrower Protections and Effective Oversight.** The Treasury is recommending subjecting small business lenders to increased oversight that is similar to that imposed on depository institutions to foster greater transparency and better outcomes for borrowers.

Because the Treasury believes that small business loans under \$100,000 share common characteristics with consumer loans, the Treasury also is recommending that small business loans be subject to the same consumer protections. The Treasury stated that it is willing to work with members of Congress to consider legislation that addresses both oversight and borrower protections. The Treasury specifically pointed to the Responsible Business Lending Coalition's Small Business Borrowers' Bill of Rights as evidence that future legislation can be enacted without adding undue burden or cost to the industry. See our ALERT dated Sept. 16, 2015 for more information on the creation of the Small Business Borrowers' Bill of Rights.

- **Ensure Sound Borrower Experience and Back-End Operations.** The Treasury is recommending that the industry adopt standards that are designed to provide a sound borrower experience from consumer acquisition through collections in the event of delinquency or default.
- **Promote a Transparent Marketplace for Investors and Borrowers.** For a well-functioning capital market to develop, the Treasury is recommending that the industry adopt (i) standardized representations, warranties and enforcement mechanisms, (ii) consistent reporting standards for loan origination data and ongoing portfolio performance, (iii) loan securitization performance transparency and (iv) consistent market-driven pricing methodology standards. To improve transparency for investors and borrowers, the Treasury also is recommending the creation of a private sector-driven public registry for tracking data on transactions.
- **Expand Access to Credit Through Partnerships that Ensure Safe and Affordable Credit.** Because the Treasury's data shows that online marketplace lenders may primarily be serving prime and near-prime consumer and small business borrowers, the Treasury believes that more must be done to serve borrowers who are creditworthy but may not be scoreable under traditional credit scoring models. The Treasury is recommending that online marketplace lenders work with Community Development Financial Institutions to better serve so-called "no-file" or "thin file" consumers or small businesses with less than three years of operations.

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- **Support the Expansion of Safe and Affordable Credit Through Access to Government Held Data.** The Treasury is recommending that online marketplace lenders use “smart disclosures” that will enable third-party companies and nonprofits to create shopping sites that consumers could use to compare loan terms, similar to travel and flight comparison shopping sites today. The Treasury is recommending that the Consumer Financial Protection Bureau (CFPB) and the Federal Trade Commission (FTC) include the use of smart disclosure in its guidance and standards on consumer disclosures. In addition, the Treasury is recommending the exploration of opportunities that would allow borrowers to voluntarily share government data that lenders can use to verify their ability to repay loans.
- **Facilitate Interagency Coordination through the Creation of a Standing Working Group for Online Marketplace Lending.** The Treasury is recommending the formation of an interagency working group that would enable member agencies to coordinate efforts to identify areas where additional regulatory “clarity” could protect borrowers and investors and expand access to credit. The proposed working group would include the Treasury, CFPB, Federal Deposit Insurance Corporation, Federal Reserve Board, FTC, Office of the Comptroller of the Currency, Small Business Administration, Securities and Exchange Commission and a representative of a state bank supervisor.

In addition to the above recommendations, the Treasury identified a number of potential trends that the Treasury believes require ongoing monitoring, including (i) the evolution of credit scoring, (ii) the impact of changing interest rates, (iii) potential liquidity risk, (iv) increasing mortgage and auto loans originated by online marketplace lenders, (v) potential cybersecurity threats and (vi) compliance with anti-money laundering requirements.

A number of others are examining the need for or otherwise promoting increased regulations for online marketplace lenders including small business lenders. For example, (i) three United States senators sent a letter to the Government Accountability Office questioning the role of the federal government in regulating small business lending and suggesting that there is a need to extend consumer protection laws to the online lending space, (ii) three New York legislative committees held a hearing on small business lending practices during which presenters urged lawmakers to enact laws providing for borrower education and uniform disclosures regarding the cost of credit, including annual percentage rates, (iii) a proposed amendment to Illinois Senate Bill 2865 would establish the Illinois Small Business Lending Act which would subject small business lenders to licensing and other onerous requirements and restrictions and establish stiff penalties for violations, (iv) the FTC will host a forum this June 9th to examine the range of marketplace lending models, their potential benefits to consumers, possible consumer protection concerns and the applicability of consumer protection laws to market participants and (v) the California Department of Business Oversight released summary findings from its 2015 survey of online consumer and small business financing companies and has stated that it has sent participating companies follow-up requests for additional documents and information. See our ALERT dated April 15, 2016 for more information.

The online marketplace lending industry is represented by various groups that are taking steps to respond to the Treasury’s white paper and counter any legislative and regulatory initiatives that may be unnecessary and disadvantageous to the industry. We are monitoring developments. □

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