OPPORTUNITY FINANCE NETWORK™

January 15, 2017

The Honorable Thomas J. Curry
Comptroller of the Currency
Office of the Comptroller of the Currency
400 7th St SW #3E-218
Washington, DC 20219

Re: Special Purpose National Bank Charters to Financial Technology Companies

Dear Comptroller Curry:

Opportunity Finance Network (OFN) appreciates the opportunity to comment on the "Exploring Special Purpose National Bank Charters for Fintech Companies" white paper.

OFN is a national network of community development financial institutions (CDFIs) investing in opportunities that benefit low-income, low-wealth, and other under-resourced communities across America. OFN Members are performance-oriented, responsible investors that finance community businesses, sparking job growth in the areas that need it most, and delivering both sound financial returns and real changes for people and communities.

Our network has originated more than $48 billion in financing in urban, rural, and Native communities through 2015. With cumulative net charge-off rates of less than 1 percent, we have demonstrated our ability to lend prudently and productively in unconventional markets often overlooked by conventional financial institutions.

Underserved Communities Lack Access to Credit

Although lending conditions have been relatively stable for the past several years, credit standards have remained tight since the Great Recession. Less credit-worthy borrowers – like those in communities disproportionately affected by the financial crisis -- face significant challenges to accessing capital. This reality is having an adverse impact on the economically underserved people and regions that CDFIs serve, including people of color, immigrants, and residents of rural and tribal areas.

The emergence of online lending has produced a seismic shift in the delivery of financial services to consumers. As traditional brick and mortar institutions continue to retract and reduce their numbers, the world of online lending is experiencing massive growth**.** The FDIC's Survey of Unbanked and Underbanked Households found that:

> "The use of online and mobile banking to access accounts increased substantially from 2013 to 2015, while use of bank tellers decreased …The proportion of banked households that used online banking to access their accounts in the past 12 months increased from 55.1 percent in 2013 to 60.4 percent in 2015 … The proportion of households that used a bank

teller to access their accounts in the past 12 months fell from 78.8 percent in 2013 to 75.5 in 2015" [1]

However, this emergence of online lending presents challenges and opportunities. For many consumers, access to financial services is now available right from their mobile phones. And, while there is a clear need for lending innovations providing open access to capital for underserved communities, we still need to provide safeguards for these same consumers. As this space of open access through fintech has developed, so too has the proliferation of potentially predatory financial products and practices that take advantage of borrowers.

OFN agrees with the OCC that applying a bank regulatory framework to fintech companies may help ensure that these alternative lending companies operate in a safe and fiscally responsible manner to effectively serve the needs of customers, businesses, and communities without allowing any lending practices that may have a destabilizing impact on residents. The chartering of fintech companies could increase access to capital especially for communities left out of the traditional banking system as long as there are strong borrower protections in place, financial inclusion investments are required, and fintech companies share data about their lending, asset quality, and portfolio performance.

CDFIs engaged in fintech also see potential in this proposal to scale their work to a national level and increase loan volume while providing access to affordable responsible credit. However, greater clarity and additional information is needed about the details of the chartering requirements in order to fully assess its impact.

The OCC must carefully consider the implications of issuing this charter to nondepository companies. A national bank charter obtained from a federal regulatory agency conveys a level of safety and security to consumers, and the OCC must take steps to ensure that only responsible actors providing access to affordable financial products and services are able to access the benefits of the charter. We urge caution in issuing special purpose bank charters to marketplace lenders, particularly without safeguards and/or requirements related to transparency of lending terms.

OFN's responses to the questions in the proposal are focused on financial technology companies providing consumer and small business loans.

1. What are the public policy benefits of approving fintech companies to operate under a national bank charter? What are the risks?

There are several public policy benefits to approving fintech companies to operate under a national special purpose bank charter:

- **Increased access to capital -** The closures of thousands of bank branches has practical implications on the provisions of financial services in certain

[1] Federal Deposit Insurance Corporation, "2015 National Survey of Unbanked and Underbanked Households", October 2016. Accessed January 10, 2017. https://www.fdic.gov/householdsurvey/2015/2015report.pdf.

communities. U.S. banks closed 4,821 branches between 2009 and 2014, reducing the total number of branches by about 5 percent.[2] This decrease in bank lending has created banking deserts, especially in low-income communities, rural communities, and communities of color. The Federal Reserve Bank of New York found that people in low-income census tracts are more than twice as likely to live in a banking desert than their counterparts in higher income tracts.[3] As branches close, access to banking services as well as credit and loans is diminished for the areas served by the branches.

Even as traditional lenders retreat, there is still a need for access to financial services in underserved communities. To an extent, marketplace lenders are filling the gap and providing access to capital for people with limited access to traditional financial services. However, not enough is known about their business models, underwriting methods, and portfolio quality. Additional oversight and transparency in the market could boost confidence in the overall marketplace lending market.

- **Transparency -** The supervision of the OCC presents an opportunity to regulate a market that currently has limited oversight and bring more transparency into the online lending market. The current lack of regulation in the market and transparency about loan pricing and terms limits the ability of consumers to make informed decisions. The OCC's position as a regulator provides an opportunity to collect and analyze data on the market that is currently unavailable to the public, and provide more insight into the portfolio and asset quality of marketplace lenders.

- **Adequate consumer protection –** Limited regulation and oversight in the marketplace lending market has allowed some harmful and predatory practices to flourish, with a particular negative impact on low income individuals and communities. OFN's recent paper, CDFI Futures, found "…practitioners thought that the line between predatory and non-predatory practices for a number of Fintech lenders was thin, based on their pricing models and business practices (marketing). Small businesses certainly report that many online lenders offer loans at higher costs than common factoring credit."[4] In addition, the Federal Reserve's Small Business Credit Survey shows most online applicants, even when funded, reported relatively low satisfaction levels with their experience. When asked why, 85 percent cited the interest rate and two-thirds (66 percent) unfavorable repayment terms, indicating many borrowers may not fully understand the cost of credit

[2] Donald Morgan, Maxim Pinkovskiy, and Bryan Yang, "Banking Deserts, Branch Closings, and Soft Information", Liberty Street Economics, Federal Reserve Bank of New York, March 2016.
[3] Ibid.
[4] Jeremy Nowak, "CDFI Futures: An Industry at a Crossroads", Opportunity Finance Network, March 2016, Accessed January 6, 2017.
http://ofn.org/sites/default/files/resources/PDFs/Publications/NowakPaper_FINAL.pdf.

products they are considering.[5] Oversight from the OCC could provide borrowers with an additional level of consumer protection.

- **Financial Inclusion Requirements –** The OCC has the authority to ensure fintech companies must remain accountable to the communities in which they lend by imposing a regulatory requirement for non-depository fintech companies similar to Community Reinvestment Act (CRA) for FDIC-insured institutions. OFN urges the OCC to hold fintech companies seeking a charter to a high standard to demonstrate that commitment to financial inclusion. Accessing affordable credit is still a challenge for millions of Americans. The OCC should use its supervision authority to compel fintech companies to define and implement strategies that meet the credit needs of low- and moderate-income communities as condition of receiving the charter.

While marketplace lending has the potential to stimulate the flow of capital into communities, especially those underserved by traditional financial institutions, OFN is concerned that there are potential risks in some of the business models employed by fintech models that the OCC should consider when assessing any application for a special purpose bank charter:

- **Untested Models** - Many of the technology platforms and algorithm-based lending models used by fintech companies to underwrite loans and assess risk are new and untested business models. Most fintech companies sprang into existence in the aftermath of the Great Recession, meaning most of their loan portfolios have yet to experience a market correction that could impact repayment, delinquency, and losses. Online marketplace lenders offer more and ever changing financial products with minimal oversight from regulators, no requirements related to clarity and transparency of loan terms, and no safeguards for vulnerable borrowers. OFN Member and Minneapolis-based CDFI Community Reinvestment Fund noted in their response to the U.S. Department of Treasury's Request for Information on Online Marketplace Lending, "Once the marketplace lending portfolios in the process of being assembled today experience a recession, it will be clear as to whether these new streams of data, investments in big data, data mining and predictive analytics added value to the overall lending risk and default equation. The alternative would be the realization that risk and default are simply functions

[5] Cleveland Federal Reserve Bank, "New Insights on Online Lender Applicants from the Small Business Credit Survey", October 2016. Accessed January 5, 2017. https://www.clevelandfed.org/en/newsroom-and-events/ publications/special-reports/sr-20161012-click-submit.aspx

of the overall economy's performance, which current tools, such as FICO, adequately address today."[6]

- **Rapidly changing external environment –** Advancements in technology have created a fast paced world in which business models and underwriting algorithms can be adjusted quickly, but the ability of government to respond to these changes is far more limited. Further, the diversity of the business models of fintech companies require examiners must also be able to understand these new models in order to effectively assess and regulate these companies. The OCC must take measures to ensure staff remain trained and up to date on any emerging trends and new business models in the fintech space. OFN is also concerned about the continued availability of resources at the OCC to ensure compliance and enforcement of regulation. Related to the risk associated with understanding a diverse set of fintech business models is that technology moves fast, but often government does not. The OCC must be prepared to respond to the rapid industry-level changes that are happening in the fintech space in a timely matter.

- **National preemption of state anti-predatory lending laws –** The special purpose bank charter proposal indicates that some state laws will be pre-empted, as well as the ability of state regulators to issue licenses for fintech companies to engage in certain activities and the ability to conduct examinations of those companies operating within their jurisdiction. This is of major concerns to the responsible lending community. An OCC charter could significantly diminish the enforcement capabilities of state regulators, many of whom have developed robust regulatory infrastructure and enforcement mechanisms to effectively curb payday and predatory lending. The OCC needs to clearly define how the charter would interact with state lending laws, how pre-emption would work in practice, and confer with state regulators to ensure this charter does not undermine the protections of consumers and business owners in states with strong anti-predatory lending laws.

- **Voluntary nature of the charter -** OFN is also concerned that the voluntary nature of the special purpose charter will create a competitive advantage for those fintech companies with enough scale and capacity to seek the charter – those that choose not to seek the charter will still be able to operate business as usual without regulatory oversight, leaving a hole in consumer protection.

[6] Community Reinvestment Fund, Response to Treasury Department Marketplace Lending Request for Information, September 30, 2015. http://www.lendacademy.com/responses-from-the-treasury-rfi-on-marketplace-lending/

2. What elements should the OCC consider in establishing the capital and liquidity requirements for an uninsured special purpose national bank that limits the type of assets it holds?

The OCC must take steps to ensure that fintech companies are properly capitalized based on the risk in their portfolio. The diversity of business models among fintech companies means a one-sized fits all approach will not work. Capital and liquidity requirements should be flexible enough to adjust to the risk of each individual applicant's portfolio.

As mentioned in our response to Question 1, the OCC should also consider whether these untested business models present an additional, unforeseen risk to the banking system. Most fintech companies were created after the Great Recession, meaning many companies have yet to experience an economic downturn that may put a strain their portfolios or result in delinquencies and charge-offs.

CDFIs, as responsible lenders, have weathered economic downturns with strong balance sheets and minimal losses because they employ sound and prudent lending practices, policies and procedures. CDFIs ensure their lending products are structured to adequately meet the needs of their borrowers and provide development services to ensure their clients understand their loan terms, repayments, fees, and possess the financial and credit skills to manage their finances. These time-tested methods of lending capital have proven to be a business model that works, allowing CDFIs to lend with confidence and experience charge-off rates comparable to those of FDIC-insured institutions.[7]

However, when it comes to online lending, information about the lending practices of marketplace lenders is not widely available, making it difficult to determine the actual risk in their underwriting and lending practices. Some fintech companies make lending decisions based purely on data rather than more traditional underwriting, and it remains to be seen if this type of lending will prove to be a viable business model. Once marketplace lending portfolios experience a recession, it will provide more clarity about the efficacy of these new business models. Until that happens, the OCC should require charter applicants to take additional risk management measures and hold additional capital and liquidity reserves in order more is known about the performance of these loans.

3. What information should a special purpose national bank provide to the OCC to demonstrate its commitment to financial inclusion to individuals, businesses and communities? For instance, what new or alternative means (e.g., products, services) might a special purpose national bank establish in

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[7] Opportunity Finance Network, "Opportunity Finance Institutions: Side by Side, Fiscal Year 2015 Eighteenth Edition," October 2016. http://ofn.org/publications.

furtherance of its support for financial inclusion? How could an uninsured special purpose bank that uses innovative methods to develop or deliver financial products or services in a virtual or physical community demonstrate its commitment to financial inclusion?

Responsible financial technology can stimulate financial inclusion for the unbanked and underbanked, especially in immigrant communities, rural communities, and communities of color, all of which have much higher rates of being underbanked than their White counterparts. Less than half of Black and Hispanic households are fully banked, compared to more than 75 percent of White households. Black and Hispanic households are also far more likely than White households to turn to alternative financial services, even when they do own a bank account.[8] As the OCC noted in its paper on Supporting Responsible Innovation in the Federal Banking System, "Technology, for example, can promote financial inclusion by expanding services to the underserved. It can provide more control and better tools for families."[9]

However, consumers, particularly those seeking to borrow capital from marketplace lenders, are often operating without pertinent information about loan terms and pricing, leaving them vulnerable to predatory lenders. The OCC could close the information gap by compelling charter applicants to adopt strong financial inclusion practices, including reining in predatory lending practices, increasing access to safe and affordable financial services and products, expanding financial education, encouraging saving, and implementing policies to improve credit and manage debt.[10]

Specifically, fintech companies seeking the charter should have to demonstrate that they:

- have transparent pricing and terms;
- are non-abusive;
- employ responsible underwriting practices;
- encourage fair treatment from brokers;
- facilitate inclusive credit access; and
- engage in fair debt collection processes.

CDFIs in our network also expressed concern that in spite of the growth of marketplace lending, many low- and moderate-income communities remain underserved, and those that do receive loans from online lenders can become

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[8] Corporation for Enterprise Development, "Unaccounted: The Millions of Americans without Bank Accounts", November 2016. http://cfed.org/assets/pdfs/unaccounted_americans_fact_file.pdf.
[9] Office of the Comptroller of the Currency, "Supporting Responsible Innovation in the Federal Banking System: An OCC Perspective", March 2016. https://www.occ.gov/publications/publications-by-type/other-publications-reports/pub-responsible-innovation-banking-system-occ-perspective.pdf
[10] Corporation for Enterprise Development, "Financial Inclusion Policy Action Initiative 2014 Request for Proposal", http://cfed.org/assets/pdfs/NWAF_Policy_Action_RFP.pdf.

trapped in cycle of struggling to repay predatory debts. Often, CDFIs in our network are left to refinance high-cost loans individuals and business owners received from online lenders to relieve them from unsustainable debt burdens. However, there is a lack of information about the business practices of some of these online lenders, making it difficult to assess the impact it is actually having on communities.

In order to close this information gap, fintech applicants for the charter should also be required to disclose their business profile, marketing strategies, and the geographic distribution of their loans to help determine if online lenders are actually providing increased access to capital in low and moderate income communities or simply creating more unsustainable debt. The disclosure of this information will give regulators and the public greater understanding of where these marketplace loans are going, and help identify any gaps in coverage.

4. Should the OCC seek a financial inclusion commitment from an uninsured special purpose national bank that would not engage in lending, and if so, how could such a bank demonstrate a commitment to financial inclusion?

Under the CRA, insured depository institutions have an affirmative obligation to serve the credit needs of low- and moderate-income communities and provide equal access to responsible financial products and services to underserved individuals and communities. However, many fintech companies are non-depository institutions that will not be subject to CRA statutory and regulatory requirements.

Absent any CRA obligation like those of insured depository institutions, the OCC should take steps to ensure that the fintech company is increasing access to affordable, responsible financial products and services. Non-depository fintech banks should still have some affirmative obligation to make credit available in low- and moderate-income communities even without a statutory requirement. The OCC will need to develop new tools and mechanisms for fintech companies to demonstrate their commitment to financial inclusion, as traditional CRA assessment requirements based on physical bank branch and ATM locations will not work for fintech companies. The Federal Reserve Board of Governors Community Advisory Council recently acknowledged the shortcomings of the current system, stating "the prevalence of credit card usage and increases in online banking challenges the convention that geographic targeting of the CRA should be driven only by physical branches."[11]

Requiring fintech companies to demonstrate their lending practices are fair and inclusive, coupled with information about loan pricing and other disclosures, are

[11] Community Advisory Council and the Board of Governors "Record of Meeting: Friday, November 20, 2015". Accessed January 13, 2017. https://www.federalreserve.gov/aboutthefed/cac-20151120.pdf.

ways that applicants can demonstrate their commitment to financial inclusion. Applicants could also demonstrate this commitment by funding credit building and credit counseling services and supporting the development of other asset building tools.

Since CDFIs are mission-driven lenders that provide access to affordable, responsible credit, fintech companies seeking a special purpose bank charter should also be able to demonstrate their commitment to financial inclusion through partnerships with and investments in CDFIs, similar to FDIC-insured institutions.[12]

5. How could a special purpose national bank that is not engaged in providing banking services to the public support financial inclusion?

As in question 4, even if the applicant for the special purpose bank charter is not engaged in providing banking services to the public, they should still be required to support financial inclusions. Fintech companies seeking a charter should be able to demonstrate their commitment to financial inclusions through partnerships with and investments in CDFIs, similar to insured institutions seeking CRA credit. In addition, financial inclusion could be supported by funding credit building and credit counseling services in low- and moderate-income communities; providing training and technical assistance to small business borrowers; or engaging in other activities that help build assets and create wealth for low-income people and communities.

6. Should the OCC use its chartering authority as an opportunity to address the gaps in protections afforded individuals versus small business borrowers, and if so, how?

The OCC should use its authority to address the gaps in consumer protection for small business borrowers. OFN Member's experience and a significant body of research indicate that small businesses, particularly minority-owned and women-owned businesses and those businesses serving communities of color, do not have the same access to credit as other small businesses. The Small Business Administration's research shows minority business owners are disproportionately denied financing even when controlling for factors such as business credit scores and personal wealth.[13] The Minority Business Development Agency's research finds that

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[12] Federal Deposit Insurance Corporation, "Strategies for Community Banks to Develop Partnerships with Community Development Financial Institutions", March 2014. Accessed January 5, 2017. Https://www.fdic.gov/consumers/community/cdfi/cdfis_entirereport.pdf
[13] Christine Kymn, "Access to Capital for Women- and Minority-owned Businesses: Revisiting Key Variables By Advocacy", Issue Brief 3: Access to Capital, Small Business Administration, Office of Advocacy January 2014. Accessed January 11, 2017. https://www.sba.gov/sites/default/files/Issue%20Brief%203%20Access%20to%20Capital.pdf.

minority business owners are denied loans at nearly three times the rate of non-minority owners.[14]

This disparity in access to capital has allowed online marketplace lenders to flourish. The 2015 Federal Reserve Small Business Credit Survey found that the smallest firms (revenues less than $25K) were nearly twice as likely to apply with an online lender as non-employers with $100K in annual revenue. Application rates to online lenders were 19 percent, and 37 percent, respectively.[15] The study also found that minority-owned firms comprise a larger share of the online applicant pool (36 percent) than of the traditional-source applicants (14 percent).[16]

As online lending to small businesses grows, regulations to prevent lenders from engaging in predatory behavior are essentially nonexistent. While the Consumer Financial Protection Bureau and some state governments have made great strides in developing rules to regulate payday and predatory lending to individuals, currently no such protections exist in marketplace lending to small business. When it comes to historically underserved communities and small business lending, a "Wild West" environment has emerged. The OCC's supervision will bring much needed oversight to the online small business lending sector. The OCC should also use its supervision authority to collect data from fintech companies about lending to minority owned businesses, and determine if lack of access to capital drives small business owners to seek financing for their businesses through predatory consumer products that are riddled with fees and predatory terms.

7. What are potential challenges in executing or adapting a fintech business model to meet regulatory expectations, and what specific conditions governing the activities of special purpose national banks should the OCC consider?

OFN urges the OCC to take more time to understand and dissect fintech business models, underwriting procedures, before issuing any special purpose charters. The risks to consumer protection is too great, especially for consumers and business owners whose financial security is already tenuous. Well trained staff, understanding of technology, availability of resources to ensure enforcement and compliance with

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[14] Robert W. Fairlie, Ph. D. and Alicia M. Robb, Ph.D, "Disparities in Capital Access between Minority and Non-Minority-Owned Businesses: The Troubling Reality of Capital Limitations Faced by MBEs", U.S. Department of Commerce, Minority Business Development Agency, January 2010. Accessed January 11, 2017. http://www.mbda.gov/sites/default/files/DisparitiesinCapitalAccessReport.pdf.
[15] Federal Reserve Banks Of New York, Atlanta, Boston, Cleveland, Philadelphia, Richmond, St. Louis, "2015 Small Business Credit Survey Report on Nonemployer Firms, December 2016. , https://www.clevelandfed.org/en/community-development/small-business/about-the-joint-small-business-credit-survey/2015-joint-small-business-credit-survey.aspx.
[16] Id at 5.

regulations are all necessary to ensure the OCC is able to provide the much needed oversight of this growing market.

As mentioned in the response to Question 1, the potential for national preemption of state anti-predatory lending laws is of major concern. OFN would like to ensure that this special charter is not used as a way to circumvent state laws limiting fees and interest rates for certain types of loans. We urge the OCC to proceed with caution The OCC should not move forward with issuing charters before closely examining the implications on the current regulatory landscape. The OCC must look for ways to ensure fintech banks seeking the charter are not engaging in predatory lending practices in violation of existing state laws. Finally, the OCC must diligently assess the permissibility of granting nondepository companies a special purpose charter.

OFN applauds the forward thinking of the OCC and the efforts to bring order, fairness, and stability to online marketplace lending. We appreciate the opportunity to comment on this regulatory proposal. We look forward to continuing to work with the OCC to expand access to affordable, responsible credit. OFN appreciates your consideration of our comments. If you have any questions, please feel free to contact me at dwilliams@ofn.org or 215.320.4318.

Thank you,

Dafina Williams

Dafina Williams
Vice President, Public Policy

cc: Liz Lopez, Executive Vice President, Public Policy
Nancy Santiago Negron, Chief External Affairs Officer