2021 POLICY PRIORITIES

> "I believe the United States must be a leader in the digital asset and financial technology areas."
>
> Janet Yellen, U.S. Secretary of the Department of Treasury[1]

INTRODUCTION

The Online Lenders Alliance's (OLA) core mission is to promote a diverse and responsible marketplace for innovative online financial products and services while expanding access to credit for all consumers—including those who are financially underserved. We represent distinctly innovative financial technology companies committed to the highest standards of conduct and dedicated to ensuring the best possible customer experience. OLA members must be compliant with all applicable federal and state laws; abide by a robust set of Best Practices; and adhere to a stringent Code of Conduct to ensure customers are fully informed and fairly treated.

The products and services that our members offer empower consumers to access non-collateralized, shorter-term, smaller-dollar financial products with competitive, market-leading fees and rates. Many of these consumers do not have access to the credit products they need from other financial institutions, for reasons including a) they have lower credit scores with credit histories that are often sparse or nonexistent; b) financial products at the smaller loan amounts they want do not exist within the mainstream banking system and/or they do not want to risk their assets (such as their home or automobile) as collateral; or c) they choose the convenience and speed at which fintech companies can make lending decisions, underwrite the loan, and transfer funds—even when other options are available. Furthermore, many consumers who use these products report improved credit and better overall financial health.

Innovation and competition are giving consumers more products and more choices to meet their credit needs. OLA strives to provide consumers with the products they want and need safely and responsibly. Our members continue to work with policymakers to strike a balance between consumer protection and preserving credit access for the millions of Americans who routinely turn to online lending to address their financial needs.

OLA will continue to serve as an information resource to federal and state policymakers on issues related to credit access and financial technology. We will continue to educate consumers about online lending and play an active role in policing the industry through our consumer hotline, our portal to report fraud, and our aggressive efforts to catch and root out fraudsters.

This document includes OLA's main policy priorities for consideration by the Biden Administration and members of Congress. We look forward to continuing our work and collaboration with policymakers and opinion leaders to serve consumers' best interests.

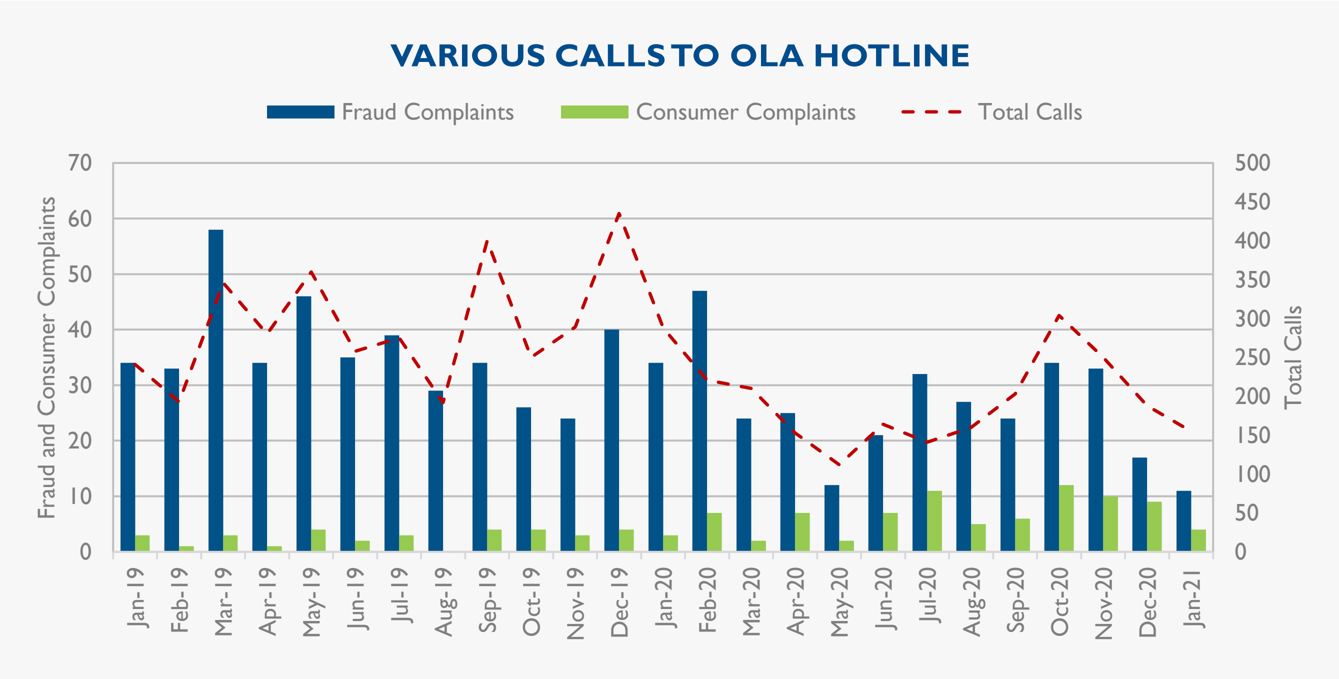
OLA BACKGROUND

OLA members encompass a growing variety of businesses providing credit to a wide array of consumers, including the 100 million nonprime consumers who are unable to obtain the assistance they need from mainstream financial institutions. According to the FDIC, approximately one in five Americans utilize alternative financial services (AFS) every year.[2] Installment lending, specifically online lending, is one of the fastest growing sectors in the AFS space because it provides consumers greater flexibility of loan duration, often combined with smaller, more manageable payments.[3] Unlike payday loans, these installment loans are amortized, leading to a structured decline in loan principal following each payment.

Consumer protection separates OLA members from others in the online lending space. As a trade association, OLA has developed a dynamic series of Best Practices and a Code of Conduct that helps govern its members and influence the industry. We work tirelessly to ensure consumers are protected and better understand the credit products available to them. Only lenders who comply with OLA's strict standards may display the OLA seal, which means consumers can trust the company they work with, that the company is committed to the highest standards of conduct, and that it is dedicated to ensuring the best possible experience for its customers.

Moreover, OLA operates a sophisticated policing effort, consisting of a Consumer Hotline and web crawling service that scours the Internet for a long list of banned marketing terms to root out those looking to commit fraud or mislead consumers.

The Consumer Hotline allows consumers to speak with a live operator if they have any outstanding issues they are not able to resolve with a lender in the marketplace. That operator can report this activity and help the consumer navigate the online lending market. Cases of suspected fraud are forwarded to the Federal Trade Commission (FTC). OLA's hotline receives hundreds of calls each month and served as an especially important resource during the COVID-19 pandemic.

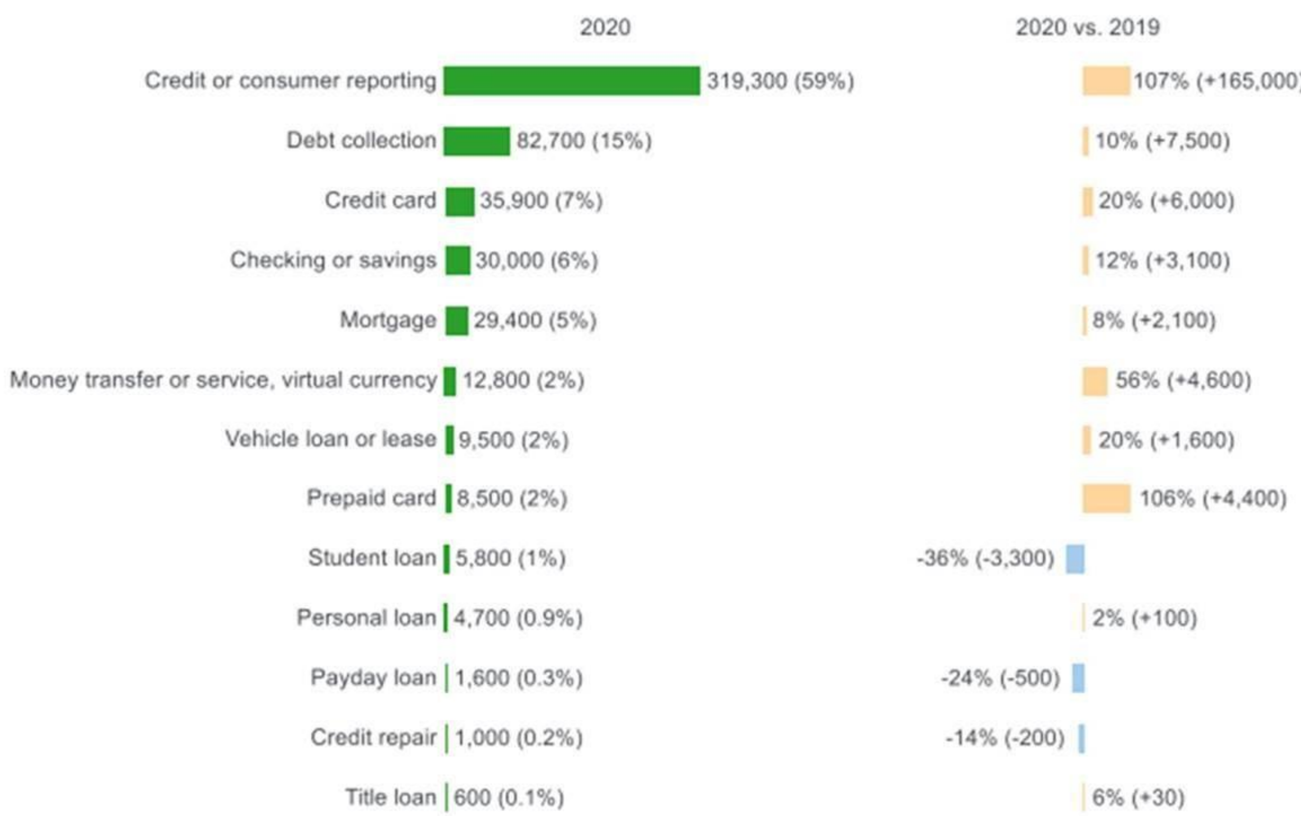


Finally, our online policing efforts have analyzed more than a million websites, remediating where possible and referring to authorities when companies refuse to act. In fact, since 2016, more than one million URLs have been discovered and more than 706,485 violations have been flagged.

In early 2021, the Consumer Financial Protection Bureau (CFPB) issued its Consumer Response Annual Report for 2020. In a year of record consumer complaints, the Bureau's complaint data for 2020 shows that the loan products OLA members offer performed very well with consumers. Of the more than half a million total complaints the CFPB received, personal loans (which include installment and line of credit loans) constituted less than one percent.

We believe the data in this report reflects OLA and its members' commitment to the highest industry standards, and it provides compelling information about consumers' use of online loans during the health and financial crisis that gripped our nation in 2020.

FIGURE 2: COMPLAINT VOLUME BY FINANCIAL PRODUCT OR SERVICE[13]



OCC SPECIAL USE CHARTERS

OLA Principle/Position: To increase innovative options for creditworthy customers, OLA supports the Office of the Comptroller of the Currency's (OCC) Special Purpose National Bank Charters.

> "To be clear, the National Bank Act does give the OCC the legal authority to grant national bank charters to companies engaged in the business of banking. That authority includes granting charters to companies that limit their business models to certain aspects of banking, and it is not circumscribed just because a company delivers banking services in new ways with innovative technology."
>
> Thomas Curry, former Comptroller of the Currency[4]

For decades, banks have existed in a two-tiered federal- and state-chartered system. The non-bank financial industry has expanded and evolved to benefit consumers with increased competition and an array of products and offerings. The two-tiered charter system is necessary to deliver these competitive products and services.

On July 31, 2018, the OCC announced it would begin accepting applications for national bank charters from nondepository financial technology (fintech) companies engaged in the business of banking.[5] Qualifying fintech companies may also apply for federal charters under the OCC's authority to charter full-service national banks and other special purpose banks, such as trust banks, banker's banks, and credit card banks.[6]

The OCC's decision to accept applications for special purpose charters from fintech businesses is currently being challenged in the New York federal district court. The presiding judge refused to dismiss the challenge and is allowing the case to move forward after finding the term "business of banking" as used in the National Bank Act to require "receiving deposits as an aspect of the business."[7]

OLA supports legislation to clarify and assert the OCC's authority to issue Special Purpose National Bank Charters and to clarify fintech companies' standing to obtain these charters.

BANK FINTECH RELATIONSHIPS

OLA Principle/Position: To increase options for creditworthy customers, OLA supports a clear, straightforward, and consistent standard in the spirit of the True Lender rule that identifies the lender of a loan in a bank partnership with a third party, like a fintech.

By working with fintech companies that have superior resources dedicated to research and technology, banks—often community banks—can enhance customer offerings and compete with nonbank online lending businesses. These partnerships also create opportunities and expand choices for low- to moderate-income borrowers who may have poor or thin credit.

In recent years, banks partnering with online lenders to provide non-prime borrowers with opportunities to access credit and strengthen their position in the banking system have been plagued by "true lender" lawsuits. These lawsuits challenge whether the named bank is the true lender, even if the bank extends the credit according to underwriting criteria it has approved, is included as the lender in the loan agreement, and holds the loan for some time after the loan is made.[8]

A split in courts' analysis of "true lender" litigation—and whether the bank or fintech company is the lender for purposes of federal banking laws, including provisions in the Federal Deposit Insurance Act (FDIA) and National Banking Act (NBA) that authorize a bank to export the maximum interest rate permitted in the bank's home state—will have a chilling effect on innovation in the United States. Without certainty, these market participants may no longer make loans (and consumers will be denied credit) if there is a real possibility of a court invalidating their loans after the fact.

OLA supported the OCC's 2020 True Lender rule as a critical step towards bringing stability and regulatory certainty to banks as they seek to offer safe and reliable credit to underserved consumers. As expanding credit access to these populations has been a priority for regulators and government agencies, uncertainties over True Lender have inhibited banks' ability to meet these goals. Therefore, OLA opposed the reversal of the OCC's True Lender rule under the Congressional Review Act.

It should be noted that the policy issue of the True Lender argument is different from that of "valid when made" raised by *Madden v. Midland Funding*. In *Madden*, a loan originated by a bank was charged-off and sold by the bank to a debt buyer. Long-standing doctrine states that because the loan was valid when made by the bank, any fees that could be charged by the bank also could be charged by the buyer of the loan. In a true lender challenge, however, the validity of the underlying loan is called into question, with the plaintiff typically alleging that the loan was originated by a nonbank with terms and conditions that violate state law.[9]

RATE CAPS

OLA Principle/Position: To ensure that affordable loan products are available for all consumers, including those with thin or poor credit, OLA opposes non-market-based APR caps.

The annual percentage rate, or APR, is an "annual" representation of the cost of credit as a percent of the amount borrowed. Because the APR equation is based heavily on the duration of the loan, the rate dramatically increases for short term loans, and by itself, the APR can be a misleading representation of the cost of the loan for the consumer.

For example, what is the APR for a $100 loan that charges a $1 interest fee? Well, it depends on loan duration. Under the standard APR formula:

- If paid in one year, the APR is 1 percent.
- If paid in one month, the APR is 12 percent.
- If paid in one day, the APR is 365 percent.
- If paid in one hour, the APR is 8,760 percent.

The loan amount and fee are the same, but the duration of the loans significantly impacts the APR calculation. Given that short-term loans are generally repaid over a duration measured in months, APRs naturally tend to appear much higher than longer-term loans, even if the overall cost is comparable to other forms of credit. That can make APR a highly misleading metric when evaluating the true cost of short-term, small-dollar loans. Furthermore, studies indicate that borrowers who take out smaller dollar loans place far more attention and emphasis on the actual finance charges associated with the loans than the APR—meaning that APRs are not the driving force in consumer decision making.

Another factor in the APR calculation is the fixed costs associated with making the loan. An August 2020 Federal Reserve study found that due to the fixed costs associated with making any loan—whether $500 or $5,000—smaller loans result in higher interest rates compared to larger ones. That study also found that break-even interest rates decline sharply as the amount of the loan increases, as operating costs are spread across larger loan amounts.[10]

While opponents of short-term loans often cite the Military Lending Act (MLA) as absolute proof that a 36 percent APR cap on consumer loans is good policy, such advocacy turns a blind eye to the MLA's overall impact on military borrowers. A 2017 study by the U.S. Military Academy at West Point closely examined this issue, finding that many of the short-term, small-dollar loan products outlawed by the MLA for military borrowers had "few adverse effects" on servicemembers. In fact, the West Point study found that small dollar loan access may actually decrease the probability of being involuntarily separated from the Army by 10 percent. It also found that the alternatives—such as using pawn shops, bouncing checks, overdrafting accounts, or having utilities shut off—"could be equally or even more costly" to servicemembers and their families.[11]

A 2020 survey conducted by HarrisX found that nearly half (47 percent) of Americans use their entire paycheck to cover expenses with almost nothing left over in savings for at least half of the year, with 33 percent doing so every month. Among active duty military households, this number is significantly higher, with 68 percent living paycheck-to-paycheck at least every other month and a 54 percent doing so every month.

The survey also found that active duty military households have a higher likelihood of considering different sources to cover an unexpected expense of $400, including paying bills late (35 percent for active duty military, 11 percent for all Americans), pawning a valuable item (34 percent for active duty military, 10 percent for all Americans), overdrafting a bank account (32 percent for active duty military, 8 percent for all Americans), taking out a short-term loan due in 30 days (35 percent for active duty military, 7 percent for all Americans), getting a pay advance from their employer (34 percent for active duty military, 7 percent for all Americans), or taking out a loan from an online or non-bank lender (31 percent for active duty military, 6 percent for all Americans). Active duty military households are also more than twice as likely to hold debt from different sources, including banks/credit unions, family/friends, or an online lender or non-bank lender.

Furthermore, borrowing restrictions imposed as a result of the Military Lending Act (MLA) have resulted in a majority (51 percent) of active-duty military households being denied credit. This is clear evidence that the MLA has been problematic to servicemembers' financial health and, when examined in practice, demonstrates that this is the wrong model for the rest of America. In fact, a 2021 study found that regulations that ban short-term, small-dollar loans, like a blanket rate cap, reduced consumer welfare relative to existing regulation, which is the exact opposite of what rate cap proponents claim.[12] An earlier study found that after interest rate caps were imposed in Georgia and North Carolina, consumers bounced more checks, submitted more complaints about debt collectors, and filed for Chapter 7 bankruptcy at higher rates, according to economists at the Federal Reserve Bank of New York.[13]

Furthermore, a 2018 study by the World Bank Group's Finance, Competitiveness, and Innovation Global Practice found, when presenting six case studies of different types of interest rate caps, that such caps "often have substantial unintended side-effects," including "increases in non-interest fees and commissions, reduced price transparency, lower credit supply and loan approval rates for small and risky borrowers, a lower number of institutions and reduced branch density, as well as adverse impacts on bank profitability."[14]

OLA supports providing access to credit to the millions of Americans who have subprime credit scores and are unable to access credit at traditional financial institutions. A 36 percent APR cap would eliminate critical credit access for millions of consumers.

— ARTIFICIAL INTELLIGENCE AND MACHINE LEARNING —

OLA Principle/Position: OLA supports the exploration and development of Artificial Intelligence (AI) and Machine Learning (ML) technologies as ways to increase efficiencies, expand product offerings, and better manage risk in the financial services and lending system.

Driven by advancements in computer science, the use of artificial intelligence (AI) and machine learning (ML) in fintech has grown dramatically and shows no sign of diminishing. AI/ML has the potential to improve efficiencies in banking procedures, allowing financial institutions to better understand customer needs, transform credit options, and help the underbanked gain more access to traditional financial services.

AI/ML builds on statistical methods that have existed for years, including extending linear regression models to give users the ability to manage millions of inputs through statistical techniques to summarize and analyze large datasets for easy consumption. These advances enable financial institutions to access, analyze, and draw conclusions about enormous amounts of data far faster and more efficiently than the human brain. AI/ML not only allows for the high-speed processing of massive datasets, but it gives computers the ability to learn from the data, helping them become more effective at parsing data over time.
These techniques have taken on a prominent role due to the increased availability of data. One unique aspect of these tools is that the value of data does not diminish when used and, in some cases, the value increases as more data is accumulated. These characteristics, coupled with the expanded availability of different types of data, have spurred the accelerated adoption of AI/ML in the financial services space, fueling phenomenal growth and creating new products and services that are revolutionizing the marketplace.

Much of the focus on AI/ML centers around the role it can play in reducing fraud, lowering defaults, and improving overall efficiencies through enhancements in algorithms. Even more significant, though, are the ways in which these innovations have changed how consumers function in today's financial services environment. Consumers are now able to tailor the process to meet their needs in ways that were not possible a decade ago. The results—expanded credit markets, new product offerings, and greater financial inclusion—are a win-win for lenders and borrowers alike.

Yet, with all its promise, AI/ML faces potential barriers that could limit its adoption in the lending field. Regulators have at times been overly cautious about innovation, and in the case of AI/ML have communicated the rules of engagement inconsistently. This has led to uncertainty that discourages traditional financial institutions from engaging in new and creative uses for these techniques that could end up limiting availability of credit to consumers.

As with any new product or service, important questions remain around appropriate uses and oversight. It will be important to monitor the application of AI/ML models to track adherence with safety and soundness protocols, particularly in the areas of cyber security and data privacy. It is also incumbent upon the industry to provide proper training and transparent testing of its models and algorithms to guard against unintended bias creeping into its products and services. But these concerns should not be used as an excuse to block the smart use of AI/ML in the financial system.

AI/ML has harnessed the power of data to revolutionize the financial services sector. These changes already have altered business models, risk mitigation strategies, and systems performance. As this technology continues to evolve, consumers increasingly will come to expect more accessible products and services in real time, which will change the way both individuals and companies engage in financial activities.

DATA SECURITY

OLA Principle/Position: OLA believes that data must be both secure and available. OLA thus supports the development of a national data standard that protects customers while facilitating innovation.

If technology has revolutionized the financial services industry, then data is at the vanguard. The availability, assessment, and manipulation of vast amounts of information has enabled the industry to reach new consumers with new products and services not possible just years ago. In fact, many consider data to be the most valuable commodity in today's economy.

The increased availability of data has made it easier for the financial sector to meet consumer demands, but it comes with a downside: vulnerability to security breaches. For the fintech industry, the big question is how to balance innovation with privacy.

Data security tactics used by the fintech industry are as varied as the companies themselves; there is simply no "one size fits all" solution that works for everyone. This has required fintech companies and their partners to tailor their tactics and strategies, developing protocols based on specific and unique security challenges. While necessary, this presents additional barriers to product development and access to new customers, particularly for niche products or companies looking to enter smaller markets.

These challenges are exacerbated by an antiquated regulatory patchwork structure that is ill-suited to adapt to today's rapidly changing digital landscape. The rules are better suited to an age when data was mainly on paper or floppy disk and stored on servers down the hall. It's a far cry from today's environment, where massive amounts of information are moved seamlessly and instantaneously around the globe.

Data privacy rules have a sizable influence over innovations that will be critical to the growth of fintech firms. Machine learning, digital ID, artificial intelligence, and cloud-based systems are all impacted by the regulatory framework. Policymakers need to make sure the rules are technology neutral to prevent impeding innovations that otherwise could meet the financial needs of consumers.

To maximize the potential of fintech, regulators should keep in mind that data-driven technologies are exponentially more powerful and effective when they have access to larger pools of information. The harmonization of definitions, requirements, and expectations for data protection through a national standard would provide a level of legal certainty that would help facilitate the continued growth of these new technologies, while protecting consumers from unwanted access and use of their data.

A national standard offers the flexibility and space to innovate. It gives companies of all sizes the ability to take a risk-based approach to data security that is tailored to their own business models, needs, and practices. This is particularly critical for startup companies, allowing them to devote limited resources to expanding their products and services instead of towards complying with prescriptive rules unfit for their risk profiles. This also makes it easier for firms to operate securely across various jurisdictions and enter new markets.

As technology becomes increasingly omnipresent in the financial services industry, fintech companies' ability to protect sensitive personal information and give consumers more control over their data will depend on the structure that regulators impose on them. A well-crafted regulatory environment that utilizes both private and public avenues to improve operational standards, and which focuses on principles rather than prescriptive mandates, can balance privacy with innovation. That's the best way to boost economic growth while ensuring stability for financial markets and the protection of consumer data.

OPERATION CHOKEPOINT

OLA Principle/Position: OLA opposed Operation Choke Point and supports efforts to ensure fair access to the financial system; OLA believes that the federal government should not be able to use access to the financial system as a political weapon against lawful industries or companies.

Launched in 2013, Operation Choke Point pushed thousands of legal, licensed, and regulated companies out of business by cutting off their access to the U.S. banking system. This was a gross misuse of government power. It circumvented the legislative and policymaking processes to unfairly punish legitimate and legal organizations.

This program dangerously inserted politics into essential banking services. Unsealed court documents revealed an effort by high-ranking, unelected FDIC and OCC officials to discontinue banking relationships with small dollar online lenders based on their personal and subjective views of these and other lawful industries.

The government was right to officially put an end to Operation Choke Point in 2017, and OLA supports efforts that would ensure the integrity of the banking system and protect the millions of Americans who rely on access to short-term, small-dollar credit products to make ends meet.

The OCC's proposed Fair Access rule is a step in the right direction. The rule would codify OCC guidance stating that banks should conduct risk assessments of individual customers rather than make broad-based decisions affecting whole categories or classes of customers when providing access to services, capital, and credit.

OLA supports legislation that would protect discrimination by banks or other financial service providers against law abiding industries and companies. OLA supports the Fair Access to Banking Act (S. 563) which would require banks to provide justification for denying services while penalizing those financial institutions that refuse to do business with legally compliant industries.

OLA also supports protective language in the Secure and Fair Enforcement (SAFE) Banking Act (H.R. 1996) that would prohibit a federal banking agency from even discouraging a depository institution from having a business relationship with a customer based on reputational risk.

ENDNOTES

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