

January 14, 2017

Mr. Thomas J. Curry  
Comptroller of the Currency  
Office of the Comptroller of the Currency  
Washington, D.C.  
[Regs.comments@occ.treas.gov](mailto:Regs.comments@occ.treas.gov)

*Re: California Group Comments on Exploring Special Purpose National Bank Charters for Fintech Companies*

Dear Comptroller Curry,

The undersigned community groups write to express our strong concerns regarding the OCC's proposal to develop a special purpose charter for fintech companies. We represent California based community organizations that work to promote the financial health and wealth accumulation of small businesses, consumers, residents and communities in our state. We do very much appreciate this opportunity to comment.

Fintech, or the intersection between financial services and technology, represents not only a vastly expanding market, but both an opportunity and grave threat to low income communities and communities of color. As the OCC has noted, fintech has the potential to create opportunities for such consumers and communities. Yet the experience of groups working with small businesses and consumers in our state to date has demonstrated that fintech can also have devastating impacts, and be destabilizing to communities and harmful to small businesses.

Community groups in California report fintech abuses that inflict continuing and significant harm on small business and consumer clients. Frequently, CDFIs, community lenders and technical assistance providers need to expend limited capital and resources to extricate clients from harmful fintech loans and other products. This is especially true for small and micro businesses who may see and experience fintech lending as the "default" credit option in light of banks' withdrawal from small business lending. We know that, just as with subprime mortgage lending, many of these loans are not sustainable, as the experience of community development practitioners working with small businesses, and industry data<sup>1</sup> suggest.

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<sup>1</sup> Matt Scully, "U.S. Consumers Are Increasingly Defaulting on Loans Made Online," Bloomberg, November 15, 2016, noting four bond deals facing default and delinquency "triggers" which would force lenders or underwriters to start paying down the bonds early.

A seminal look at how fintech affects small businesses in California is a recent report by Opportunity Fund entitled “Unaffordable and Unsustainable: The New Business Lending,” which analyzed loan applications from over 100 small businesses that sought to refinance debt that included 150 alternative loans. Key findings include:

- The average alternative loan carried an APR of 94%, with one loan reaching a shocking 358% APR;
- More than a quarter of businesses had loans outstanding with multiple alternative lenders, which is reminiscent of loan “stacking” by predatory payday lenders which confine borrowers into a cycle of debt that is hard to escape;
- The average monthly loan payment for businesses was nearly double the net income available to the owners;
- Disturbingly, among Hispanic/Latino borrowers, the average monthly payment was more than 400% of take home pay (which raises serious fair lending concerns);
- For businesses that Opportunity Fund could refinance, monthly payments fell by more than 60% and APRs dropped by an average of 85%; and
- Most of the refinance applications that were denied by Opportunity Fund were from businesses that owed so much money they could not afford to repay a lower cost and longer term loan.

**One thing that is clear is that fintech companies across the board must be subject to greater regulation and oversight, especially and including certain companies like Merchant Cash Advance providers that have managed to fly below the radar of state and federal oversight (and presumably would not seek an OCC special purpose charter).**

Our threshold concerns with the OCC proposal are many, and fall into the following broad categories:

- **Supervision.** The OCC is not well equipped to handle a new charter, as recent revelations regarding long standing consumer abuses at Wells Fargo Bank<sup>2</sup> demonstrate.<sup>3</sup> Additionally, it is not clear that the OCC has the expertise to properly supervise new companies using new technologies;

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<sup>2</sup> Wells Fargo was found to have created over 2 million unauthorized consumer accounts over a period of years. More recent revelations indicate that this conduct may have extended to insurance products, and may have been targeted at ethnic minorities. The OCC only recently took enforcement action, in conjunction with the Los Angeles City Attorney and the Consumer Financial Protection Bureau. This regulatory failure does not argue well for the OCC creating a new charter for new companies which use new technologies.

<sup>3</sup> A further example comes from a recently leaked memo demonstrating the challenges facing the state Attorney General’s office in investigating and seeking to subpoena OCC-chartered OneWest Bank, despite concerns by staff attorneys in that office about “widespread misconduct.” The Attorney General’s office wound up taking no formal enforcement action. It is not clear whether the OCC took any action relating to the egregious practices identified in the AG’s office preliminary investigation. See David Dayen, “Treasury Nominee Steve Mnuchin’s Bank Accused of ‘Widespread Misconduct in Leaked Memo,’” Intercept, January 3, 2017.

- **Preemption.** Predatory fintech actors will seek to take advantage of any preemption protection a charter brings, which will lead to further harm to small businesses, consumers and communities. This is unacceptable. Providing preemption protection to fintech firms will also encourage a regulatory race to the bottom with the all too real and familiar danger of the OCC competing with state and possibly other federal regulators to provide the most lenient and inviting forum to the industry.
- **A Done Deal.** Regardless of the numerous concerns that have been raised by consumer and community groups, state regulators, and even banks, the OCC seems prepared to plow ahead with a new charter. Indeed, in a recent interview with the American Banker, the OCC’s Chief Counsel indicated that such a charter could possibly be granted before the end of the Comptroller’s term in April.<sup>4</sup>

If the OCC determines to proceed with a new special purpose charter, despite all objections, the following components must be incorporated into its process and oversight:

- **Strong protections** for small businesses and consumers. We reiterate that a special purpose charter should not preempt state laws that regulate lending and other practices. If the OCC determines to provide preemption protection for fintech companies, it cannot “preempt and fail to replace” state level protections. Any preemption must be accompanied by:
  - Imposition of federal protections, including a clear and strong ability to repay standard (such as the CFPB’s Qualified Mortgage rules and proposed payday lending rules), and reasonable rate caps. These protections should extend equally to small businesses and consumers;
  - Consumer Compliance Ratings Systems evaluations of fintech companies with charters, with these grades being made public;<sup>5</sup>
  - Appropriate and more frequent use of the OCC’s Unfair and Deceptive (UDAP) authority to protect small businesses and consumers from unfair practices by fintech companies;
  - All investment advice provided by fintech banks should be subject to a fiduciary rule (like the Department of Labor rule for retirement investment advice);<sup>6</sup>
  - All payments by fintech banks should be consistent with the CFPB’s Guiding Principles for Faster Payment Networks and the recommendations of the FPTF Consumer Interest Segment;<sup>7</sup> and,

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<sup>4</sup> Lalita Clozel, “Fintech Charter Q&A: OCC Answers Skeptics,” American Banker, January 3, 2017.

<sup>5</sup> Josh Silver, “An Opportunity to Shed Sunlight on Lender Legal Compliance is Missed,” Rooflines, the Shelterforce Blog, November 21, 2016.

<sup>6</sup> Available at: <http://webapps.dol.gov/FederalRegister/PdfDisplay.aspx?DocId=28806>

<sup>7</sup> See <http://www.consumerfinance.gov/about-us/newsroom/cfpb-outlines-guiding-principles-for-faster-payment-networks/>.

- A clear and unambiguous statement by the OCC that preemption, at a minimum, does not extend, to state laws regarding anti-discrimination, fair lending, debt collection, taxation, zoning, criminal law and torts, as noted in the OCC proposal itself.
- **Fair lending** laws must be honored and enforced, and the OCC should ensure equal access and non-discrimination. In addition to clarifying that state fair lending laws would apply to fintech companies with OCC charters, the OCC should hold such companies to the high standards of the Equal Credit Opportunity Act (ECOA) and other fair lending and anti-discrimination laws. This is important for all financial institutions, but is especially important for fintech companies that often rely on Big Data algorithms that very well may have discriminatory factors baked into their formulas. Fintech lending patterns and other services should be scrutinized to ensure that all small businesses and consumers have equal access to all products and services at the same terms as all similarly situated and qualified borrowers and customers. Recent research suggests that small businesses owned by people of color may be vulnerable to being charged more due to “reservation prices,” – the notion that certain business owners may be willing to pay more for credit, given concerns the business owners may have about barriers to accessing any credit, and that this knowledge results in lenders charging these business owners more.<sup>8</sup>
  - It is critical that the OCC review, scrutinize, understand, and assess the “black box,” or “secret sauce” of fintech algorithms to ensure that there is NO opportunity for bias to be baked into the formulas or for disparate impact to result from fintech operations.
  - The OCC should publicize any fair lending enforcement actions or referrals it makes to instill confidence that the OCC is monitoring this critical issue.
- **Community Reinvestment Act obligations** must apply. We appreciate the proposal’s discussion of financial inclusion and reinvestment obligations, but the lack of clarity is concerning and will likely lead to weak reinvestment and minimal impact. We believe that the current CRA obligations for banks can be imposed in substantially the same form on fintech companies. Lending, Investment and Service tests can apply as appropriate to a given company’s business model. Fintech lenders must ensure that good loan products are being marketed and reaching low and moderate income consumers and communities, and that costly and harmful products are not targeted there. Just as we have argued for internet and other banks without a substantial branch presence, the CRA assessment area

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<sup>8</sup> See Timothy Bates and Alicia Robb, “Impacts of Owner Race and Geographic Context on Access to Small-Business Financing,” *Economic Development Quarterly* 2016, Vol. 30(2) 159-170, October 12, 2016. “We believe, finally, that racial differences in owner reservation prices are an important cause of the differing loan terms received by MBEs and White business borrowers. Applicable loan terms include not only loan dollar amount but loan maturity and interest rate as well. Our operating hypothesis is that the restricted borrowing choices faced by minority business owners produce observed loan-term differentials. Debt providers recognizing racial differences in these reservation prices are able to provide less favorable loan terms, on average, to MBE owners than to White loan recipients.”

can include those areas which represent the largest markets in which the lender operates, as well as those markets where the lender has a substantial local market share. We join NCRC in suggesting a threshold of more than one half of one percent of the market that would trigger a CRA assessment area. Investments and contributions, as well as financial services - such as highly relevant work in supporting and serving on boards of groups working on financial literacy and financial inclusion - can be focused in these same assessment area markets. Non lending fintech firms must be subject to the same CRA and financial inclusion obligations, which can be assessed using CRA Investment and Community Development tests, and which can focus on firms investing and providing grants to relevant organizations in low and moderate income communities. The OCC should establish guidelines and benchmarks for the level of investment to be expected, as reflected in a percentage of deposits, profits, and/or assets. Fintech reinvestment plans and implementation performance should be subject to public input and public regulatory examination, and considered during any application to merge, change business plan or expand business. Regulations should be promulgated, subject to public comment, to clarify these obligations.

- **Transparency** must be a cornerstone of fintech activities and regulatory oversight. One clear problem with respect to many fintech companies is the extent to which loan and other terms are not fixed, standard or transparent. Further, there is very little information available regarding the activities of Fintech firms. We note approvingly as a rare exception, the recent data collection effort of our state Department of Corporations,<sup>9</sup> which has resulted in some of the only data of its kind on fintech. The OCC must:
  - Require fintech firms to clearly display the pricing and terms of loans, products and services, including “all-in” APR disclosures for all consumers and small businesses;
  - Require fintech firms to report data on the census tract of loans and services that are originated or arranged, in line with requirements set out in section 1071 of the Dodd Frank Act. These data must be made public;
  - Allow consumers to file an online complaint in an easy, transparent and public fashion if there are problems. The model here should be the CFPB complaint system which allows consumers to review complaints filed against companies in a matter of seconds, and thereby to be informed about problematic practices and companies. There is no reason that a new agency such as the CFPB should have a vastly superior complaint system to that of the 150+ year old OCC; and
  - Directors and Officer Transparency. Often the only contact information for fintech companies is a 1-800 customer service number. Like any bank charter member, fintech companies should have their Board of Directors and Executive Management team posted on their websites, as well as corporate office location.

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<sup>9</sup> Commissioner of Business Oversight Jan Owen, “California Online Lending Grows by More than 930% Over Five Years: Total Dollar Amount, Volume Top 2013 Levels; Average Size and APR Fall,” Press Release, April 8, 2016.

- **Privacy concerns** of consumers and small businesses must be addressed. Comments by Federal Reserve Board Governor Brainard suggest that regulators may share concerns that data collection practices of the fintech sector could put consumer protection at risk.<sup>10</sup> Big data underlies much of the technology used by fintech firms. Consumer and small business privacy must be protected so as not only to prevent identify theft, but also to ensure that the data are not sold and used to facilitate marketing by abusive actors.
- **Public participation** and input must be preserved and accentuated in light of these numerous concern. As with banks, fintech charter applications, changes in fintech business plans, fintech reinvestment performance, and fintech mergers and business expansions should be subject to extensive public comment periods. Fintech firms should not be provided a competitive advantage vis a vis banks in any respect, especially given that this is a fledgling industry comprised of, at least some, unscrupulous actors.

In conclusion, we retain genuine and significant concerns about the explosion of online, marketplace and fintech lending and products, and remain unconvinced that the OCC will be able to effectively mitigate harms from these companies through the use of a special purpose national charter, especially in light of the expected harmful impacts of federal preemption. If the OCC proceeds to offer a charter to fintech firms, as all indications suggest, than we implore the OCC to impose vigorous obligations, supervision and enforcement of fintech firms with regard to consumer and small business protection, fair lending, community reinvestment, transparency, privacy and public participation concerns.

Thank you very much for the opportunity to comment, and for taking our views into account. Should you have any questions about this letter, feel free to contact Kevin Stein of the California Reinvestment Coalition at (415) 864-3980 or Robert Villarreal of CDC Small Business Finance, at (619) 243-8652.

Very Truly Yours,

A-1 Community Housing Services  
 Asian Law Alliance  
 Bankers Small Business CDC of California  
 California Capital Financial Development Corporation  
 California Coalition for Rural Housing  
 California Reinvestment Coalition  
 California Resources and Training  
 CDC Small Business Finance  
 Community Legal Services of East Palo Alto (CLSEPA)

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<sup>10</sup> See comments by Governor Brainard reported in an article by Rachel Witkowski in the Wall Street Journal on December 2, 2016 entitled “Regulator Will Start Issuing Bank Charters for Fintech Firms.”

Consumer Action  
Law Foundation of Silicon Valley  
Main Street Launch  
Mission Economic Development Agency (MEDA)  
NPHS, Inc.  
Nuestra Casa de East Palo Alto  
Pacific Asian Consortium in Employment (PACE)  
Public Counsel  
Vermont Slauson Economic Development Corporation