



Innovative Lending Platform Association

July 12, 2021

SENT VIA ELECTRONIC MAIL

Attn: Ann E. Misback
Secretary of the Board
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

Re: Proposed Guidelines for Evaluating Account and Services Requests (Docket No. OP-1747)

The Innovative Lending Platform Association (ILPA) appreciates the opportunity to provide comments to the Board of Governors of the Federal Reserve System (FRB or Board) surrounding its proposed guidelines (Account Access Guidelines) to evaluate requests for accounts and services at Federal Reserve Banks.

ILPA appreciates the FRB's decision to propose the Account Access Guidelines to standardize the Federal Reserve Banks' consideration of applications for master accounts and/or access to Federal Reserve Bank financial services. The FRB notes such standardization is needed as technological advancement has prompted a paradigm shift in the financial services industry with new financial products and services being offered by new market entrants (such as our members). These new entrants are also reimagining the provision of traditional banking services.

As the FRB notes in its release, many of these new market entrants are seeking novel bank charters, and it has seen an exponential increase in the number of these new market entrants with these novel bank charters applying for accounts and services at Federal Reserve Banks. Given the confluence of new charter types applying for accounts and services in record numbers, the Board believes it prudent to issue the Account Access Guidelines to standardize the approval process to reduce the risk these institutions might pose to the broader financial system.

The FRB proposes six principles Federal Reserve Banks should consider when evaluating the merits of novel new market entrants' applications for Federal Reserve Bank master accounts and services. The six principles are structured in such a way as to promote the Board's policy goals: (1) ensure the safety and soundness of the banking system; (2) effectively implement monetary policy; (3) promote financial stability; (4) protect consumers; and (5) promote a safe, efficient, inclusive, and innovative payment system. The six principles the Board proposes to govern Reserve Banks' consideration of applications for accounts and services are:

1. Each institution requesting an account or services must be eligible under the Federal Reserve Act or other federal statute to maintain an account at a Federal Reserve Bank (Reserve Bank) and receive Federal Reserve services and should have a well-founded, clear, transparent, and enforceable legal basis for its operations.
2. Provision of an account and services to an institution should not present or create undue credit, operational, settlement, cyber or other risks to the Reserve Bank.
3. Provision of an account and services to an institution should not present or create undue credit, liquidity, operational, settlement, cyber or other risks to the overall payment system.

4. Provision of an account and services to an institution should not create undue risk to the stability of the U.S. financial system.
5. Provision of an account and services to an institution should not create undue risk to the overall economy by facilitating activities such as money laundering, terrorism financing, fraud, cybercrimes, or other illicit activity.
6. Provision of an account and services to an institution should not adversely affect the Federal Reserve's ability to implement monetary policy.

ILPA applauds the FRB for taking the initiative to proactively address concerns around granting access to accounts and services to novel new market entrants. While we are thankful for the attempt to provide greater certainty to these novel applicants as they seek to gain access to Federal Reserve Bank accounts and services, we believe the Account Access Guidelines could be substantially improved in specific ways that further promote the Board's policy goals and strengthen the financial ecosystem. Our comments will seek to address the three specific questions the Board poses in the release:

1. Do the proposed account access guidelines address all the risks that would be relevant to the Federal Reserve's policy goals?
2. Does the level of specificity in each principle provide sufficient clarity and transparency about how the Reserve Banks will evaluate requests?
3. Do the proposed account access guidelines support responsible financial innovation?

About ILPA

ILPA is the leading trade organization for online financing and service companies serving small businesses. Our member companies¹ share a commitment to the health and success of our nation's small businesses and dedicate themselves to advancing best practices and standards that promote responsible innovation and access to capital. Our members have provided over \$50 billion to more than 1 million small businesses in a variety of industries, from restaurants, to construction to hair salons and beyond. Our members provide financing from \$5,000 to \$500,000 with an average loan size of between \$35,000 and \$80,000 primarily to businesses with fewer than 10 employees. In addition, ILPA members meaningfully participated in the Paycheck Protection Program (PPP) lending, both directly and through bank partnerships. Our members facilitated over 600,000 PPP loans with an average size of approximately \$35,000 and a median loan size of approximately \$15,000. According to the data submitted by borrowers, ILPA members saved over 2 million jobs and served small businesses with an average of 5 to 6 employees. Additionally, fintechs were active members in the Federal Reserve's Paycheck Protection Program Liquidity Facility (PPPLF) throughout the pandemic.

In 2016, ILPA launched an industry-first, voluntary model disclosure tool – the SMART Box® – that presents small businesses with comprehensive pricing metrics and identifies key financing terms in plain, easy-to-understand language. In addition to the SMART Box®, each ILPA member adheres to a Code of Ethics that sets forth the best practices for our members involved in providing, facilitating, and supporting the provision of capital to small businesses. Those best practices include the following commitments: (1) offers of capital or financing should be transparent and comprehensive; (2) small business customers should be treated fairly; (3) capital to small business customers should be offered responsibly; (4) agents and brokers should be encouraged to adhere strictly to all applicable laws and treat small businesses honestly and fairly; and (5) adoption of this Code of Ethics throughout company operations.

¹ Members of ILPA include A10 Capital, BFS Capital/Nuula, Bizz2Credit, BlueVine, Fundbox, Funding Circle, Kabbage/AMEX, Lendio, Mulligan Funding, OnDeck/Enova, Paynet/Equifax

As small business lending platforms, ILPA members have a tangible impact on our nation's businesses every day. ILPA members believe that in order to grow and invest in their business and employees, small business owners need access to timely and affordable credit. They need capital to purchase inventory and equipment, to upgrade or expand their facilities or operations, and to hire new workers. Unfortunately, small businesses have historically lacked access to capital, a challenge exacerbated by the Great Recession. The cost and approach of traditional underwriting practices continue to render "Main Street" lending not economically viable for many banks, resulting in a credit gap for small businesses that risks their success and vitality. ILPA members leverage innovative technologies, business models, and in some cases, bank partnerships to fill that gap.

Overview of Response To Account Access Guidelines Proposal

In response to the Board's third question in the release, ILPA is encouraged by the possibility of non-depository fintech lenders that are subject to regulation by a state(s) being permitted access to the Fed's settlement services. At present, fintech's have to rely on a bank partnership with a legacy financial institution to gain access. While that relationship has been beneficial in allowing banks to expand their reach into traditionally underserved communities, fintechs can achieve far greater scale and provide greater service to millions of consumers and small businesses if these companies are allowed to access the Fed's settlement service directly. ILPA is encouraged that the FRB includes special purpose charters granted through the Office of the Comptroller of the Currency (OCC) in its Account Access Guidelines. However, ILPA believes the proposal does not adequately encompass all potential new market entrants that should be eligible for account access and services. Special purpose charters through the OCC are difficult to qualify for and the Acting Comptroller has recently issued a pause on applications as the agency undertakes a comprehensive review. The ILPA encourages the FRB to move forward in the meantime, expanding access to fintechs beyond those that have applied for and been granted special purpose charters through the OCC. With respect to including a broader set of institutions, we believe the principles and factors used in the framework to govern access to accounts and services should be tailored to the specific risk these new market entrants present – risk posed which is oftentimes far less than the risk of deposit-taking institutions.

Such payment system access is not without precedent since many fintechs participated in the PPPLF with no emerging systemic threat to the financial system. More specifically, fintech participation in the payments system would further the Board's five policy goals as outlined above, increasing stability, consumer protection and access.

Guidelines Do Not Support Responsible Financial Innovation

A. Guidelines are Contrary to the Promotion of an Inclusive and Innovative Payment System

As previously mentioned the ILPA is encouraged that the Fed is open to supporting responsible innovation through allowing access to the FRB settlement service. With regard to institutions that have received a special purpose charter through the OCC, ILPA contends that these institutions meet the criteria for inclusion. ILPA asserts new market entrants that obtain special purpose charters, whether through the OCC or the various states, are legally entitled to access to accounts and services as they meet the definition of a "depository institution" under Section 19 of the Federal Reserve Act which governs eligibility for accounts and services. Section 19 defines a "depository institution," in part, as any banking entity that is "eligible to make an application to become" insured under section 5 of the Federal Deposit Insurance Act.

ILPA, along with the OCC, has long maintained that a "bank" is constituted by any entity substantially engaged in lending, payments or deposit taking. While a new market entrant with a special purpose charter might only be engaged in lending, payments, or a combination of the two at present, pursuant to its charter, it is

eligible to take deposits as a line of business in the future. Thus, it is also “eligible to make an application to become” insured rendering it qualified for access to accounts and services at a Federal Reserve Bank.

Beyond those institutions that have received a special purpose charter through the OCC, the ILPA encourages the FRB to broaden the scope of the proposal, to include non-depository state-regulated lenders. As previously mentioned, such a step would help foster innovation and drive down costs for customers. As noted by other commenters, the Bank of England recently took a similar action in providing “non-bank payment service providers” direct access to its wholesale settlement services. This approach is consistent with the idea of regulating institutions based on the activities said institutions perform, rather than a broad-based one-size-fits-all approach that only allows legacy institutions into the settlement service network.

The lack of access to Federal Reserve Bank master accounts and services for new market entrants does create barriers to entry which reduce competition in the financial services arena and inevitably raise the cost of doing business which is then passed onto the customer. Many new market entrants offering new financial products and services and traditional banking services to customers partner with existing banks to offer their services. However, many of these new entrants, if they obtained direct access to master accounts and services at a Federal Reserve Banks, would not need to partner with a bank in order to conduct their operations, at least as it relates to the transmission of payments. If new market entrants were able to hold an account at a Federal Reserve Bank, it would eliminate the need to hold an account with and process payments through a correspondent bank. The elimination of this banking intermediary would reduce operational costs for new entrants which could and ultimately would be passed onto their customers. PPP lenders that ultimately accessed the PPPLF can attest to the costs and friction incurred in securing a correspondent bank to access the Federal Reserve Bank. In fact, most banks do not even offer the correspondent service as the costs do not justify the operational burden required to facilitate such intermediary relationships. In addition, access to Federal Reserve Bank services could also lower costs to the extent pricing of those services is advantageous to the pricing provided by private banks.

B. Guidelines Fail to Support Financial Innovation by Entrenching Existing Regulatory Structures

In proposing the Account Access Guidelines, ILPA believes the FRB should seek to balance the need for additional oversight with risk posed by new entrants in the settlement service, no more and no less. Fintechs are not traditional banks, do not take deposits and do not pose the same risks to the FRB. As currently written, we believe the principles and factors established entrench the traditional regulatory structure governing access to Federal Reserve Bank master accounts and services which inordinately centers around the risks posed by and protects the interests of deposit-taking institutions.

There are numerous factors in the proposal that guard against the increased risks posed by depository institutions, for instance the capital and liquidity requirements suggested in factors 2(d)(ii), 3(c)(i) and 3(d)(ii). These factors are appropriate for a deposit-taking financial institution, especially large banks that pose a systemic risk. Non-depository state regulated fintech lenders, however, tend to be far smaller, do not pose a risk to the FDIC insurance fund, and pose no systemic risk. The imposition of this factor to new market entrants who are overwhelmingly non-depository institutions is extraneous and excessive. Such a requirement would only serve to hamstring new market entrants with additional regulatory burdens that are not necessary to protect the system all the while reducing their ability to compete with established industry participants by increasing costs that will need to be passed onto customers.

Finally, while ILPA believes it understands the Board’s rationale for permitting new accounts and services to new market entrants enhances the efficacy of monetary policy transmission, as factors 6(b) and 6(c) appear designed to do, we do not believe this is an important consideration or useful policy goal to determine the merits of permitting access to accounts and services given the limited role fintechs play in credit intermediation as compared to legacy institutions. Subjecting approval for these entrants to accounts and

services based upon their utility toward and ability to facilitate this policy goal is not a suitable criterion for evaluation. Subjecting them to such a standard would only make it more likely they would be denied access further consolidating the industry and increasing costs for customers.

ILPA strongly urges the Board to reconsider amending the proposed guidelines to more adequately reflect the reduced risk new market entrants pose to the system when gaining access to master accounts and services at Federal Reserve Banks. The Board should reform the guidelines to reflect the risk to the system presented by these new market entrants as they do indeed introduce less risk vis-à-vis traditional banking entities. This is exemplified by their predominant business models. Specifically, these entrants do not seek to replicate the traditional banking model of making highly illiquid loans (assets) with highly liquid deposits (liabilities). The lack of any meaningful maturity transformation poses less risk to both these institutions and the broader financial system.

C. Establish A Separate but Complimentary Access Regime Specific To Certain New Market Entrants

ILPA sees much value in and is a proponent of proposals, posited by many industry stakeholders, to streamline the guidelines governing access to accounts and services by stipulating new market entrants that already retain certain bank charters and state licenses meet the requirements of the guidelines. Such an approach would also allow the Board to attach supplemental requirements to specific charters and licenses it deems necessary. These additional requirements would help protect against any remaining risks posed to the system presented by account access and services for those charter and license types.

Conclusion

We are encouraged by the FRB releasing the Account Access Guidelines and encourage the FRB to both look at a broader universe of market participants and focus on tailoring additional regulatory to meet the activities of the institution, rather than apply a one-size-fits-all approach which unfortunately leads to further entrenchment of legacy financial institutions. The Account Access Guidelines need to be amended to facilitate more access to master accounts and services for new market entrants by expanding the types of business entities able to obtain accounts and services. The proposal also needs to tailor the principles and factors governing access to more adequately address the risks posed by new entrants. The Board should consider instituting a separate, complimentary regime to govern access to accounts and services for these new entrants. These changes would promote competition in the financial services industry thereby reducing costs for new market entrants and ultimately the customers they serve.

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We look forward to continuing to work with the FRB on the proposed Account Access Guidelines. If you have any questions, please do not hesitate to contact me at scott@innovativelending.org.

Best regards,



Scott Stewart, CEO
Innovative Lending Platform Association