Chapman and Cutler LLP

Chapman Client Alert

April 14, 2021 Current Issues Relevant to Our Clients

Two Court Actions with Implications for Marketplace Lenders

In the past few days, two courts have actions that are of significance to marketplace lenders and their funding sources. In Maryland, a state regulatory action purporting to require licensing of a sponsor bank and its fintech service providers has been removed to federal court. Conversely, a California federal court has dismissed an action challenging a marketplace lending program.

Maryland Regulator Seeks Licensing of Bank and Its Service Providers

In *Salazar v. Fortiva Financial, LLC, Atlanticus Services Corporation and the Bank of Missouri s/b/m Mid-America Bank & Trust Company*, the Maryland Office of the Commissioner of Financial Regulation (*"Commissioner"*) recently alleged a Missouri state chartered bank and its fintech partners engaged in a "bank partnership" program violating various Maryland licensing and credit related statutes. Depending on the outcome of this matter, it could significantly change how banks and their fintech partners approach such Maryland requirements.

In the Charge Letter, the Commissioner alleged both the bank and its fintech partners engaged in unlicensed activities. Specifically, the Commissioner alleged the bank made unsecured consumer loans without complying with the regulatory provisions found in the Maryland Consumer Loan Law. The Commissioner also alleged the bank violated the installment loan licensing requirements by making unsecured consumer loans pursuant to Maryland's Credit Grantor Closed End Credit Provisions without a license or an exemption.

As for the bank's fintech partners, the Commissioner alleged they failed to obtain a license under the Maryland Credit Services Businesses Act. Maryland takes the view that this registration is required to solicit or arrange unsecured consumer loans for others such as banks. Because the bank allegedly failed to comply with the regulatory provisions found in the Maryland Consumer Loan Law, Maryland charged that neither the bank nor its fintech partners may receive or retain any principal, interest or compensation with respect to any loan made to a Maryland resident. The Commissioner also alleged the fintech partners violated the Maryland Collection Agency Licensing Act by soliciting and collecting consumer claims for others (i.e., the bank) without a license.

The defendants removed the matter to federal court on the grounds that the federal court has federal question jurisdiction over the Commissioner's claims against the bank and federal law preempts the Commissioner's claims.

We will advise of significant developments. This case is yet another reminder of the importance of licensing that may apply to marketplace lending programs between a non-bank service provider and a bank. In this action, the state alleges that both the non-bank service provider and the out of state bank are subject to licensing and credit requirements.

Challenge to Bank Partnership Program Dismissed

On April 13, 2021, a case was decided in the Northern District of California involving FinWise Bank, a sponsor bank and its non-bank service provider Opportunity Financial, LLC challenging the validity of loans and business practices associated with a bank partnership program. *Sims v. Opportunity Fin.*, et al, 2021 U.S. Dist. LEXIS 71360. Originally filed in state court, the defendants removed the action to federal court and filed a motion to dismiss. The plaintiff, a California consumer alleged that the defendants operated a "rent-a-bank" scheme to issue high cost loans although the bank was listed as the lender on the loan. The plaintiffs claimed the bank was lender in name only, with the service provider marketing the loan, purchasing the loan and then servicing and collecting the loan which plaintiffs alleged were to evade California interest rate restrictions.

The plaintiff made several claims against the defendants under both California and Utah law for unfair and unconscionable conduct and requested reformation of the loan contract and refunds for excessive charges. The defendants challenged all claims based on the doctrine of federal preemption and alternatively that if preemption failed that the action failed to state a cognizable claim under either state's law.

The court found that all of the plaintiff's claims failed on the merits and as a result, did not need to address or resolve the issue of federal preemption. In part, the Court held that the plaintiff failed to show that the defendants were subject to the California Financial Code which contains wording that the California statute does not apply to any person doing business under any law of any state relating to banks. In that regard, the Court upheld existing precedent that as to usury, the court may look only to the face of the transaction and not to the intent of the parties (citing *Beechum v. Navient Sols., Inc.*, 2016 WL 5340454 (C.D. Cal. 2016). On the face of the loan agreement, it was not subject to California law. The court noted that arguments as to evasion of California law are irrelevant since the bank is the lender on the documents. The court also reviewed the service provider's website and found that it was not misleading as to who was the lender on the loans. The Court also dismissed claims under Utah law for unconscionability in that Utah law allows any rate of interest to be charged on a loan.

A claim was also made under the Electronic Funds Transfer Act that a preauthorized transfer was required as a condition of the loan and therefore violated EFTA and Regulation E. The court found this claim to be insufficient based on language in the loan agreement allowing for alternative payment methods.

This decision is welcome news for marketplace lending programs.

For More Information

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