

New York Department of Financial Services Issues Online Lending Report That Includes Recommendations Impacting More Than Online Lenders

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Last week, the New York Department of Financial Services (DFS) published an [Online Lending Report](#) (Report) that analyzed the operations, products, and practices of entities engaging in online lending activities in New York. In reaching its findings and recommendations, the DFS utilized information submitted by both licensed and unlicensed lending institutions in response to its Marketplace Lending Survey issued earlier this year. As outlined below, the DFS determined that the Report leads to the conclusion that the DFS should have its regulatory authority increased.

Background

The DFS first provided a background overview of New York's laws and regulations relating to consumer lending. In its discussion, the DFS argued that high-interest lenders, who are often located outside of New York, pose a significant threat to New York consumers because they can evade New York usury laws by operating exclusively online or by partnering with banks not subject to New York laws. While acknowledging that certain banks and depository institutions may import their states' rates into New York, the DFS noted that these imported rates do not apply to non-banks, such as non-depository lenders. Specifically, the DFS expressed concern with payday lenders who partner with out-of-state banks or Native American tribes to avoid New York's ban on payday lending.

The DFS discussed other high-level issues relating to the activities of online lenders. The DFS cemented its position regarding the ongoing "true lender" cases, seemingly taking the position that entities engaged in business in New York must be licensed even if licensure is not explicitly required by statute or regulation. Moreover, the DFS stated that a future market downturn would present specific problems for marketplace lenders as investors would lose their appetite for funding speculative lending in a down market. The DFS also noted more pointed concerns, taking issue, for example, with the fact that online lenders currently are not subject to either the federal or New York Community Reinvestment Act.

Finally, the DFS detailed its recent regulatory actions and consent orders, primarily focusing on its actions against payday lenders, lead generators, debt buyers, and other entities in the payday lending space. The DFS also indicated that it plans to engage in further study of the consumer litigation financing industry, hinting that these transactions could be considered usurious if lending rules were to apply.

The DFS' Recommendations

Based on its findings, the DFS made three recommendations at the conclusion of the Report. If these recommendations are implemented, they may impact the regulatory and licensing requirements imposed on online lenders, as well as other creditors.

- The DFS recommends applying New York's consumer protection laws equally to all consumer lending and small business lending. The recommendation includes protections relating to transparency in pricing, fair lending, fair debt collection practices, and data protection.
- The DFS is also recommending that New York's usury limits apply to all lending in New York, regardless of whether the loan is made by a bank, credit union, or from an online lender.
 - **McGlinchey Insight:** It is worth noting that New York has limited authority to regulate interest rates when certain institutions, such as national banks or federal savings associations, export interest from another state.
- Finally, the DFS is recommending that the rate threshold that is used to determine whether licensure under Banking Law Article IX (Licensed Lenders) be reduced from its current threshold of 16% to 7%.
 - **McGlinchey Insight:** It is worth noting that Article IX does not explicitly require a license to make a loan and charge interest greater than 16%. Instead, with respect to the rate threshold, Article IX currently requires a license to charge "a greater rate of interest than the lender would be permitted by law to charge if he were not a licensee." This language allows certain lenders relying on alternative rate authority, such as 12 U.S.C. § 1831d or DIDA § 501, 12 U.S.C. § 1735f-7a, to make loans with interest greater than New York's civil usury limit of 16% without the need to obtain a licensed lender license. As a result, if this recommendation is implemented, a significant number of lenders, including out-of-state state-chartered banks, may find themselves subject to New York's licensing requirements.

Conclusion

On balance, the Report indicates a strong desire by the DFS to expand its authority to include online and other lending operations not currently regulated by the DFS, such as those that operate through the use of bank partnership programs and those with interest rates below New York's civil usury limit. As a result, online lenders should prepare for the possibility of increased regulatory scrutiny from the DFS in the future, while other lenders should prepare for the prospect of expanded licensing requirements, regardless of whether they operate online. The DFS' emphasis on the ability to apply New York usury limits to all lenders, including loans made by FDIC insured depository institutions involved in a bank partnership program, would likely have a significant impact on current bank partnership models operating in New York.

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