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BANK PARTNERSHIP AGREEMENTS

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Prior FinTech Flash installments have addressed the pros and cons of marketplace lending companies entering into bank partnerships as well considerations relevant for determining whether a marketplace lending platform or its bank partner is the "true lender." If a marketplace lending platform decides that it makes sense to enter into an arrangement with a bank partner, then it will need to negotiate and enter into a contractual agreement with its bank partner that satisfies applicable legal and regulatory requirements, establishes a structure for the arrangement intended to result in the bank partner being viewed as the "true lender," and addresses other legal and business considerations.

Although arrangements between banks and marketplace lending platforms are often referred to as "partnerships," these arrangements are not legal partnerships that involve joint sharing of profit and loss but rather highly negotiated arrangements between independent third parties. A typical arrangement between a marketplace lending platform and a bank involves the performance by the marketplace lending platform of specific functions related to the marketing, origination, sale and servicing of loans made and funded by the bank, with the bank supervising the activities of the marketplace lending platform performed on the bank's behalf. After the bank has funded the loans and held them on its balance sheet for a period of time, it may retain some or all of the loans for its own portfolio or sell some or all of the loans to the marketplace lending platform or other third parties. As a result, marketplace lending arrangements with banks are typically documented in a marketplace lending program agreement that addresses the manner in which loans will be originated and funded, and separate but related loan or receivables purchase and sale and servicing agreements. These agreements commonly include provisions in which the parties agree to collaborate on development of marketing plans, underwriting criteria, servicing guidelines and other operational processes as well as assess the effects of changes in law and market conditions on the program. However, the bank normally retains authority to approve and supervise the key aspects of the lending program in which it is involved or that are carried out on its behalf. Marketplace lending program agreements also typically allocate risk between the bank and the marketplace lending platform through detailed covenants, representations and warranties and through indemnification provisions.

The federal bank regulatory agencies—the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Board of Governors of the Federal Reserve System—have issued guidance to the institutions they supervise addressing requirements for business relationships between banks and third parties. In general, this guidance requires banks to apply a risk management process to third-party relationships that is commensurate with the level of risk and complexity of the relationship. Banks are required to subject critical relationships with third parties to the most comprehensive

and rigorous level of oversight and management. The bank regulatory agencies regard as "critical" third-party relationships that involve significant bank functions or services, or the performance of activities that could subject the bank to significant risk or materially affect the bank's customers. Since arrangements between marketplace lending platforms and banks typically require the marketplace lending partner to perform marketing functions, engage in loan underwriting activities, prepare and deliver legally mandated disclosures to consumers and engage in other functions on behalf of and subject to the direction of the bank partner, these arrangements are subject to the guidance provided by the federal bank regulatory agencies relating to third-party relationships and are typically viewed as critical relationships for this purpose.

When applicable, the third-party relationship guidance requires banks to conduct initial due diligence before entering into a relationship with a third party such as a marketplace lending platform and to engage in ongoing monitoring throughout the life of the relationship. Among other matters, banks should consider whether the third party has all necessary licenses or qualifications to perform its obligations; the third party's experience, reputation and financial condition; the effectiveness of the third party's risk management, control and oversight process; the strength of the third party's information security program; the third party's business continuity plan; and other matters. A marketplace lending platform seeking to enter into an arrangement with a bank should anticipate that its bank counterparty will want to conduct extensive and robust due diligence before entering into the relationship and on a going-forward basis.

The bank regulatory agencies have also advised that third-party relationships must be documented in a written contract that addresses the following items, among others:

- the nature and scope of the arrangement and services to be performed by each party to the agreement;
- appropriate performance measures and benchmarks;
- applicable record-keeping requirements;
- responsibility for compliance with anti-money laundering requirements and economic and trade sanctions administered by the Office of Foreign Assets Control;
- appropriate audit and access rights to verify compliance with the agreement and address any regulatory examination authority, including acknowledgment by the third party that its performance of functions for a bank subjects it to the jurisdiction of the federal bank regulatory agencies under the Bank Service Company Act;
- fees, costs and expenses;
- information security, confidentiality and use of the bank's information and nonpublic personal information concerning the bank's customers;
- termination rights, including a right on the part of the bank to terminate the agreement if directed by regulatory authorities;
- indemnification for breaches of representations and warranties or contractual obligations on the part of either party;
- business continuity;
- customer complaint resolution; and
- a requirement that the third party comply with applicable laws and regulations.

As a practical matter, an arrangement between a marketplace lending platform and a bank must be structured so that the bank will be regarded as the "true" lender of loans that it originates and funds through the program. The contract between the bank and the marketplace lending platform should allocate risk and responsibility for performing various functions related to loan origination in a manner consistent with the bank's role as the lender, taking into account the considerations and factors discussed in prior FinTech Flash installments and all the facts and circumstances of the relationship. A bank that participates in a marketplace lending arrangement should consider whether it faces any credit or other risks in the event that it is unable to sell loans as contemplated, and both parties should consider whether any steps taken to mitigate these risks affect the characterization of the bank as the true lender.

Further, since banks that enter into arrangements with marketplace lending platforms often sell

the loans that are originated through the relationship to the marketplace lending platform or other purchasers, there is typically one or more separate loan or receivables purchase and sale agreement(s). Loan purchasers will want to ensure that the arrangement is structured in a manner that addresses the Second Circuit's decision in Madden v. Midland Funding, LLC, which held that a provision of the National Bank Act that permits national banks to charge interest at the rate permissible for the most favored lender in the state where the bank is located does not protect an assignee of a national bank that is neither a bank nor acting on behalf of one from state usury claims. If the interest rate on the loan exceeds the rate permitted by applicable state law, then a purchaser of a loan made to a borrower in a state where Madden is controlling may not be able to enforce its rights under the loan agreement or may even be required to disgorge amounts paid by the borrower.

Some market participants have sought to address the Madden case by not purchasing loans made to borrowers in states that are part of the Second Circuit—Vermont, Connecticut and New York. Other market participants have sought to structure their loan purchase and sale arrangements in a manner that they believe will distinguish these arrangements from the facts in Madden. Madden involved a situation in which a national bank sold a loan in which it did not retain any interest, so some market participants prefer to purchase participation interests in loans in which the originating bank remains the named lender. Others have structured loan sale arrangements where the marketplace lending platform pays the originating bank trailing payments that depend upon the performance of the loan and that are intended to provide the bank with a continuing economic interest in the loan. These types of arrangements need to be carefully evaluated under all of the facts and circumstances before making any determination whether they adequately address the risks created by the Madden decision for loan purchasers.

This summary is not meant to be an exhaustive description of all of the items that may need to be addressed in an agreement between a bank and a marketplace lending platform. These types of arrangements are complex, and each arrangement must be carefully structured and documented so that it functions in the manner intended for both parties.

ABOUT GOODWIN'S FINTECH PRACTICE

Goodwin's FinTech Practice is backed by a cross-disciplinary team of approximately 70 attorneys with expertise in financial services, private equity, technology, investigations, intellectual property, consumer financial services, business and securities litigation. Having represented more than a quarter of the companies on the current *Forbes FinTech 50* list and ranked as one of the top 5 most active law firms advising on FinTech industry deals according to *PitchBook* and SNL rankings, Goodwin is a recognized market leader in the FinTech sector and serves an extensive client base on corporate, regulatory, litigation and enforcement matters.

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