Partnering-up: Structuring a successful bank partnership lending model with fintechs

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Over the last several years, banks of all sizes have successfully partnered with emerging fintech companies to offer innovative loan products to a broader range of customers. Under a typical form of this partnership, a fintech, which is subject to the policies of the partner bank, will market loan products, take and process loan applications, and will service those loans once they are funded. The bank will determine customer eligibility standards, underwrite and fund the loan, and will often sell a controlling interest back to the fintech or a third-party investor.

Partnership with a fintech gives banks a cost-effective way to leverage technology to reach new markets and satisfy the technological expectations of current customers. In turn, fintech companies benefit from a bank's existing customer base as well as the bank's experience handling the ever-increasing complexity of the regulatory environment. Customers also benefit from these partnerships by enjoying increased access to credit and convenient, internet-based channels through which to obtain credit.

Despite its benefits, this model has faced legal challenges. These partnerships often involve a partial sale of the loan to either the fintech or a third-party investor, and downstream purchasers expect to be able to receive interest at the rate agreed by the parties in the loan contract—even if the purchaser lives in a state where that interest rate might be considered usurious. Interest rate exportation rules, sometimes referred to as the "valid-when-made" doctrine, allow a loan's original interest rate to remain valid and not rendered usurious by a subsequent transfer. Some private litigants and state regulators have filed suit against fintech partners related to the banks' ability to export their home-state interest rate, including a recent notable "safe harbor" settlement in Colorado.

Recently, the FDIC and OCC have issued final rules designed to provide clarity regarding interest rate exportation, as well as rules designed to identify whether the bank is the "true lender" in a bank-partnership loan transaction. However, some Attorneys General have filed suit challenging the FDIC's and OCC's final rules. As a result, banks and their fintech partners should continue to carefully structure their partnership in a manner that tends to lower the risk of a legal challenge by regulators and private litigants. Although not an exhaustive list, banks and their partners should keep the following issues in mind when structuring their partnership:

- **The Bank is "In Charge"**
  Your partnership with a fintech company allows your bank to benefit from that company's technological expertise and access to potential new customers. However, when push comes to shove, the bank is the ultimate lender of record. Under this model, the bank should apply its underwriting standards to all loan applications received through the partnership and make the final decision regarding whether to fund the loan.

- **Apply your Compliance Program**
  The bank will almost always have more compliance expertise than its partner and will be expected by regulators to monitor its service providers. Indeed, fintech companies often depend on their bank partners to ensure compliance with the myriad state and federal laws and administrative guidance governing consumer loans. When developing a partnership, the bank should implement its compliance program to all aspects of the loan products offered through the partnership.

- **The Bank Must Have Skin in the Game**
  A critical piece of good bank balance sheet management involves selling loans. This is no different when working with fintech companies, and banks engaged in this model will often sell these loans to their fintech partners, or to third-party investors. However, in order to mitigate some of the legal risk, the bank should maintain an economic interest in the loan. Similarly, the bank should consider assuming the first payment default risk.

- **Find the Right Partner**
  There are plenty of fintech companies and loan funders looking for banks with whom to partner. Although this model provides excellent benefits for everyone involved, banks should take care to find the right partner. Look for companies that share your bank's values and goals, and who are willing to work with your bank to make sure that your business strategies are aligned.

Bank partnerships offer a prime opportunity to expand your bank's market by efficiently leveraging another company's technological expertise. And while there are certain legal challenges facing the model, there are methods to reduce risk and make the model mutually beneficial for both the bank and the fintech partner. If your bank is considering offering loan products with a partner, it would be well worth your time and energy to carefully structure your partnership.