Online Loans Across State Lines: Protecting Peer-to-Peer Lending Through the Exportation Doctrine

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INTRODUCTION

In 2005, the first online peer-to-peer lending platform appeared in the United Kingdom.[1] The premise was simple: provide a system for facilitating lending and borrowing between individuals.[2] Rather than borrow through financial institutions, borrowers were provided the opportunity to bypass those intermediaries and find individuals willing to lend through an online platform.[3] By 2006, peer-to-peer lending appeared in the United States as well.[4] Although peer-to-peer lending currently comprises a small portion of the consumer lending market, it is growing rapidly and could significantly impact the way consumers borrow money in the future.[5]

Because peer-to-peer lending is a relatively new form of lending, the regulation of peer-to-peer lending has been extensively debated.[6] Currently, peer-to-peer lending is primarily regulated by the Securities and Exchange Commission (SEC), but it is also subject to federal consumer protection laws and state regulation.[7] Due to the various laws and regulations that could apply to peer-to-peer lending platforms, prior research on this emerging industry has focused on

1. Peter Renton, *Understanding Peer to Peer Lending*, LENDACADEMY (Sept. 2015), http://www.lendacademy.com/Understanding-Peer-to-Peer-Lending.pdf [https://perma.cc/NDX4-RLKK].

2. ZOPA, http://www.zopa.com/ [https://perma.cc/N86V-W2U3].

3. *Id.*

4. Simon Cunningham, *Peer to Peer Lending Sites: An Exhaustive Review*, LENDINGMEMO (May 8, 2015), http://www.lendingmemo.com/p2p-lending-sites/ [https://perma.cc/ZPM4-N59H].

5. *See* PRICEWATERHOUSECOOPERS LLP, PEER PRESSURE: HOW PEER-TO-PEER LENDING PLATFORMS ARE TRANSFORMING THE CONSUMER LENDING INDUSTRY 2 (Feb. 2015), https://www.pwc.com/us/en/consumer-finance/publications/assets/peer-to-peer-lending.pdf [https://perma.cc/CQU9-KE8T] [hereinafter PWC REPORT].

6. *See, e.g.*, U.S. GOV'T ACCOUNTABILITY OFFICE, GAO 11–613, PERSON-TO-PERSON LENDING: NEW REGULATORY CHALLENGES COULD EMERGE AS THE INDUSTRY GROWS (July 2011), http://www.gao.gov/new.items/d11613.pdf [https://perma.cc/B47W-VQL9] [hereinafter GAO REPORT] (outlining possible regulatory approaches for peer-to-peer lending in the future); Paul Slattery, *Square Pegs in A Round Hole: SEC Regulation of Online Peer-to-Peer Lending and the CFPB Alternative*, 30 YALE J. ON REG. 233 (2013) (advocating for a new regulatory approach to peer-to-peer lending).

7. *See infra* Section III.B.

determining the most appropriate regulatory body.[8] Although there is no consensus on the proper regulator and the specific aspects of peer-to-peer lending that should be regulated, prior research generally agrees that future regulation should be designed to protect and foster the growth of the peer-to-peer lending industry.[9] In light of a recent decision in the Second Circuit,[10] this Note builds upon prior research by advocating for a new method to protect peer-to-peer lending: explicitly permitting peer-to-peer lending platforms to utilize the exportation doctrine through their relationship with state-chartered banks.

Part I of this Note outlines the lending process of two peer-to-peer lending platforms, Prosper Marketplace (Prosper) and Lending Club, and describes the relationship between these platforms and WebBank, a state-chartered bank. Part I also looks to data from Prosper and Lending Club to better understand why borrowers are using peer-to-peer lending. Part II examines peer-to-peer lending in the context of lending more generally by describing the advantages and disadvantages that peer-to-peer lending presents in comparison with traditional lending.

Part III introduces the exportation doctrine and explains how this doctrine impacts the state regulation of peer-to-peer lending platforms. Under the exportation doctrine, national and state-charted banks are permitted to "export" the interest rate laws of the state where the bank is located to transactions across the country, regardless of where the borrower resides.[11] Thus, if Prosper and Lending Club are also permitted to export interest rate limits through their partnership with a state-chartered bank, these platforms can facilitate loans on a national level without concern for the many different interest rate limits set by each individual state. However, if Prosper and Lending Club cannot rely on the doctrine, the platforms will need to comply with the various interest rate limits and procedural requirements in each individual state.

Part IV outlines a recent decision in the Second Circuit, *Madden v. Midland Funding*, which held that a nonbank debt purchaser of a loan originated by a national bank could not rely on the exportation doctrine to avoid liability for state interest rate violations.[12] This Part then explains why the reasoning of the

8. *See, e.g.*, Eric C. Chaffee & Geoffrey C. Rapp, *Regulating Online Peer-to-Peer Lending in the Aftermath of Dodd-Frank: In Search of an Evolving Regulatory Regime for an Evolving Industry*, 69 WASH. & LEE L. REV. 485 (2012) (asserting that peer-to-peer lending should be governed by multiple regulators in a similar fashion to the regulation of traditional lending institutions); Carl E. Smith, *If It's Not Broken, Don't Fix It: The SEC's Regulation of Peer-to-Peer Lending*, 6 BUS. L. BRIEF 21 (2010) (asserting that the SEC is not the appropriate regulator for peer-to-peer lending and that regulators should instead let the market develop the industry); Andrew Verstein, *The Misregulation of Person-to-Person Lending*, 45 U.C. DAVIS L. REV. 445 (2011) (asserting that the Consumer Financial Protection Bureau (CFPB), rather than the SEC, is the appropriate regulator for peer-to-peer lending).

9. *See supra* note 8.

10. Madden v. Midland Funding, LLC, 786 F.3d 246 (2d Cir. 2015). The consequences of the decision are discussed more fully in Part IV of this Note.

11. *See* 12 U.S.C. § 85 (2012); 12 U.S.C. § 1831d(a) (2012); Marquette Nat'l Bank v. First of Omaha Serv. Corp., 439 U.S. 299 (1978).

12. *Id.* at 250.

Midland Funding decision likely prevents peer-to-peer lending platforms from relying on the exportation doctrine as well.

Finally, Part V recommends that Congress or the Federal Deposit Insurance Corporation (FDIC) explicitly permit peer-to-peer lending platforms to utilize the exportation doctrine through their relationship with state-chartered banks.[13] Although opponents of this proposal may argue that the doctrine was not intended for lending platforms or that it exacerbates certain risks associated with peer-to-peer lending, the exportation doctrine is ultimately appropriate and necessary because it promotes a competitive credit market, enables peer-to-peer lending to retain its core benefits to borrowers and investors,[14] and provides certainty in the industry. Furthermore, the risks associated with peer-to-peer lending and the exportation doctrine can be addressed through additional regulation and market forces.

I. PEER-TO-PEER LENDING

Section I.A outlines the mechanics of peer-to-peer lending by explaining the lending process at the two primary peer-to-peer lending platforms in the United States, Prosper and Lending Club. It also outlines the role of WebBank, a state-chartered bank that issues the loans facilitated by Prosper and Lending Club, and explains how WebBank affects the structure of the loans. Section I.B then relies on borrower statistics from Prosper and Lending Club to better understand why borrowers are using peer-to-peer lending platforms.

A. THE PEER-TO-PEER LENDING PROCESS

Peer-to-peer lending provides individuals with the opportunity to borrow and loan money through an online platform.[15] By connecting borrowers and investors directly, these platforms allow individuals to bypass traditional financial institutions that have historically occupied the consumer lending market.[16] Although peer-to-peer lending did not introduce the concept of lending between individuals or strangers, it has changed the way in which individuals can lend

13. The FDIC has regulatory authority to interpret section 27 of the Federal Deposit Insurance Act, which allows state-chartered banks to export interest rates. *See* Elizabeth R. Schiltz, *The Amazing, Elastic, Ever-Expanding Exportation Doctrine and Its Effect on Predatory Lending Regulation*, 88 MINN. L. REV. 518, 567 (2004); *see also* Interest Charges by Interstate State Banks, Fed. Banking L. Rep. (CCH) ¶ 64–016B, 2009 WL 3692466 (May 18, 1998).

14. Individuals lending money through peer-to-peer lending platforms are referred to as "investors." *See* Prosper Funding LLC & Prosper Marketplace, Inc., Prospectus at 3 (Form 424(b)(3)) (Aug. 13, 2015) https://www.prosper.com/Downloads/Legal/Prosper_Prospectus_2015-08-13.pdf [https://perma.cc/J3JE-ZFTS] [hereinafter Prosper, Prospectus].

15. *See How It Works*, LENDINGCLUB, https://www.lendingclub.com/public/how-peer-lending-works.action [https://perma.cc/2RVR-EAFG] [hereinafter LENDINGCLUB, *How It Works*]; *How It Works*, PROSPER, https://www.prosper.com/welcome/how-it-works/ [https://perma.cc/WJQ5-F4HZ] [hereinafter PROSPER, *How It Works*].

16. *See* LENDINGCLUB, *How It Works*, *supra* note 15; PROSPER, *How It Works*, *supra* note 15.

and borrow money.[17] With the emergence of the Internet and the ease in which money can be transferred online, lending between strangers is easier than ever.[18] Because of the relative anonymity associated with online transactions, however, investors and borrowers may be less willing to engage in a loan transaction when the interaction occurs in a completely unregulated space. Both borrower and investor may be wary of fraud by the other party.[19] Peer-to-peer lending platforms, in contrast, capitalize upon the advantages of online lending with significantly less risk for the parties involved. Though concerns still exist for investors and borrowers, peer-to-peer lending platforms mitigate those concerns and instill a level of confidence in the parties involved by screening applicants and facilitating the lending process.[20]

In the United States, the two primary platforms are Prosper and Lending Club.[21] Both are for-profit companies using online platforms to facilitate personal, unsecured loans.[22] Although other for-profit platforms exist, as well as nonprofit platforms such as Kiva,[23] 98% of peer-to-peer loans in the United States occur through Prosper and Lending Club.[24] Thus, this Note focuses on the borrowing and lending process for those two platforms. Furthermore, although both platforms offer loans for business purposes, this Note focuses solely on the personal consumer loans[25] facilitated by the two platforms.

1. Prosper

Prosper, which launched in 2006 as the first peer-to-peer lending platform in the United States, allows interested individuals to borrow and lend money through an online marketplace.[26] The Prosper online marketplace is an Internet platform where borrowers can request loans and interested lenders, referred to as "investors,"[27] can then view those loan request listings and bid on

17. Slattery, *supra* note 6, at 235.

18. *See* Lisa T. Alexander, *Cyberfinancing for Economic Justice*, 4 WM. & MARY BUS. L. REV. 309, 312 (2013).

19. *See* Mary Beth Quirk, *Finding or Being a Loan Co-Signer on Craigslist Doesn't Sound like the Best Idea*, CONSUMERIST (Nov. 9, 2012), http://consumerist.com/2012/11/09/finding-a-loan-co-signer-on-craigslist-doesnt-necessarily-sound-like-the-best-idea/ [https://perma.cc/2XNE-WP86].

20. *See infra* Section II.A.

21. *See* Slattery, *supra* note 6, at 236; Verstein, *supra* note 8, at 452.

22. Slattery, *supra* note 6, at 238.

23. Kiva allows investors and borrowers to connect for socially motivated causes. The platform's mission is to "connect people through lending to alleviate poverty." *See* KIVA, http://www.kiva.org/about [https://perma.cc/QKE5-VCFE].

24. *See Banking Without Banks*, ECONOMIST (Mar. 1, 2014), http://www.economist.com/news/finance-and-economics/21597932-offering-both-borrowers-and-lenders-better-deal-websites-put-two [https://perma.cc/7UZW-4YKE].

25. *See Personal Loans*, LENDINGCLUB, https://www.lendingclub.com/public/personal-loans.action [https://perma.cc/RFA7-C2LS] [hereinafter LENDINGCLUB, *Personal Loans*]; *Personal Loans with Great Rates*, PROSPER, https://www.prosper.com/loans/ [https://perma.cc/Q8DC-ZRTM] [hereinafter PROSPER, *Personal Loans*].

26. Prosper, Prospectus, *supra* note 14, at 14; *see also* Slattery, *supra* note 6, at 238.

27. *See* Prosper, Prospectus, *supra* note 14, at 3.

them.[28] Because Prosper is only facilitating loans, rather than issuing loans, Prosper generates revenue by charging origination fees.[29] Therefore, Prosper earns money with each loan it facilitates.[30]

In order to obtain a loan, prospective borrowers must apply for a loan through Prosper, receive approval from Prosper to use the Prosper marketplace, and receive the requested loan amount from interested investors.[31] Thus, an interested borrower must first complete a loan application on the Prosper website.[32] If Prosper approves the application, the applicant may then post a loan listing on the Prosper online marketplace.[33] However, not all applicants receive approval: Prosper imposes eligibility requirements that are consistent with the underwriting criteria of WebBank, the bank that issues the loans facilitated by Prosper.[34] Furthermore, application approval does not guarantee that a borrower will be successful in obtaining the requested loan.[35] Approval simply allows the applicant to use Prosper as a platform to request a loan.[36] The borrower cannot obtain the loan until investors commit to providing the requested loan amount.[37]

If a borrower is approved to post a loan listing on the Prosper platform, the posting will include relevant information about the requested loan.[38] For example, all Prosper loans are unsecured, charge a fixed rate, and are fully amortizing.[39] The requested loan amount can range from $2,000 to $35,000, with terms of either three or five years,[40] and the annual percentage rate (APR) can range from 5.99% to 36%.[41] The amount of the loan, length of term, and APR depend on the borrower's "Prosper Rating," which is determined by Prosper and is based upon the borrower's credit score.[42] Prosper also provides

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28. *Id.*

29. *Id.* at 52. The origination fee requires the borrower to pay Prosper an upfront fee at the time the borrower receives the funds. *Id.* The origination fee at Prosper ranges from 1% to 5% of the loan, depending on the type of loan. *Id.*

30. As of June 30, 2015, Prosper had facilitated $3.9 billion in consumer loans since inception. *Id.* at 31. The company's total annual loan volume has consistently increased over time as well: Prosper facilitated $1.6 billion in consumer loans in 2014 alone. *Id.*

31. *Id.* at 3, 31–32.

32. *Id.* at 31. Any person can apply to be a borrower, as long as the person is eighteen or older, is a U.S. resident in a state where loans through Prosper are available, has a bank account, and has a social security number. *Id.* at 32.

33. Prosper, Prospectus, *supra* note 14, at 31.

34. *Id.* at 32. The applicant must: "(1) have at least a 640 credit score, (2) have fewer than seven credit bureau inquiries within the last 6 months, (3) have an annual income greater than $0, (4) have a debt-to-income ratio below 50%, (5) have at least three open trades reported on their credit report, and (6) have not filed for bankruptcy within the last 12 months." *Id.* The relationship between Prosper and WebBank is discussed more fully in Section I.A.3.

35. *See id.* at 3.

36. *Id.*

37. *Id.*

38. *See id.* at 49.

39. Prosper, Prospectus, *supra* note 14, at 31.

40. *Id.*

41. PROSPER, *Personal Loans*, *supra* note 25.

42. Prosper, Prospectus, *supra* note 14, at 3, 13, 31, 51.

other relevant information about the loan for investors viewing the listing, such as the monthly payment, the investor yield percentage, the Prosper Rating, and information about the borrower's credit history.[43]

Borrowers may also provide additional self-reported information about the loan, such as the borrower's purpose for requesting the loan, income, occupation, and employment status.[44] Prosper, however, provides no assurances that it will verify this self-reported information. The borrower's identity is verified through the borrower's credit report and other antifraud verification databases, but Prosper does not guarantee that any supplemental information will be verified.[45] Prosper will "[i]n some instances" verify income or employment information, and it will cancel a loan listing if it is unable to verify material information provided in the listing, but such verification is not guaranteed and typically does not occur until after the loan has been listed.[46] Thus, Prosper explicitly recommends in its prospectus that potential investors "not rely on an applicant's self-reported information such as income, employment status, or occupation in making investment decisions."[47]

Individuals or institutions that have passed a separate Prosper screening process may then bid on a loan posting. In order to receive approval, the investor must be at least eighteen and a U.S. resident, and must provide a social security number or, in the case of an institution, a taxpayer identification number and "entity formation documentation."[48] In certain states, investors are also subject to other restrictions related to gross income, net worth, and total amount invested.[49] Although individuals initially provided the majority of peer-to-peer loans, institutional investors are beginning to provide more loans in the peer-to-peer lending market.[50]

If an investor chooses to bid on a loan posting, the investor is not required to provide the full amount of the loan requested. Investors can provide as little as $25 in a requested loan, regardless of the amount requested by the borrower.[51] When an investor chooses to provide less than the full amount requested, the loan transaction will not occur until the borrower receives the total requested loan amount through bids from other investors.[52] Thus, a borrower may need bids from multiple investors to successfully obtain a loan. If the borrower does

43. *Id.* at 49.
44. *Id.*
45. *Id.* at 3, 12.
46. *Id.* at 3.
47. *Id.* at 12.
48. Prosper, Prospectus, *supra* note 14, at 33.
49. Additional restrictions apply to investors who are residents of Alaska, Idaho, Missouri, Nevada, New Hampshire, Virginia, Washington, or California. *Id.* at 9.
50. *See* PwC REPORT, *supra* note 5, at 2–3.
51. Prosper, Prospectus, *supra* note 14, at 3.
52. *Id.* Once an investor bids on a loan, the investor cannot revoke those funds unless the borrower's listing expires without receiving sufficient funds. *Id.*

not receive sufficient bids within a specified bidding period,[53] the borrower will not receive any funds.[54]

2. Lending Club

Lending Club entered the peer-to-peer lending industry after Prosper, but recently it has grown more successful.[55] Similar to Prosper, Lending Club offers unsecured loans ranging from $1,000 to $35,000, with terms of three or five years.[56] Loan APRs range from 5.32% to 28.99%, depending on the Lending Club rating assigned to the borrower.[57] Lending Club operates in a very similar fashion to Prosper, but it also differentiates itself in two important ways.

First, until recently, Lending Club imposed greater restrictions on potential borrowers. In 2011, in order to attract investors and foster investor confidence, Lending Club offered "higher quality" loans by strictly screening potential borrowers.[58] Prosper has since tightened its screening criteria to resemble that of Lending Club,[59] but subtle differences between the two remain. For example, although neither Prosper nor Lending Club guarantee verification of self-reported borrower income and employment, Lending Club verifies such information for 79% of borrowers.[60] In contrast, Prosper provides no data as to how often it verifies such information.[61]

Second, Lending Club has taken a more proactive approach in addressing and adapting to legal developments. For example, when Prosper received a cease-and-desist order from the SEC, Lending Club had already voluntarily registered with the SEC.[62] Additionally, Lending Club altered its relationship with WebBank,[63] the bank that issues the loans facilitated by Lending Club, in response to the

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53. The length of the bidding period cannot be greater than fourteen days. *Id.*

54. *Id.*

55. *See* Lending Club, Prospectus (Form 424(b)(3)) (Aug. 22, 2014), https://www.lendingclub.com/fileDownload.action?file=Clean_As_Filed_20140822.pdf&type=docs [https://perma.cc/5DEW-8646] [hereinafter Lending Club, Prospectus]. As of September 30, 2015, Lending Club had facilitated more than $13 billion in loans since its inception in 2008. *Lending Club Statistics*, LENDINGCLUB, https://www.lendingclub.com/info/statistics.action [https://perma.cc/9ZN5-9ML6] [hereinafter LENDINGCLUB, *Statistics*]. The annual loan volume has steadily increased as well, with $2.2 billion facilitated in the third quarter of 2015 alone. *Id.*

56. Lending Club, Prospectus, *supra* note 55, at 9.

57. *Rates and Fees*, LENDINGCLUB, https://www.lendingclub.com/public/rates-and-fees.action [https://perma.cc/F364-X9WT] [hereinafter LENDINGCLUB, *Rates and Fees*].

58. Slattery, *supra* note 6, at 241.

59. *Id.*

60. Lending Club, Prospectus, *supra* note 55, at 44–45.

61. *See* Prosper, Prospectus, *supra* note 14, at 3.

62. Slattery, *supra* note 6, at 241. The SEC has been the primary regulator of peer-to-peer lending since issuing the cease-and-desist order to Prosper in 2008. *See infra* note 175.

63. *See infra* Section I.A.3. Lending Club was the first platform to change its relationship with WebBank. It is unclear whether other lending platforms, such as Prosper, will adopt a similar model in the future. *See* Richard P. Eckman & Philip Hoffman, *Lending Club's Enhanced Relationship with WebBank Comes into Focus*, PEPPER HAMILTON LLP (Mar. 9, 2016), http://www.pepperlaw.com/publications/lending-clubs-enhanced-relationship-with-webbank-comes-into-focus-2016-03-09/ [https://perma.cc/5M22-M922].

Midland Funding decision in the Second Circuit.[64]

3. WebBank

WebBank, a state-chartered bank insured by the FDIC, originates all loans facilitated by Prosper and Lending Club.[65] Because WebBank issues the loans, the loan structure differs from that in a traditional loan. In a traditional loan, the transaction directly connects lender and borrower: a lender provides money to a borrower in exchange for a promise to repay. In a peer-to-peer loan, however, that direct connection does not exist.[66] Instead, the lending platform has two separate obligations: one with respect to the borrower and one with respect to the investor. The discussion below will first outline the relationship that Prosper and Lending Club have traditionally maintained with WebBank. It will then describe how Lending Club recently restructured this relationship.

Traditionally, both Prosper and Lending Club have relied upon WebBank to originate any loan facilitated by the lending platform, but they have also separated WebBank from the borrower receiving the loan.[67] Under this approach, when a borrower receives sufficient bids from investors, WebBank begins the loan process by issuing the loan to the borrower.[68] WebBank then "sells and assigns" the promissory note to the lending platform "without recourse,"[69] and the lending platform "permanently retains ownership of the borrower indebtedness."[70] The sale price is the principal amount of the note.[71] Then, in a separate transaction, the platform receives the principal amount from the group of investors that successfully bid on the loan.[72] Thus, the investors become creditors to the lending platform. WebBank has no obligations to the investors.[73] The platform's ability to repay the investors is contingent upon the borrower repaying the platform, but, importantly, the notes held by the investor are still the obligation of the platform rather than the borrower. Rather than a single note passing from borrower to WebBank to platform to investor, this process creates two different loans with two separate sets of notes: a note for the loan between the borrower and the platform, and a note for the loan between the platform and the investors.[74]

As result of WebBank's involvement, the investors in a peer-to-peer loan are not directly linked to the borrower, even though they are functionally acting as

64. *See* Madden v. Midland Funding, LLC, 786 F.3d 246 (2d Cir. 2015).
65. Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 3.
66. *See* Verstein, *supra* note 8, at 476–77.
67. Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 3–4, 34, 52.
68. Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 34, 52.
69. Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 52.
70. Verstein, *supra* note 8, at 477.
71. Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 34.
72. Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 4.
73. Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 3.
74. *See* Verstein, *supra* note 8, at 476–77.

the "true" lenders by providing the borrower with his or her requested funds.[75] Because the investors are creditors of the platform, the investors' ability to be repaid not only depends on the borrower's creditworthiness, but also on the platform's creditworthiness.[76] Furthermore, the investors' separation from the borrower prevents the investors from initiating debt collection if the borrower fails to repay the loan. The investors must instead rely on the platform to perform any necessary debt collection.[77]

Due to concerns created by the *Midland Funding* decision,[78] Lending Club recently announced that it is altering its relationship with WebBank in order to strengthen the connection between WebBank and the loans issued.[79] First, to connect WebBank with the borrowers using the loans, WebBank will maintain a contractual relationship with the borrower through a "Borrower Account."[80] This Borrower Account will allow peer-to-peer borrowers to apply for a loan directly from WebBank "from time to time."[81] Lending Club, however, will "service the Borrower Accounts" by delivering any necessary disclosures or information to the borrower, filing any required statements associated with the account, and holding all the documents pertaining to the account.[82] Second, to give WebBank a greater interest in the success of the loan, Lending Club will pay WebBank a "Loan Trailing Fee."[83] This will be a monthly fee that is paid as the borrower repays the loan: WebBank will not receive the full fee if the borrower fails to fully pay back the loan.[84] Ultimately, these changes were designed to ensure that WebBank maintains "an ongoing contractual relationship with borrowers" and "an on-going economic interest in all loans."[85]

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75. The risks created by the separation of investors and borrowers are discussed more fully in Section II.B.

76. *See* Verstein, *supra* note 8, at 476–77.

77. *Id.* at 455–56.

78. *See* Madden v. Midland Funding, LLC, 786 F.3d 246 (2d Cir. 2015).

79. Press Release, *Lending Club Enhances Relationship with Issuing Bank*, LENDINGCLUB (Feb. 26, 2016), http://ir.lendingclub.com/file.aspx?IID=4213397&FID=33116294 [https://perma.cc/6647-AAQP] [hereinafter LENDINGCLUB, Press Release]. This new relationship will only affect loans issued in the future. *See* Peter Rudegeair & Telis Demos, *LendingClub to Change Its Fee Model*, WALL ST. J. (Feb. 26, 2016), http://www.wsj.com/articles/fast-growing-lending-club-to-change-its-fee-model-1456488393 [https://perma.cc/6647-AAQP].

80. Lending Club, Current Report (Form 8-K) (Mar. 2, 2016), Ex. 10.2, at 2–4, http://ir.lendingclub.com/Cache/33197558.pdf?IID=4213397&FID=33197558&O=3&OSID=9 [https://perma.cc/EV35-JMX6] [hereinafter Lending Club, Current Report].

81. *Id.* at 1. WebBank, however, is not obligated to accept any applications. *Id.* at 2.

82. *Id.* at 3–4.

83. *See id.* at 1–3.

84. *Id.*; *see also* Eckman & Hoffman, *supra* note 63.

85. LENDINGCLUB, Press Release, *supra* note 79.

B. WHY BORROWERS USE PEER-TO-PEER LENDING

Although Prosper and Lending Club cannot ensure that a borrower is using the loan for the borrower's stated purpose, the borrower's stated purpose nonetheless provides insight into why the borrower is looking to peer-to-peer lending.[86] At Prosper, borrowers identified the following purposes for loans originated between July 13, 2009 and June 30, 2015: approximately 74% requested a loan for debt consolidation, 6% for home improvement, 3% for business use, and 15% for "other."[87] Lending Club reported that as of September 30, 2015, approximately 49% of its borrowers used the loans to refinance existing loans, and 19% of borrowers used the loans to pay off credit card debt.[88] The other 32% of borrowers used loans for a variety of reasons, including car financing, business, major purchases, medical expenses, home improvement, home buying, moving or relocating, vacation, and green loans.[89]

II. ADVANTAGES AND DISADVANTAGES OF PEER-TO-PEER LENDING

Peer-to-peer lending only comprises a small portion of the consumer credit market, but it has grown significantly in recent years because Prosper and Lending Club offer a new and distinct source of credit with unique benefits for borrowers and investors.[90] This Part will describe the various benefits and risks associated with peer-to-peer lending in comparison to traditional lending institutions.

A. ADVANTAGES OF PEER-TO-PEER LENDING

Peer-to-peer lending offers several important advantages in comparison to traditional lending institutions, including (1) lower interest rates for borrowers, (2) a simplified and more appealing borrower experience, (3) the ability to provide credit to a greater number of borrowers, and (4) new investment opportunities for investors.

First, peer-to-peer lending provides better interest rates for borrowers by reducing transaction costs.[91] When compared to interest rates for unsecured

86. Both Prosper and Lending Club ask borrowers to state the intended purpose of the loan request. Lending Club, Prospectus, *supra* note 55, at 41; Prosper, Prospectus, *supra* note 14, at 49.

87. Prosper, Prospectus, *supra* note 14, at 49. Prosper offers the following loan types: debt consolidation, home improvement, short-term, auto and vehicle, small business, baby & adoption, engagement ring, "special occasion," friend and family, green energy, and military. *Prosper Personal Loan Types*, PROSPER, https://www.prosper.com/loans/loan-types/ [https://perma.cc/T457-UGNU].

88. Lending Club, Prospectus, *supra* note 55.

89. *Id.* A green loan is where the borrower requests a loan for the purpose of increasing his or her energy efficiency, such as installing solar panels or building a water preservation system. *See Get a "Green Loan" for Home Improvement*, PROSPER, https://www.prosper.com/loans/loan-types/green-loans/ [https://perma.cc/T457-UGNU].

90. *See* Luc Olinga, *Peer-to-Peer Lending Is Surging in the US, and It Could Hurt Big Banks*, BUS. INSIDER (Apr. 3, 2015), http://www.businessinsider.com/afp-peer-to-peer-lending-surges-in-us-challenging-traditional-banks-2015-4 [https://perma.cc/Z2V5-QUB3].

91. Verstein, *supra* note 8, at 457–58.

personal bank loans or credit cards, peer-to-peer lending platforms offer lower interest rates for borrowers obtaining personal loans.[92] These platforms can offer lower rates because, unlike banks or other traditional financial institutions, peer-to-peer lending platforms operate online without a physical location, daily operating hours, or underwriting staff.[93] By avoiding these traditional costs, peer-to-peer lending platforms are able to pass the savings on to borrowers in the form of reduced interest rates.[94] Furthermore, many traditional lending institutions offer transactional services and lines of credit, which can be expensive for the institutions.[95] To offset these costs, the institution may bundle the costs into the borrower's interest rate when a borrower obtains a loan.[96] Peer-to-peer lending platforms, in contrast, do not provide transactional services or credit cards so there is no need to pass the costs of these products on to borrowers.[97]

The high number of borrowers using Prosper and Lending Club to consolidate other debt or reduce credit card interest also supports the conclusion that peer-to-peer lending interest rates are better than the alternatives.[98] According to a survey conducted by Lending Club in 2015, borrowers using personal loans through Lending Club to consolidate debt or pay off credit card interest reported that the interest rate on their Lending Club loan was on average 7.4% lower than the interest rate on their outstanding debt or credit card balance.[99]

Second, peer-to-peer lending provides a simplified experience that is more appealing for borrowers.[100] A traditional bank loan may be complicated to the average, or even sophisticated, borrower: banks may attempt to bundle together several different financial products,[101] there may be several different contracts,[102] and the disclosures can be overwhelming.[103] As borrowers become less trusting of traditional banks and the complicated procedures associated with

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92. Slattery, *supra* note 6, at 243. Prosper offers loans with an APR as low as 5.99% for borrowers with the best credit rating, and Lending Club offers loans with an APR as low as 5.32%. *See* PROSPER, *Personal Loans*, *supra* note 25; LENDINGCLUB, *Rates and Fees*, *supra* note 57. In the second quarter of 2015, the average interest rate for a three-year loan at Lending Club was only 11.25%, whereas the average credit card interest rate in January of 2016 was more than 15.6%. *See Demand & Credit Profile*, LENDINGCLUB, https://www.lendingclub.com/info/demand-and-credit-profile.action [https://perma.cc/AP6Z-NNUW] [hereinafter LENDINGCLUB, *Demand & Credit Profile*]; *Current Interest Rates*, BANKRATE, http://www.bankrate.com/finance/credit-cards/current-interest-rates.aspx [perma.cc/5Z8W-KAHB].

93. Slattery, *supra* note 6, at 242; Verstein, *supra* note 8, at 457–58.

94. Slattery, *supra* note 6, at 242; Verstein, *supra* note 8, at 457–58.

95. Verstein, *supra* note 8, at 458.

96. *Id*.

97. *Id.*

98. *See* Lending Club, Prospectus, *supra* note 55; Prosper, Prospectus, *supra* note 14, at 49.

99. LENDINGCLUB, *Personal Loans*, *supra* note 25.

100. Verstein, *supra* note 8, at 462–63.

101. *Id.* at 457–58.

102. *Id.* at 462–63.

103. *See generally* Ben-Shahar & Schneider, *The Failure of Mandated Disclosure*, 159 U. PA. L. REV. 647 (2011) (explaining that the failure of mandated disclosure is in part attributable to the large amount of disclosure, which may cause disclosees to become overwhelmed).

obtaining a loan,[104] it is vital that borrowers have a safe and appealing alternative. Although peer-to-peer lending platforms also provide federally required disclosures to borrowers,[105] the loan process itself is simpler and less intimidating: there are no other products offered, there is a single standardized contract, and the website is simple and easy to understand.[106] A borrower simply needs to determine the amount of money he or she needs and the length of time he or she needs to pay the money back.[107] After providing basic information, the borrower can quickly learn the applicable interest rate.[108] Once the borrower submits the application and is approved, he or she can then easily track the amount of money that investors are providing.[109] This simplicity not only makes the platform more appealing, but also reduces the risk that the borrower will misunderstand the terms of the loan.[110]

Third, peer-to-peer lending provides a greater and more diverse number of borrowers with access to credit.[111] Traditional lending institutions have been heavily criticized for offering little or no credit to residents of certain geographic areas because of the racial or ethnic composition of those neighborhoods, a practice known as redlining.[112] Although such a practice is now illegal, redlining problems continue to persist.[113] Additionally, even if lenders comply with antiredlining and other antidiscrimination laws, these laws are unlikely to "address the economic, geographic, and social isolation that precludes many borrowers from participating in mainstream markets."[114] More specifically, if a particular region or community presents a substantial credit risk, the lender may be legally permitted to restrict credit in that region or community on an economic basis. Providing credit within the area may present too great a risk of default, or the transaction costs associated with finding the few credit worthy borrowers may be too high.[115]

In contrast, by looking to peer-to-peer lending platforms, those credit worthy borrowers in marginalized areas can access the credit they need.[116] Unlike traditional lending, peer-to-peer lending occurs entirely online, thus allowing peer-to-peer lending platforms to connect borrowers and investors from across

104. *See* Ronald J. Mann, *After the Great Recession: Regulating Financial Services for Low- and Middle-Income Communities*, 69 WASH. & LEE L. REV. 729, 743–44 (2012).

105. *See infra* note 175.

106. *See* Verstein, *supra* note 8, at 462–63; LENDINGCLUB, *How It Works*, *supra* note 15.

107. LENDINGCLUB, *How It Works*, *supra* note 15.

108. PWC REPORT, *supra* note 5, at 3–4.

109. *Id.*

110. *See* Verstein, *supra* note 8, at 462–63.

111. GAO REPORT, *supra* note 6, at 18.

112. *See* Alexander, *supra* note 18, at 315–19.

113. Emily Badger, *Redlining: Still a Thing*, WASH. POST, May 28, 2015, http://www.washingtonpost.com/news/wonkblog/wp/2015/05/28/evidence-that-banks-still-deny-black-borrowers-just-as-they-did-50-years-ago/ [https://perma.cc/LG5N-2U8P].

114. *See* Alexander, *supra* note 18, at 343.

115. *Id.*

116. *Id.* at 336–337; Chaffee & Rapp, *supra* note 8, at 505.

the country without any geographic limitations.[117] The online nature of peer-to-peer lending neutralizes the risk of geographic marginalization: traditional lending institutions may overlook credit worthy borrowers who reside in poor economic areas, whereas peer-to-peer investors will consider every borrower through an online platform, regardless of where the borrower resides.[118] Additionally, unlike a typical loan involving a face-to-face interaction between lender and borrower, the relative anonymity of borrower and investor in peer-to-peer lending can also reduce the risk of discriminatory lending.[119]

Peer-to-peer lending platforms can also provide an important source of credit for borrowers when traditional financial institutions become more reluctant to lend.[120] Although peer-to-peer lending was introduced in the United States before 2007, peer-to-peer lending platforms did not experience significant growth until the recession of 2007.[121] When traditional lenders restricted credit access due to economic conditions, peer-to-peer lending continued to provide money for a wide range of borrowers in need of credit.[122] Thus, when the consumer credit market unexpectedly weakens, peer-to-peer lending can provide a certain level of protection for borrowers because its success is not necessarily linked to advantageous economic conditions.[123]

Fourth, peer-to-peer lending also offers several advantages for investors.[124] For example, the various reduced transaction costs in peer-to-peer lending not only result in lower interest rates for borrowers, but "solid returns" for investors as well.[125] Furthermore, peer-to-peer lending offers a new investment vehicle that allows investors to diversify their investment portfolio.[126] Additionally, investors can reduce risk within the peer-to-peer lending market by investing money across many different borrowers.[127] Peer-to-peer lending platforms also allow investors to download and search through borrower loan data so as to

117. *See* Alexander, *supra* note 18, at 336–37.

118. Chaffee & Rapp, *supra* note 8, at 505.

119. *See id.*; Slattery, *supra* note 6, at 244.

120. *See* Alexander, *supra* note 18, at 336–37.

121. *See* Slattery, *supra* note 6, at 235.

122. Chaffee & Rapp, *supra* note 8, at 503–04.

123. Slattery, *supra* note 6, at 244.

124. *Id.* at 243.

125. *See* LENDINGCLUB, *How It Works*, *supra* note 15; Slattery, *supra* note 6, at 243. At Lending Club, investors have received, on average, adjusted net annualized returns between 5.14% and 9.04%, depending on the credit rating of the borrower. LENDINGCLUB, *Demand & Credit Profile*, *supra* note 92. In comparison, in January of 2016, the yield curve rate on a government bond was under 1.75% for a five-year bond and under 1.4% for a three-year bond. *See Daily Treasury Yield Curve Rates for January, 2016*, U.S DEP'T TREASURY, https://www.treasury.gov/resource-center/data-chart-center/interest-rates [https://perma.cc/PWC7-N7SP] (under "Select Time Period, select "2016").

126. Peer-to-peer loans allow for investors to balance an investment portfolio that has a high number of investments in large institutions. *See* Jack R. Magee, *Peer-to-Peer Lending in the United States: Surviving After Dodd-Frank*, 15 N.C. BANKING INST. 139, 143–44 (2011).

127. *See* Prosper, Prospectus, *supra* note 14, at 3.

evaluate all potential borrowers on the platform at minimal cost.[128]

B. DISADVANTAGES OF PEER-TO-PEER LENDING

Although peer-to-peer lending offers many benefits, risks still exist. In addition to the risks associated with any loan, peer-to-peer lending potentially creates certain disadvantages in comparison to traditional lending institutions, including (1) greater risk of borrower fraud, (2) limited recourse for investors, (3) investor dependence on the creditworthiness of the platform, and (4) institutional investors using the platform to circumvent regulation.

First, there can be greater risk of borrower fraud in peer-to-peer lending because much of the information provided by the borrower may be unverified.[129] Unlike a personal loan at a traditional financial institution, where the lender will verify the borrower's employment and financial situation,[130] peer-to-peer investors may be providing money to borrowers who are not accurately describing their employment, income, or purpose of the loan.[131] If a borrower misrepresents his or her ability to pay the loan back, the investor's risk may be greater than he or she realizes.[132] The risk of borrower fraud then creates a greater risk of borrowers defaulting.

The relatively low default rates at Lending Club and Prosper, however, may indicate that incidents of borrower fraud in peer-to-peer lending are rare. In 2014, for example, Lending Club reported a default rate of 5% for three-year loans originated in 2010.[133] Based on Lending Club's data after 2010, analysts estimate that the default rate will remain at approximately 5% in the future.[134] Although Prosper reported a default rate of 7.49% for three-year loans originated in 2010, analysts estimate that Prosper's default rate in the future will be closer to Lending Club's default rate because Prosper subsequently changed its criteria for accepting borrower applications to resemble that of Lending Club's.[135] The risk of borrower fraud may be mitigated by the strict standards that Prosper and Lending Club currently apply for applicants: only approximately 10% of loan applications are approved.[136]

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128. Slattery, *supra* note 6, at 242; *Download Data*, LENDINGCLUB, https://www.lendingclub.com/info/download-data.action [https://perma.cc/27TL-YCWR].

129. *See* Lending Club, Prospectus, *supra* note 55, at 44–45; Prosper, Prospectus, *supra* note 14, at 3, 12.

130. *See, e.g.*, *Applying for Your Loan*, BANK OF AMERICA, https://www.bankofamerica.com/home-loans/refinance/applying-for-refinance/apply-for-your-refinance-loan.go [https://perma.cc/6FD2-FAZU].

131. *See* Prosper, Prospectus, *supra* note 14, at 3, 12.

132. Verstein, *supra* note 8, at 467.

133. Simon Cunningham, *Default Rates at Lending Club & Prosper: When Loans Go Bad*, LENDINGMEMO (Oct. 17, 2014), http://www.lendingmemo.com/lending-club-prosper-default-rates/ [https://perma.cc/6RUA-VV59].

134. *Id.*

135. *Id.*

136. Alexandra Mateescu, *Peer-to-Peer Lending*, DATA & SOC'Y RES. INST. 21 (July 1, 2015), http://www.datasociety.net/pubs/dcr/PeertoPeerLending.pdf [https://perma.cc/XGA5-ZBNB].

Second, investor recourse is limited if the borrower fails to repay because the loans are unsecured[137] and investors must rely on the lending platforms if debt collection is necessary.[138] Because of the loan structure,[139] the investor cannot collect any debt directly from the borrower.[140] Instead, the investor must rely on the "commercially reasonable" efforts of the platform or a third party debt collector, as designated by the platform.[141] Although peer-to-peer lending platforms retain a percentage of the debt recovered,[142] the platforms do not have the same financial incentive as the investors to vigorously conduct debt collection because the platforms are not bearing the loss.[143] The investors only profit when the borrower fulfills his or her obligations, whereas the lending platform profits when a loan is originated, regardless of whether the borrower subsequently fulfills his or her obligation to repay the investor.[144] Due to the "mismatched incentives" between platforms and investors,[145] the platforms have been described as "notoriously bad" at collecting debt.[146]

The concerns over mismatched incentives are at least partially mitigated, however, by the peer-to-peer lending platforms' desire to attract investors.[147] Because the entire peer-to-peer lending industry is dependent upon willing investors, platforms have a strong incentive to ensure that investors are satisfied and willing to provide credit in the future.[148] Fostering investor confidence is critical to platform success: Lending Club became a more popular platform than Prosper by screening borrowers more rigorously so as to offer "higher quality" loans for investors.[149] Thus, even if Prosper and Lending Club do not have a direct financial stake in the payment of each loan, they have a significant stake in the success of the loan because their ability to find willing investors may depend upon it.

Third, unlike a traditional loan where the risk of default simply depends on the creditworthiness of the borrower, the risk of default for a peer-to-peer investor depends on both the creditworthiness of the borrower and the peer-to-peer lending platform.[150] Because the lending platform purchases the borrower's loan from WebBank, then sells a separate note to the investor, the investor

137. *See* Lending Club, Prospectus, *supra* note 55, at 9; Prosper, Prospectus, *supra* note 14, at 31.
138. *See* Verstein, *supra* note 8, at 455–56.
139. *See supra* Section I.A.3.
140. Lending Club, Prospectus, *supra* note 55, at 12.
141. Lending Club, Prospectus, *supra* note 55, at 54.
142. Lending Club, Prospectus, *supra* note 55, at 54 (reserving the right to retain up to 35% of the amount recovered); Prosper, Prospectus, *supra* note 14, at 53 (reserving the right to retain "[u]p to 40% of the amount recovered").
143. Verstein, *supra* note 8, at 470.
144. Verstein, *supra* note 8, at 468.
145. Slattery, *supra* note 6, at 246–47.
146. Chaffee & Rapp, *supra* note 8, at 506.
147. Slattery, *supra* note 6, at 246–47.
148. *Id.*
149. *Id.* at 241.
150. Verstein, *supra* note 8, at 477.

is a creditor of the platform.[151] Thus, the investor's ability to be repaid not only depends on the creditworthiness of the borrower, but the platform as well. This platform risk may be considerable, given the recent financial difficulties of peer-to-peer lending platforms: Prosper and Lending Club have consistently experienced net operating losses and both have a significant amount of debt.[152] If either or both of these platforms were to go bankrupt, an investor would be at significant risk of losing his or her investment, regardless of the borrower's financial situation.

Fourth, institutional investors may be lending in the peer-to-peer industry[153] to circumvent banking regulations, which could create risks for the nation's economy on a broader scale. Although the peer-to-peer lending industry supports the emergence of institutional investors by claiming that their presence increases competition and reduces interest rates for borrowers,[154] there are risks accompanying this trend. In a 2011 report on peer-to-peer lending, the U.S. Government Accountability Office (GAO) warned that institutional investors could create regulatory concerns.[155] Because the peer-to-peer lending industry is less regulated than the traditional finance industry,[156] there is a concern that institutions can circumvent applicable laws and regulations by lending through platforms such as Prosper and Lending Club.[157] For example, banks and other traditional lending institutions are subject to certain capital and reserve regulations that require banks to hold a certain portion of the bank's deposits in reserve.[158] Institutional investors using peer-to-peer lending platforms, in contrast, are not subject to such requirements.[159]

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151. *See id.* at 476–77.

152. Slattery, *supra* note 6, at 250. For example, Lending Club, a platform that has experienced significant and steady growth in loans facilitated recently, has nonetheless been operating at a loss and reported an accumulated deficit of $66.8 million as of June 30, 2014. Lending Club, Prospectus, *supra* note 55, at 14. In 2015, Prosper reported that it "has incurred annual operating losses since its inception," including a loss of $4.9 million in the first six months of 2015 alone. Prosper, Prospectus, *supra* note 14, at 22. Prosper reported an accumulated deficit of $134.4 million as of June 30, 2015. *Id.*

153. Reports have consistently found that institutions are entering the peer-to-peer lending market as investors. *See* Mateescu, *supra* note 136, at 2; PwC REPORT, *supra* note 5. *The New York Times* also reported that large financial institutions funded more than eighty percent of the loans issued through Prosper in March of 2014. Amy Cortese, *Loans That Avoid Banks? Maybe Not*, N.Y. TIMES, May 3, 2014, http://www.nytimes.com/2014/05/04/business/loans-that-avoid-banks-maybe-not.html?_r=0 [https://perma.cc/MV28-CZJB].

154. Cortese, *supra* note 153.

155. GAO REPORT, *supra* note 6, at 55.

156. Matt Scully & Tracy Alloway, *People Have Some Interesting Thoughts About Peer-to-Peer Lending*, BLOOMBERG (Oct. 29, 2015), http://www.bloomberg.com/news/articles/2015-10-29/people-have-some-interesting-thoughts-about-peer-to-peer-lending [https://perma.cc/K739-257Y].

157. *Id.*

158. Verstein, *supra* note 8, at 458–59.

159. *Id.* at 59.

III. THE EXPORTATION DOCTRINE AND STATE REGULATION

Due to their relationship with WebBank,[160] Prosper and Lending Club have previously used the exportation doctrine to "export" the state interest rate laws in Utah, where WebBank is located, to transactions across the country. Section III.A will describe the exportation doctrine and how the doctrine benefits Prosper and Lending Club. Section III.B will then outline the significant state regulation that Prosper and Lending Club would be subject to if the exportation doctrine is no longer available for peer-to-peer lending platforms.[161]

A. THE EXPORTATION DOCTRINE

Prosper and Lending Club's relationship with WebBank allows the platforms to benefit from certain protections afforded to national and state-chartered banks. Under section 85 of the National Bank Act (NBA), national banks are entitled to certain protections from state laws that might disadvantage national banks.[162] Section 85 of the NBA permits a national bank to impose the highest interest rate allowed to any type of lender within the state where the national bank is located.[163] This is known as the "most favored lender doctrine."[164]

The scope of section 85 was broadened in 1978 when *Marquette National Bank v. First of Omaha Service Corporation* introduced the exportation doctrine.[165] The Supreme Court held that under section 85 of the NBA, national banks can "export" the laws of the state where the bank is located to loans across the country, regardless of where the borrower resides.[166] Thus, a national bank can only be liable for violating state usury laws if it charges an interest that exceeds the usury laws of its home state.[167] If a national bank is located in a state with no interest rate limits, that bank can charge any interest rate to borrowers from any state, even if the interest rate exceeds the rate limit in the borrower's state of residence.

Shortly after *Marquette*, in order to ensure that section 85 of the NBA did not unfairly disadvantage state-chartered banks, Congress enacted section 27 of the Federal Deposit Insurance Act (FDIA).[168] Section 27 likewise allows state-chartered banks to utilize the exportation doctrine and export the interest rate

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160. *See supra* Section I.A.3.

161. The ability of peer-to-peer lending platforms to use the exportation doctrine is in significant doubt after *Madden v. Midland Funding, LLC*, 786 F.3d 246 (2d Cir. 2015). *See infra* Part IV.

162. *See* 12 U.S.C. § 85 (2012).

163. *See* Tiffany v. Nat'l Bank of Mo., 85 U.S. 409, 411–13 (1873).

164. Schiltz, *supra* note 13, at 544–45.

165. 439 U.S. 299 (1978).

166. *See id.* at 299, 309–13.

167. A usury law limits the amount of interest a lender can charge on a loan. *Usury Laws*, WASH. STATE DEP'T FIN. INSTS., http://dfi.wa.gov/financial-education/information/usury-law [https://perma.cc/PX8S-KEKZ].

168. 12 U.S.C. § 1831d(a) (2012). Section 27 of the FDIA was included through section 521 of the Depository Institution Deregulation and Monetary Control Act of 1980, Pub. L. 96-221, 94 Stat. 132 (1980).

laws of their home states to loans across the country.[169]

As a state-chartered and federally insured bank, WebBank is entitled to utilize the exportation doctrine through section 27 of the FDIA.[170] By partnering with WebBank and issuing loans through WebBank, Prosper and Lending Club have also utilized the exportation doctrine in loan transactions.[171] Because Utah, where WebBank is located, has no limit on interest rates,[172] Prosper and Lending Club have been permitted to charge interest on any loan across the country without concern for state law usury claims, even if the rate exceeded the usury laws in the investor's or borrower's state of residence.[173] Due to the *Midland Funding* decision in the Second Circuit, however, there is significant doubt as to whether Prosper and Lending Club will be permitted to continue utilizing the exportation doctrine in the future.[174]

B. STATE REGULATION

Although the exportation doctrine does not affect federal regulation of peer-to-peer lending platforms, such as SEC and Consumer Financial Protection Bureau (CFPB) regulation,[175] the doctrine does allow Prosper and Lending Club to connect investors and borrowers on a national scale without concern for variations in individual state lending regulations.[176] If Prosper and Lending Club can no longer use the doctrine, these platforms will need to consider (1) the varying interest rate limits within each individual state where the platform offers loans, as well as (2) the procedural requirements for licensed lenders within each of those states.[177]

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169. *See* 12 U.S.C. § 1831d(a) (2012).

170. Lending Club, Prospectus, *supra* note 55, at 31; Prosper, Prospectus, *supra* note 14, at 82.

171. Lending Club, Prospectus, *supra* note 55, at 31; Prosper, Prospectus, *supra* note 14, at 27.

172. UTAH CODE ANN. § 15-1-1(1) (LexisNexis 2015) ("The parties to a lawful contract may agree upon any rate of interest for the loan or forbearance of any money, goods, or chose in action that is the subject of their contract.").

173. *See* Lending Club, Prospectus, *supra* note 55, at 31; Prosper, Prospectus, *supra* note 14, at 82.

174. *See infra* Part IV.

175. The SEC has been the primarily regulator of peer-to-peer lending since 2008, when it issued a Cease-and-Desist Order to Prosper. Prosper Marketplace, Inc., Exchange Act Release No. 8984, 94 SEC Docket 1913 (Nov. 24, 2008). The Order characterized the loans offered through Prosper as securities, and therefore required Prosper to register with the SEC as a seller of securities. *Id.* Additionally, because WebBank issues the peer-to-peer loans on behalf the lending platforms, the loans are subject to consumer protection laws and regulations. *See* Lending Club, Prospectus, *supra* note 55, at 33–34; Prosper, Prospectus, *supra* note 14, at 82–84. Although the rules and regulations apply to WebBank, Prosper and Lending "facilitate compliance." Prosper, Prospectus, *supra* note 14, at 82. Thus, Prosper and Lending Club make necessary disclosures and comply with relevant consumer protection rules and regulations, such as the Truth-in-Lending Act, 15 U.S.C. § 1601 (2012), and the Equal Credit Opportunity Act, 15 U.S.C. § 1691 (2012). *See* Lending Club, Prospectus, *supra* note 55, at 33; Prosper, Prospectus, *supra* note 14, at 82–84.

176. *See* Lending Club, Prospectus, *supra* note 55, at 31; Prosper, Prospectus, *supra* note 14, at 82.

177. *See* Lending Club, Prospectus, *supra* note 55, at 31.

First, without the exportation doctrine, peer-to-peer lending platforms will need to consider variations in state interest rate limits.[178] Although some states allow lenders to charge any interest rate without violating state law,[179] many states have usury statutes to limit the interest rates that lenders can charge.[180] For example, in New York, lenders may not charge an interest rate greater than 16% to borrowers residing in New York unless the lender is licensed to do so.[181] Even if a lender obtains a New York license, the lender cannot charge an interest rate greater than 25% and can only charge an interest rate greater than 16% if the loan meets certain conditions.[182] A person who knowingly "charges, takes or receives" an interest rate greater than 25% will be criminally liable.[183]

Second, without the exportation doctrine, peer-to-peer lending platforms may need to obtain a lending license in each state where the platform offers loans, which will require compliance with various licensing requirements.[184] Typically, in order to offer loans in a particular state, a lender must obtain a license and comply with the rules and regulations of that particular state.[185] State regulation of licensed lenders, however, is not uniform. State regulation can vary in recordkeeping requirements, disclosure requirements, permissible loan origination procedure, and advertisement restrictions, among other requirements.[186] For example, in order to obtain lending license in New York, a lender must file an application and certify details about the company's background, compliance with fair lending, litigation involvement, financial statements, and other information.[187] Furthermore, as a licensed lender in New York, the lender is subjected to various state regulations, including Superintendent inspection of the lender's accounts and records, and restrictions on certain types of loans and

178. State interest rate laws are not uniform. *See Usury Laws by State, Interest Rate Caps, The Bible & More*, CARDHUB (June 20, 2014), http://www.cardhub.com/edu/usury-laws/ [https://perma.cc/TQL8-PNRG] (describing how interest rate limits vary by state).

179. *See, e.g.*, S.D. CODIFIED LAWS § 54-3-1.1 (2015) ("Unless a maximum interest rate or charge is specifically established elsewhere in the code, there is no maximum interest rate or charge, or usury rate restriction between or among persons, corporations, limited liability companies, estates, fiduciaries, associations, or any other entities if they establish the interest rate or charge by written agreement."). Of the forty-six jurisdictions where peer-to-peer lending platforms are permitted to facilitate loans, seven have no limit on interest rates for consumer loans: Arizona, Nevada, New Hampshire, New Mexico, South Carolina, South Dakota, and Utah. *See* Lending Club, Prospectus, *supra* note 55, at 31.

180. *See, e.g.*, CAL. CONST. art. XV, § 1(1) (imposing a maximum interest rate of 10% for personal loans for non-exempt lenders); KY. REV. STAT. ANN. § 360.010(1) (West 2015) (imposing a default interest rate limit of 8%, or a maximum of 19% as contracted by the parties, for loans under $15,000).

181. N.Y. BANKING LAW § 14-a (McKinney 2015).

182. The loan must be "in the principal amount of twenty-five thousand dollars or less for any loan to an individual for personal, family, household, or investment purposes and in a principal amount of fifty thousand dollars or less for business and commercial loans." *Id.* § 340.

183. N.Y. PENAL LAW § 190.40 (McKinney 2015).

184. *See* Lending Club, Prospectus, *supra* note 55, at 31.

185. *See, e.g.*, *Information and Resources for Licensed Lenders*, N.Y. DEP'T FIN. SERVS., http://www.dfs.ny.gov/banking/licensedlender.htm [https://perma.cc/S52X-8B2N] [hereinafter N.Y. Licensing Information] (outlining the various rules and regulations that New York lenders are subjected to).

186. Prosper, Prospectus, *supra* note 14, at 82.

187. *See* N.Y. BANKING LAW § 341 (McKinney 2015); N.Y. Licensing Information, *supra* note 185.

forms of compensation.[188]

Therefore, based on the lending laws of a state such as New York, Prosper and Lending Club could be liable for charging impermissible interest rates to some New York borrowers. Prosper and Lending Club both offer loans exceeding 25%,[189] thus exposing the platforms to criminal usury liability in New York.[190] Even if Prosper and Lending Club wished to issue loans in New York at interest rates below 25%, but above the civil usury limit of 16%, they would need to obtain a license.[191] Obtaining a license, however, would require significant disclosure through license applications and would subject the platforms to various state regulations.[192] Such a process would also affect the way these platforms issue loans. For example, even with a license, Prosper and Lending Club could only charge above 16% interest for personal loans under $25,000:[193] both platforms currently offer loans in excess of that amount.[194] Thus, without the ability to export the state usury laws of Utah through WebBank, Prosper and Lending Club would face one of two consequences: exposure to significant civil and criminal usury liability or exposure to a burdensome licensing process that would also restrict the platforms' current lending model.[195]

IV. RECENT LEGAL DEVELOPMENT: *MADDEN V. MIDLAND FUNDING*

By partnering with WebBank, a state-chartered and FDIC insured bank, Prosper and Lending Club have utilized the exportation doctrine to export the interest rate laws of Utah to loan transactions throughout the country.[196] The ability of peer-to-peer lending platforms to continue this practice, however, is at risk after the *Midland Funding* decision in the Second Circuit.[197] This Part will outline the holding and reasoning of that decision, and will then explain why the reasoning likely prevents peer-to-peer lending platforms from using the exportation doctrine in the future.

A. *MADDEN V. MIDLAND FUNDING*

The NBA and FDIA permit national and state-chartered banks to export interest rates, but they do not address whether nonbank entities are entitled to

188. *See* N.Y. BANKING LAW §§ 340–61 (McKinney 2015).

189. *See* LENDINGCLUB, *Rates and Fees*, *supra* note 57; PROSPER, *Personal Loans*, *supra* note 25.

190. New York is not alone in imposing an interest rate limit that is below the highest interest rate offered on Prosper and Lending Club. *See, e.g.*, CAL. CONST. art. XV, § 1(1) (imposing a maximum interest rate of 10% for personal loans for nonexempt lenders); KY. REV. STAT. ANN. § 360.010(1) (West 2015) (imposing a default interest rate limit of 8%, or a maximum of 19% as contracted by the parties, for loans under $15,000).

191. *See* N.Y. BANKING LAW §§ 14-a, 340 (McKinney 2015).

192. *See id.* §§ 340–61.

193. *See id.* § 340.

194. *See* Lending Club, Prospectus, *supra* note 55, at 9; Prosper, Prospectus, *supra* note 14, at 31.

195. *See* Lending Club, Prospectus, *supra* note 55, at 31; Prosper, Prospectus, *supra* note 14, at 27.

196. *See* Lending Club, Prospectus, *supra* note 55, at 31; Prosper, Prospectus, *supra* note 14, at 82.

197. Madden v. Midland Funding, LLC, 786 F.3d 246 (2d Cir. 2015).

export interest rates when they hold loans originated by national or state-chartered banks.[198] In *Madden v. Midland Funding*, the Second Circuit addressed that issue when a nonbank entity sought the protection and benefits of the NBA after purchasing a debt that originated with a national bank.[199] Relying on the NBA, the debt purchaser, Midland Funding, sought to charge an interest rate that was permissible in the state where the national bank was located, but was impermissible in New York, where the borrower was located.[200] Although Midland Funding was a nonbank entity, it argued that the NBA still protected the loan from New York usury laws because the loan was issued by a national bank.[201] The Second Circuit rejected Midland Funding's argument, instead holding that Midland Funding was not protected from New York usury liability.[202]

In so holding, the court reasoned that applying state usury law to Midland Funding "would not significantly interfere with any national bank's ability to exercise its powers under the NBA."[203] The court did note that NBA protection applies to non-national bank entities acting on behalf of a national bank.[204] But the critical distinction, according to the court, was that Midland Funding was not acting on behalf of any national bank: once the national bank sold the loan to Midland Funding, it no longer possessed any interest or involvement in the loan.[205] Because the loan held by Midland Funding no longer had any connection to the national bank, granting NBA protection was not appropriate.[206] Furthermore, the court noted that allowing debt purchasers to claim NBA protection "would be an overly broad application of the NBA . . . [and] would

198. *See* 12 U.S.C. §§ 85, 1831d(a) (2012).

199. 786 F.3d at 247. The debt at issue was a defaulted credit card account. *Id* at 247–48. For purposes of this Note, the credit extended to the borrower will be referred to as a "loan."

200. *Id.* at 247–48.

201. *Id.* at 250. Such protection would be available through the exportation doctrine. *See supra* Section III.A.

202. *Id.* at 250–52. The debt holder, Midland Funding, petitioned for an *en banc* rehearing, but was denied the petition on August 12, 2015. Order, Madden v. Midland Funding, LLC, No. 14-2131 (2d Cir. Aug. 12, 2015). Midland Funding filed a petition for writ of certiorari with the United States Supreme Court on November 10, 2015. Petition for Writ of Certiorari, Madden v. Midland Funding, LLC, No. 15-610 (U.S. Nov. 10, 2015). The Supreme Court invited the Solicitor General to file a brief that expressed the view of the United States. *See* Midland Funding, LLC v. Madden, No. 15-610, 136 S. Ct. 1484 (Mem.) (Mar. 21, 2016). The Solicitor General responded by characterizing the Second Circuit's decision as "incorrect." Brief for the United States as Amicus Curiae at 6, Midland Funding, LLC v. Madden, No. 15-610 (U.S. May 24, 2016). However, the Solicitor General took the position that "the petition for a writ of certiorari should be denied" on the grounds that the particular case presented a "poor vehicle for resolution of the question presented." *Id.* at 1, 13–20 (explaining that a circuit split did not exist, the parties failed to present important preemption arguments at the district court level, and Midland Funding could still prevail on remand). On June 27, 2016, the Supreme Court denied Midland Funding's petition for writ of certiorari. Midland Funding, LLC v. Madden, No. 15-610, 2016 WL 3461580 (Mem.) (U.S. June 27, 2016).

203. *Midland Funding*, 786 F.3d at 249.

204. *Id.* at 251.

205. *See id.* at 251–53.

206. *See id.*

create an end-run around usury laws."[207]

B. *MIDLAND FUNDING* LIKELY APPLIES TO PEER-TO-PEER LENDING PLATFORMS

Although the *Midland Funding* decision only addressed debt purchasers, the reasoning of the decision likely applies to peer-to-peer lending platforms as well. Prosper and Lending Club may not be debt purchasers, but their lending model and relationship with WebBank is very similar to the loan purchase process utilized by Midland Funding. Just as Midland Funding purchased a loan from a national bank,[208] Prosper and Lending Club purchase each loan they provide from WebBank.[209] And just as the national bank in *Midland Funding* no longer maintained an interest in the loan after selling it,[210] WebBank traditionally has not maintained any interest in the loans purchased by Prosper and Lending Club.[211] WebBank originates the loans, but its involvement ends there because it maintains no obligations to the borrowers or investors.[212] Thus, there is not a strong justification for extending NBA or FDIA protection to peer-to-peer lending platforms as a matter of statutory interpretation. Under the reasoning of *Midland Funding*, preventing these platforms from utilizing the exportation doctrine would not significantly interfere with WebBank's ability to exercise its powers under the FDIA.[213]

Additionally, just as the Second Circuit was concerned with debt purchasers abusing their relationship with national banks to circumvent state usury laws,[214] there is a concern that lending platforms will abuse the exportation doctrine to circumvent state usury laws and charge oppressive interest rates. If a lending platform can avoid statutory usury liability by merely originating its loans through a state-chartered bank, then other online lenders may also partner with banks in states such as Utah, where is there is no interest rate limit, in order to charge high interest rates across the country.[215]

C. ARGUMENTS FOR LIMITING THE SCOPE OF *MIDLAND FUNDING*

The reasoning underlying *Midland Funding* appears to cover peer-to-peer lending, but there are still arguments for why the decision should not apply. Peer-to-peer lending platforms attempting to limit the scope of *Midland Fund-*

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207. *Id.* at 251–52.

208. Madden v. Midland Funding, LLC, 786 F.3d 246, 248 (2d Cir. 2015).

209. *See* Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 3, 52.

210. 786 F.3d at 251–53.

211. *See* Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 3, 52.

212. WebBank continues to maintain no obligations to borrowers or investors using Prosper. *See* Prosper, Prospectus, *supra* note 14, at 3. Additionally, even after Lending Club's recently restructured relationship with WebBank, which provides WebBank with an ongoing interest in the loans it issues and sells, the *Midland Funding* decision may still apply to Lending Club. *See infra* Section IV.C.

213. *Midland Funding*, 786 F.3d at 249.

214. *See id.* at 251–52.

215. Federal bank regulators stepped in to prevent payday lenders from engaging in this very practice. *See* MICHAEL S. BARR, NO SLACK: THE FINANCIAL LIVES OF LOW-INCOME AMERICANS 138 (2012).

ing may argue that the decision is (1) limited to debt purchasers,[216] (2) limited to partnerships with national banks,[217] or (3) undermined by the "valid-when-made" doctrine.[218] Additionally, Lending Club may argue that the decision is no longer applicable to its lending model because of a recent change to Lending Club's relationship with WebBank.[219] Ultimately, however, these arguments are not likely to be successful for the reasons set forth below.

First, peer-to-peer lending platforms could argue that the decision should be limited to debt purchasers.[220] The Second Circuit rejected Midland Funding's attempt to rely on the NBA, but it did acknowledge that NBA protection has extended beyond national banks to several entities that are not debt purchasers.[221] For example, both agents[222] and subsidiaries[223] of national banks are typically entitled to NBA protection, as well as non-national banks that are considered "equivalent to national banks."[224] Prosper and Lending Club are not agents or subsidiaries of WebBank, but there is a relationship between the parties at the time of origination that resembles the relationship between bank and bank subsidiary: WebBank issues the loan with the understanding that the note will then be assigned to Prosper or Lending Club.[225] Unlike the loan in *Midland Funding*, which was not issued by the bank for immediate assignment to the debt purchaser,[226] WebBank and the peer-to-peer lending platforms work together from the time the loan originates.[227] Thus, due to the consistent and continuous relationship between WebBank and the peer-to-peer lending platforms, interfering with the lending platforms' use of the exportation doctrine

216. *See* Brief in Opposition at i, Midland Funding, LLC v. Madden, No. 15-610 (U.S. Feb. 12, 2016) (stating the question presented to be whether a "debt collector" is permitted "to charge interest that is criminally usurious under New York law on defaulted consumer debt that the debt collector purchased from a national bank").

217. Deborah Festa et al., *Madden v. Midland Funding LLC—Implications and Potential Responses*, MILBANK, TWEED, HADLEY & MCCLOY LLP (Oct. 15, 2015), http://www.mondaq.com/unitedstates/x/435110/Financial+Services/Madden+v+Midland+Funding+LLC [https://perma.cc/W6X8-6WJJ] (noting that the *Midland Funding* decision did not explicitly address state-chartered banks).

218. *See* Brief for the United States as Amicus Curiae at 11–12, Midland Funding, LLC v. Madden, No. 15-610 (U.S. May 24, 2016) (asserting that the Second Circuit "failed to appreciate the significance" of the valid-when-made doctrine); *Special Alert: Second Circuit Decision Threatens to Upset Secondary Credit Markets*, BUCKLEY SANDLER LLP, http://www.buckleysandler.com/uploads/1082/doc/Special-Alert-re-Madden-v-Midland_Funding_LLC.pdf [https://perma.cc/U9ZA-95NZ] (arguing that the Second Circuit failed to consider the valid-when-made doctrine); *see also* Festa et al., *supra* note 217.

219. *See* LENDINGCLUB, Press Release, *supra* note 79; Lending Club, Current Report, *supra* note 80.

220. In her brief to the Supreme Court, Madden may have attempted to limit the decision to debt purchasers when she framed the issue of the case narrowly and argued that "marketplace lending," also referred to as peer-to-peer lending, "has nothing to do with this case." *See* Brief in Opposition, *supra* note 216, at i, 22.

221. *See* Madden v. Midland Funding, LLC, 786 F.3d 246, 250 (2d Cir. 2015).

222. *Id.* (citing Pac. Capital Bank, N.A. v. Connecticut, 542 F.3d 341, 352 (2d Cir. 2008)).

223. *Id.* (citing Watters v. Wachovia Bank, N.A., 550 U.S. 1, 18 (2007)).

224. *Id.* (citing *Watters*, 550 U.S. at 18).

225. *See* Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 3, 52.

226. *Midland Funding*, 786 F.3d at 247–48.

227. *See* Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 34, 52.

could indirectly interfere with WebBank's ability to exercise its exportation powers under the FDIA.

This distinction, however, will likely not allow peer-to-peer lending platforms to escape the *Midland Funding* holding. The Second Circuit did not limit its holding to debt purchasers or focus on the nature of debt collection in articulating its reasoning.[228] Rather, the critical fact in the court's analysis was the originating bank's lack of retained interest in the loan.[229] Similar to the national bank in *Midland Funding*, WebBank has traditionally retained no interest in the loans it sells to Prosper or Lending Club, and it still retains no interest in loans it sells to Prosper.[230] Though Prosper maintains a continuous relationship with the originating bank in a way that Midland Funding did not, WebBank's lack of retained interest in the loan indicates that the exportation doctrine is not appropriate under the reasoning of *Midland Funding*.[231]

Second, peer-to-peer lending platforms could argue that the *Midland Funding* decision should be limited to the NBA.[232] Unlike the loan in *Midland Funding*, which involved a national bank loan and application of the NBA,[233] peer-to-peer loans are issued by a state-chartered bank and involve application of the FDIA.[234] Thus, if the scope of the NBA is different than the scope of the FDIA, the peer-to-peer lending partnership with WebBank will not be affected.

This argument, however, will likely be unsuccessful in distinguishing *Midland Funding* from peer-to-peer lending. Section 27 of the FDIA, which provides WebBank with the ability to utilize the exportation doctrine, was modeled after and borrowed language from section 85 of the NBA.[235] Because "Congress made a conscious choice" to incorporate section 85 of the NBA into section 27 of the FDIA, the two statutes have been consistently construed together and interpreted the same way.[236] Therefore, a court would not likely

228. *See generally* Madden v. Midland Funding, LLC, 786 F.3d 246 (2d Cir. 2015). The Solicitor General did not limit the issue of the case to debt purchasers either. *See* Brief for the United States as Amicus Curiae at I, Midland Funding, LLC v. Madden, No. 15-610 (U.S. May 24, 2016) (presenting the question as "[w]hether the National Bank Act . . . continues to have preemptive effect after the national bank has sold or otherwise assigned the loan to another entity").

229. *See id.* at 251; *supra* Sections IV.A, IV.B; *see also* Reply for the Petitioners at 6 n.4, Midland Funding v. Madden, No. 15-610 (U.S. Feb. 12, 2016) (noting that the Second Circuit did not distinguish between the traditional credit market and peer-to-peer lending).

230. *See* Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 3, 52.

231. Additionally, Lending Club's restructured relationship with WebBank may still fall within the scope of *Midland Funding*. *See infra* text accompanying notes 245–56.

232. *See* Festa et al., *supra* note 217.

233. 786 F.3d at 247.

234. *See* 12 U.S.C. § 1831d(a) (2012); *see also* Lending Club, Prospectus, *supra* note 55, at 3; Prosper, Prospectus, *supra* note 14, at 3.

235. *See* Greenwood Trust Co. v. Massachusetts, 971 F.2d 818, 826–27 (1st Cir. 1992) (referencing The Depository Institution Deregulation and Monetary Control Act of 1980, which inserted section 27 into the FDIA).

236. *See id.* at 827 (holding that section 85 of the NBA and section 27 of the FDIA must be read "*in pari materia*"), General Counsel's Opinion No. 10, Interest Charges Under Section 27 of the Federal

limit the *Midland Funding* decision to national banks alone.[237]

Third, peer-to-peer lending platforms could argue that the *Midland Funding* decision failed to address the valid-when-made doctrine, which recognizes that the "non-usurious character of a note should not change when the note changes hands."[238] In applying this doctrine, the Eight Circuit previously held that the assignee of a defaulted credit card account, a nonbank retail store, was entitled to NBA protection from state usury claims because the credit account originated with a national bank.[239] Thus, the peer-to-peer lending industry would argue, the loans originated by WebBank are valid under Utah law at the time of issuance, and therefore remain valid when the loans are passed on to platforms like Prosper or Lending Club.

This argument, however, is also unlikely to succeed.[240] The valid-when-made doctrine is typically applied in the context of a lender assigning a loan to a third party,[241] but the peer-to-peer loan structure is different than a typical loan assignment. The borrower's note does not simply pass from WebBank to platform to investor. Instead, WebBank sells the borrower's note to the online platform, and the platform then sells a separate note to the investor.[242] Thus, applying the valid-when-made doctrine may not be appropriate because the peer-to-peer lending structure creates two different notes, rather than merely one note with an assignor and an assignee. Additionally, although the *Midland Funding* court did not explicitly address the valid-when-made doctrine, it did distinguish the facts of the case from the Eight Circuit decision that applied the doctrine, *Krispin v. May Department Stores*.[243] According to the Second Circuit, the facts of *Midland Funding* were distinguishable from the facts of *Krispin* because the bank providing the credit in *Krispin* maintained an interest in the debt after assigning it, whereas the bank in *Midland Funding* did not.[244] Thus, at least in the Second Circuit, *Midland Funding* appears to imply that the bank's retained interest in the loan, or lack thereof, trumps a valid-when-made argument.

Finally, Lending Club could argue that the *Midland Funding* decision will not apply to its loans because Lending Club recently altered its relationship with

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Deposit Insurance Act, 63 Fed. Reg. 19258, 19258–59 (Apr. 8, 1998), https://www.fdic.gov/regulations/laws/federal/98riskb.pdf.

237. *See* Festa et al., *supra* note 217.

238. FDIC v. Lattimore Land Corp., 656 F.2d 139, 148–49 (5th Cir. 1981); *see also* Brief for the United States as Amicus Curiae at 11–12, Midland Funding, LLC v. Madden, No. 15-610 (U.S. May 24, 2016); BUCKLEY SANDLER LLP, *supra* note 218.

239. Krispin v. May Dep't Stores, 218 F.3d 919, 924 (8th Cir. 2000).

240. This analysis is limited to liability for peer-to-peer lending platforms. WebBank is not subject to liability because it issued a loan that was in compliance with Utah law and WebBank's ability to use the exportation doctrine is not in dispute. *See* Lending Club, Prospectus, *supra* note 55, at 31; Prosper, Prospectus, *supra* note 14, at 82.

241. BUCKLEY SANDLER LLP, *supra* note 218.

242. *See* Verstein, *supra* note 8, at 476–77.

243. *See Midland Funding*, 786 F.3d at 252–53 (citing *Krispin*, 218 F.3d at 921–24).

244. *See id.* Because the bank retained ownership over the loan accounts, the bank was considered "the real party in interest." *Id.* at 252 (quoting *Krispin*, 218 F.3d at 924).

WebBank so that WebBank maintains an ongoing interest in the loan.[245] Unlike in *Midland Funding*, where the originating bank retained no connection to the borrower or financial interest in the loan after selling it to the debt purchaser, WebBank remains connected to both the borrower and loan after selling the loan to Lending Club.[246] Thus, even if other lending platforms are unsuccessful in limiting the scope of *Midland Funding*, Lending Club will likely argue that the decision does not extend to Lending Club's loans because WebBank retains an economic interest in the loan after selling it to the platform.[247]

This argument, however, may not succeed. Although Lending Club has given WebBank a greater interest in peer-to-peer loans in an attempt to distinguish WebBank from the national bank in *Midland Funding*, a court may still determine that Lending Club's model falls within the reasoning of *Midland Funding*. The Second Circuit in *Midland Funding* referenced the national bank's lack of retained interest in the loan, but it also mentioned that NBA protection is typically applied to nonbank entities that are acting "on behalf of" a bank.[248] Because Lending Club facilitates these loans by attracting borrowers and investors,[249] Lending Club likely could not argue it acts on behalf of WebBank.[250] Furthermore, even with WebBank's ongoing interest in the loan, the relationship is still likely distinguishable from the Eighth Circuit decision in *Krispin*.[251] NBA protection applied in *Krispin* because the originating bank was deemed the "real party in interest" even after it sold the loan accounts,[252] whereas WebBank is unlikely to be considered the real party in interest because its only connection to the loan is an account with the borrower and a monthly fee.[253] Compared to WebBank, the investors and Lending Club have a much greater interest in the loan: the investors provide the requested funds, and Lending Club's success depends upon facilitating loans and ensuring that investors are satisfied.[254] Thus, despite Lending Club's changed model, a court may determine the reasoning of *Midland Funding* still applies by dismissing WebBank's enhanced connection to Lending Club as a superficial attempt to circumvent *Midland*

245. *See* LENDINGCLUB, Press Release, *supra* note 79; Lending Club, Current Report, *supra* note 80. Lending Club explicitly stated that these changes were made "in light of concerns created by the *Madden v. Midland* decision." LENDINGCLUB, Press Release, *supra* note 79.

246. When WebBank issues a peer-to-peer loan, it establishes a relationship with the borrower and receives monthly fees from Lending Club as the borrower repays the loan. *See* LENDINGCLUB, Press Release, *supra* note 79; Lending Club, Current Report, *supra* note 80.

247. *See* LENDINGCLUB, Press Release, *supra* note 79.

248. Madden v. Midland Funding, LLC, 786 F.3d 246, 251 (2d Cir. 2015).

249. *See supra* Section II.A.

250. Rather, it appears that WebBank is acting on behalf of Lending Club. *See* LENDINGCLUB, Press Release, *supra* note 79; Lending Club, Current Report, *supra* note 80.

251. Krispin v. May Dep't Stores, 218 F.3d 919, 924 (8th Cir. 2000). The Second Circuit distinguished the originating bank in *Midland Funding* from the originating bank in *Krispin* when it determined that NBA protection was not appropriate. *See Midland Funding*, 786 F.3d at 252–53.

252. *See Midland Funding*, 786 F.3d at 252–53 (citing *Krispin*, 218 F.3d at 924).

253. *See* LENDINGCLUB, Press Release, *supra* note 79; Lending Club, Current Report, *supra* note 80.

254. *See* Slattery, *supra* note 6, at 246–47.

Funding[255] and state usury laws.[256]

Additionally, Lending Club's new model with WebBank may not be economically sustainable within the peer-to-peer lending industry. In order to provide WebBank with a greater economic interest in the loan, Lending Club uses a portion of its revenues to pay WebBank the monthly fees connected to the success of the loan.[257] Although some analysts believe that this change will have a minimal impact on interest rates of loans offered by Lending Club,[258] this change will be a cost nonetheless and Lending Club did increase the maximum APR offered for loans in 2016.[259] As transactional costs increase at Lending Club, there is a greater likelihood that those costs will be passed on to borrowers through higher interest rates or to investors through lower returns.[260] Because the success of peer-to-peer lending depends on low interest rates for borrowers and solid returns for investors, any change that disrupts those rates and returns, even if small, could significantly threaten the viability of these lending platforms.[261]

V. PEER-TO-PEER LENDING AND THE EXPORTATION DOCTRINE

Peer-to-peer lending may be relatively new, but it has garnered significant attention in the legal community and prior research has consistently suggested that peer-to-peer lending is a beneficial development.[262] Because of the advantages that peer-to-peer lending offers in comparison to traditional lending,[263] prior research has focused on the best methods for promoting and protecting this emerging form of lending.[264] For example, researchers have criticized the

255. *See* Festa et al., *supra* note 217 (noting that a change in form over substance might not satisfy the requirements of *Midland Funding*).

256. In holding that Midland Funding was not permitted to export interest rates, the Second Circuit expressed concern with nonbank entities otherwise circumventing state usury laws. *See Midland Funding*, 786 F.3d at 251–52; *see also* Ryan Weeks, *Lending Club Rejigs Relationship With Issuing Bank*, ALTFI NEWS (Feb. 29, 2016), http://www.altfi.com/article/1774_lending_club_rejigs_relationship_with_issuing_bank [https://perma.cc/4PD3-J5WK] (noting that Lending Club's new model does not address concerns related to state usury laws).

257. *See* Weeks, *supra* note 256.

258. *See* Caitlin Huston, *LendingClub Shifts Risk Ahead of Court Ruling, Others in Crowded Field May Follow*, MARKET WATCH (Feb. 26, 2016), http://www.marketwatch.com/story/lendingclub-shifts-risk-ahead-of-court-ruling-could-inspire-other-online-lenders-to-join-2016-02-26.

259. *See* Rudegeair & Demos, *supra* note 79.

260. *See supra* text accompanying notes 91–97.

261. *See supra* Section II.A.

262. *See, e.g.*, GAO REPORT, *supra* note 6, at 18 (finding that, despite certain regulatory risks, peer-to-peer lending can offer good returns for investors and expand the number of borrowers with access to credit); Magee, *supra* note 126, at 173–74 (noting that peer-to-peer lending platforms provide a much needed "legitimate source of capital otherwise unavailable to many borrowers"); Smith, *supra* note 8, at 24 (describing peer-to-peer lending as a "promising and beneficial financial innovation").

263. *See supra* Section II.A.

264. Public Input on Expanding Access to Credit Through Online Marketplace Lending, 80 Fed. Reg. 42,866 (proposed July 20, 2015), http://www.gpo.gov/fdsys/pkg/FR-2015-07-20/pdf/2015-17644.pdf [https://perma.cc/WU5Y-ALNS] [hereinafter Treasury Notice] (seeking public input on how to best expand and protect the online lending marketplace); *see also* Smith, *supra* note 8, at 24 (stating that

SEC's decision to regulate the industry due to fears that such regulation will increase costs for investors and borrowers, and ultimately stifle financial innovation.[265] In criticizing SEC regulation, researchers primarily suggest that regulation of peer-to-peer lending should instead take the form of a multiregulatory approach in a similar fashion to the regulation of traditional banks,[266] or that peer-to-peer lending should fall exclusively within the CFPB's authority.[267]

This Note builds upon prior research by advocating for an additional method of protecting peer-to-peer lending. If *Madden v. Midland Funding*[268] is extended to peer-to-peer lending and lending platforms can no longer use the exportation doctrine, the success and viability of platforms such as Prosper and Lending Club could be significantly threatened.[269] In light of the *Midland Funding* decision, this Note recommends that Congress or the FDIC explicitly permit peer-to-peer lending platforms to utilize the exportation doctrine through their partnerships with state-chartered banks.

In response to this proposal, opponents may argue that the exportation doctrine was not intended for online lending platforms and that use of the doctrine will exacerbate many of the risks associated with peer-to-peer lending. Ultimately, however, the exportation doctrine is appropriate and necessary because it promotes a competitive consumer credit market, protects the core benefits of peer-to-peer lending, and provides certainty in the industry. Furthermore, the risks associated with peer-to-peer lending and the exportation doctrine can be addressed through other forms of regulation and market forces.

A. ARGUMENTS AGAINST THE EXPORTATION DOCTRINE

Those opposed to allowing peer-to-peer lending platforms to use the exportation doctrine will likely justify their position on two grounds: (1) the doctrine was designed to protect depository institutions and other traditional lending institutions, which are distinct from peer-to-peer lending platforms, and (2) the

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regulators should allow the platforms to develop); Verstein, *supra* note 8, at 530 (proposing that regulation should be focused on protecting consumers, but not at the expense of restricting the innovation of peer-to-peer lending).

265. *See* Slattery, *supra* note 6, at 273–74; Smith, *supra* note 8, at 24.

266. *See generally* Chaffee & Rapp, *supra* note 8.

267. *See generally* Slattery, *supra* note 6; Verstein, *supra* note 8. More substantive regulation from an agency such as the CFPB would address several of the concerns and risks related to peer-to-peer lending, such as risk of borrower fraud, while also ensuring that peer-to-peer lending platforms have the necessary freedom to grow and develop. *See, e.g.*, Magee, *supra* note 126, at 170 (asserting that regulators should require lending platforms to verify borrower information); Verstein, *supra* note 8, at 530 ("The CFPB is better situated to provide [investors] and borrowers the protections they need while letting the industry evolve and grow.").

268. 786 F.3d 246 (2d Cir. 2015).

269. *See* Shah Gilani, *Storm Clouds Are Gathering Around Peer-to-Peer Lending*, WALL ST. INSIGHTS & INDICTMENTS (Aug. 21, 2015), http://wallstreetinsightsandindictments.com/2015/08/storm-clouds-are-gathering-around-peer-to-peer-lending/ [https://perma.cc/6QLW-2LEU]; Peter Rudegeair, *A New Tariff on 'Interest-Rate Exports?*,' WALL ST. J. (June 30, 2015), http://blogs.wsj.com/moneybeat/2015/06/30/a-new-tariff-on-interest-rate-exports/ [https://perma.cc/ZP32-MG43].

doctrine fails to address, and may even exacerbate, the risks associated with peer-to-peer lending.

1. Unintended Purpose

First, those opposed to extending the exportation doctrine to peer-to-peer lending platforms may argue that the doctrine was only intended for large financial institutions that are critical to the economy and highly regulated. The benefits provided by the NBA, FDIA, and exportation doctrine were premised on the idea that national and state depository institutions serve a unique and important role in the nation's financial economy.[270] For example, depository institutions provide a banking system that can effectively operate throughout the country, which improves the efficiency and stability of the nation's financial system.[271] Because depository institutions play such a vital role in the financial market and economy, the benefits of an efficient banking system outweigh the risks that banks may abuse their privileges and circumvent state usury laws through oppressive interest rates.[272] Depository institutions are also subject to significant regulation, and this regulation can effectively act as a check on the risk of abuse.[273]

When nonbank entities attempt to utilize the exportation doctrines, however, the justification for the exportation doctrine is weakened.[274] In contrast to traditional lending institutions, peer-to-peer lending platforms serve only a small portion of the consumer credit market.[275] Additionally, they are not subject to banking regulations[276] and they have escaped significant state regulation by relying on the exportation doctrine.[277] When nonbank entities that are not as heavily regulated utilize the exportation doctrine, the risk of abuse increases.[278] If peer-to-peer lending platforms continue to utilize the exportation doctrine, these relatively unregulated platforms—providing only a small portion

270. *See* Schiltz, *supra* note 13, at 599.

271. *Id.* at 599–600. Section 85 of the NBA was enacted to bolster the country's national banking system and to prevent state legislatures from unfairly favoring state banks. *See* Tiffany v. Nat'l Bank of Mo. 85 U.S. 409, 411–413 (1873); Schiltz, *supra* note 13, at 544. Similarly, section 27 of the FDIA was enacted to bolster the state banking system and prevent federal legislatures from unfairly favoring national banks. *See* 12 U.S.C. § 1831d(a) (2012). The exportation doctrine furthers both of those purposes by "fostering the development of an interstate banking system." Schiltz, *supra* note 13, at 568.

272. *See* Schiltz, *supra* note 13, at 599–600.

273. *Id.* at 569.

274. *Id.* at 599. For example, regulators and academics have opposed payday lenders' attempts to use the exportation doctrine. *See generally* Diane Hellwig, *Exposing the Loansharks in Sheep's Clothing: Why Re-Regulating the Consumer Credit Market Makes Economic Sense*, 80 NOTRE DAME L. REV. 1567 (2005); Kelly J. Noyes, *Get Cash Until Payday! The Payday-Loan Problem in Wisconsin*, 2006 WIS. L. REV. 1627 (2006); Schiltz, *supra* note 13.

275. PWC REPORT, *supra* note 5, at 2.

276. *See* Verstein, *supra* note 8, at 458–59.

277. *See* Lending Club, Prospectus, *supra* note 55, at 31; Prosper, Prospectus, *supra* note 14, at 82.

278. *See* Schiltz, *supra* note 13, at 569, 599–600.

of credit in the financial market—could undermine state legislatures throughout the country.

Thus, some may argue that the exportation doctrine is not appropriate for peer-to-peer lending platforms because the doctrine was not intended to extend beyond large, mainstream financial services. Because the exportation doctrine allows entities to export the laws of their home state to any state in the country, potentially undermining the laws of forty-nine other states, the doctrine possesses "extraordinary preemptive force" and requires a "powerful justification" for its use.[279] There is a powerful justification for its use by depositories because they stabilize and promote the financial health of the nation, and because they are subject to significant regulation.[280] The role of peer-to-peer lending platforms simply does not justify the extension of a power as great as the exportation doctrine.

2. Exacerbated Risks

Second, those opposed to extending the exportation doctrine to peer-to-peer lending platforms may argue that the doctrine exacerbates, rather than alleviates, the unique risks associated with peer-to-peer lending. Permitting peer-to-peer lending platforms to export interest rates fails to address the primary risks associated with peer-to-peer lending, such as the risk of borrower fraud or the risks created by the mismatched incentives between investor and platform.[281] Rather than addressing these risks, the doctrine may actually exacerbate certain risks. For example, institutional investors are becoming increasingly interested in lending through peer-to-peer lending platforms, possibly as a way of circumventing regulations.[282] If peer-to-peer lending platforms can explicitly export interest rates throughout the country without concern for state regulation, institutional investors will have an even greater incentive to use peer-to-peer lending as a mechanism for circumventing otherwise applicable state regulation.

B. THE EXPORTATION DOCTRINE IS APPROPRIATE

This Note argues that Congress or the FDIC should step in and explicitly permit peer-to-peer lending platforms to utilize the exportation doctrine through their partnership with state-chartered banks. Allowing peer-to-peer lending platforms to export rates is appropriate and necessary because it (1) promotes the broader purpose of the exportation doctrine by fostering a competitive financial market, (2) preserves the unique benefits associated with peer-to-peer lending, and (3) provides certainty in the industry. Furthermore, additional

279. *See id.* at 600.
280. *See id.* at 569, 599–600.
281. *See supra* Section II.B.
282. *See* PwC REPORT, *supra* note 5; Cortese, *supra* note 153. For example, banks are subject to certain capital and reserve regulations that require banks to hold a certain portion of the bank's deposits in reserve. Institutional investors using peer-to-peer lending platforms, in contrast, are not subject to such requirements. *See* Verstein, *supra* note 8, at 458–59.

forms of regulation and market forces can adequately address the risks posed by peer-to-peer lending and the exportation doctrine, while still providing the industry with the opportunity to grow and thrive.

1. Strengthening the Credit Market

First, permitting peer-to-peer lending platforms to export interest rates is consistent with the broader purpose of the exportation doctrine because it creates a stronger and more competitive credit market.[283] Peer-to-peer lending platforms bolster the consumer credit market in two important ways: they directly compete with large financial institutions, and they offer a more reliable and appealing credit alternative when compared to other alternative forms of credit, such as payday loans or refund anticipation loans.[284]

By providing loans with similar or lower interest rates compared to loans offered by banks, peer-to-peer lending platforms directly compete for many of the borrowers that might otherwise look to a traditional bank for a loan.[285] The mainstream consumer lending market is notorious for the lack of borrower credit options and the "systematic failures of competition."[286] Peer-to-peer lending platforms address that failure by offering similar loans to mainstream banks, but with additional benefits, such as better interest rates and greater transparency.[287] Such competition ultimately benefits consumers: as peer-to-peer lending grows, banks may lower interest rates or change lending procedures to remain attractive to low-risk borrowers.[288] Furthermore, because peer-to-peer lending removes geographic restraints, these platforms can also provide credit to credit-worthy borrowers who might not otherwise have access to mainstream credit.[289]

Additionally, peer-to-peer lending platforms provide needed competition within the mainstream credit market in a way that other alternative sources of credit do not. These traditional alternative sources—"fringe" products such as payday loans or refund anticipation loans—have failed to compete with banks or other large lending institutions because the lenders typically only target high-risk, low-credit borrowers who present too much risk to obtain a traditional bank

283. Schiltz, *supra* note 13, at 600, 621–22 (acknowledging that, because the exportation doctrine was originally designed to promote a competitive interstate banking system, the extension of the exportation doctrine to a nonbank entity may be justified when that entity greatly strengthens the competitiveness and efficiency of the financial market).

284. *See* Verstein, *supra* note 8, at 529 ("Disintermediated transactions such as [peer-to-peer] loans create a new core economic function that warrants preserving.").

285. Olinga, *supra* note 90.

286. Verstein, *supra* note 8, at 461.

287. *See supra* Section II.A.

288. Verstein, *supra* note 8, at 461 ("Robust competition generally benefits consumers by lowering prices and encouraging innovation.").

289. *See supra* Section II.A.

loan.[290] The borrowers are often financially distressed and unable to access credit from a large institution, and the lenders typically only offer short-term, small-amount loans with extremely high interest rates.[291] In contrast, rather than only attracting financially desperate borrowers through short-term and high-cost loans, peer-to-peer lending platforms attract lower risk borrowers with loans that are similar to, or more appealing than, loans from mainstream banks.[292] Although peer-to-peer borrowers with lower credit scores may face APRs that exceed the usury laws of certain states, the highest APRs on peer-to-peer lending platforms are still considerably better than the APRs of typical payday loans.[293] Prosper and Lending Club's findings that most borrowers use peer-to-peer loans to consolidate debt or pay off credit cards illustrates that these platforms are in fact providing favorable interest rates for borrowers compared to other forms of credit.[294] Thus, by providing a strong credit alternative where other alternative credit sources have failed, peer-to-peer lending platforms promote a competitive credit market on a national level.

2. Retaining the Benefits of Peer-to-Peer Lending

Peer-to-peer lending platforms should be permitted to utilize the exportation doctrine because otherwise, these platforms could no longer offer their core benefits.[295] If peer-to-peer lending platforms can no longer rely on the exportation doctrine, these platforms will need to comply with the interest rate limits and lending license requirements of each individual state in which they wish to offer loans.[296] As Lending Club acknowledges, the process of adapting to different procedural and substantive requirements in each state would require the platform to "substantially modify [its] business operations" and would be

290. Noyes, *supra* note 274, at 1631–32. The benefits and risks offered by these alternative lenders are debatable, but there is a general consensus that these alternative lenders are distinct from mainstream financial lending institutions. *See id.*

291. Noyes, *supra* note 274, at 1631–32; *What is a Payday Loan?*, CONSUMER FIN. PROTECTION BUREAU (Nov. 6, 2013), http://www.consumerfinance.gov/askcfpb/1567/what-payday-loan.html [https://perma.cc/KG98-FHPQ].

292. *See* Slattery, *supra* note 6, at 243; Verstein, *supra* note 8, at 457–58. The regulatory responses to peer-to-peer lending, as compared to predatory lending such as payday loans, also illustrates that the two types of lending serve different purposes and therefore deserve to be treated differently. *Compare* Treasury Notice, *supra* note 264 (seeking input on how to expand the online lending marketplace), *with* Small Business Advisory Review Panel for Potential Rulemakings for Payday, Vehicle Title, and Similar Loans, *Outline of Proposals Under Consideration and Alternatives Considered*, CONSUMER FIN. PROTECTION BUREAU (Mar. 26, 2015), http://files.consumerfinance.gov/f/201503_cfpb_outline-of-the-proposals-from-small-business-review-panel.pdf [https://perma.cc/JGQ4-TPCR] [hereinafter CFPB, *Proposal*] (seeking to restrict and further regulate payday lending).

293. The APR at Prosper and Lending Club cannot exceed 36%. *See supra* Sections I.A.1, I.A.2. The average payday loan, in contrast, has an APR of 400%. *What is a Payday Loan?*, CONSUMER FIN. PROTECTION BUREAU (Nov. 6, 2013), http://www.consumerfinance.gov/askcfpb/1567/what-payday-loan.html [https://perma.cc/KG98-FHPQ].

294. *See* Prosper, Prospectus, *supra* note 14, at 49; LENDINGCLUB, *Statistics*, *supra* note 55.

295. *See supra* Section II.A.

296. *See* Lending Club, Prospectus, *supra* note 55, at 15; *supra* Section III.B.

"costly and time-consuming."[297] These changes and costs could significantly undermine several of the benefits offered by peer-to-peer lending, as outlined below.

If platforms cannot use the exportation doctrine, and instead must comply with the requirements of each state, these platforms may not be able to attract borrowers and investors. The peer-to-peer lending industry has been positively received because it offers both low interest rates for borrowers and strong returns for investors.[298] The ability to offer attractive rates and returns, however, is contingent upon the minimal administrative costs incurred by the platform.[299] If Prosper and Lending Club instead exert significant time and resources into state lending licenses, those costs will likely be passed on to the borrowers and investors.[300] If these costs affect investor returns, the investors may no longer be willing to provide credit and the very existence of peer-to-peer lending could be threatened.[301] Given that Prosper and Lending Club are already struggling with net operating losses, the additional costs could cause the platforms to fold altogether.[302]

Additionally, the inability to use the exportation doctrine would threaten the simplicity of the peer-to-peer lending platforms. The current platform interface is simple and easy to understand: in order to determine the applicable interest rate, an interested borrower needs to only state his or her desired loan amount, his or her credit score, and the purpose of the loan.[303] If the borrower is satisfied with the rate, he or she can then move forward with the application.[304] In contrast, if a platform is subject to different requirements from each state, the platform's website will likely become more complex and more difficult to understand. For example, the borrower's interest rate will depend on the state where he or she resides and may change based on the amount the borrower is requesting.[305] Although peer-to-peer lending platforms are currently subjected to varying investor eligibility requirements based upon the investor's state of residence,[306] such variation does not affect the borrower's experience with the

297. Lending Club, Prospectus, *supra* note 55, at 15, 31.

298. *See supra* Section II.A; *see also* Jeff Rose, *Peer to Peer Lending: The Investment You Might Be Missing Out On*, HUFFINGTON POST (Jan. 22, 2014), http://www.huffingtonpost.com/jeff-rose/peer-to-peer-lending-the-_b_4628598.html [https://perma.cc/997L-L8S3] (discussing why peer-to-peer lending can benefit both borrowers and investors).

299. *See supra* Section II.A; *see also* Verstein, *supra* note 8, at 529 (noting that significant regulatory costs imposed on peer-to-peer lending platforms will likely be detrimental to both borrowers and investors).

300. *See* Slattery, *supra* note 6, at 274 (noting that "unnecessary and significant compliance costs . . . will ultimately pass through to lenders, borrowers, and investors").

301. *See* Lending Club, Prospectus, *supra* note 55, at 14–15.

302. *See* Lending Club, Prospectus, *supra* note 55, at 14–15.

303. LENDINGCLUB, *How It Works*, *supra* note 15.

304. *See* Prosper, Prospectus, *supra* note 14, at 31.

305. For example, the interest rate limit in New York depends on whether the personal loan amount is less than $25,000. *See* N.Y. BANKING LAW §§ 14-a, 340 (McKinney 2015).

306. *See* Prosper, Prospectus, *supra* note 14, at 9.

lending platform in the way that varying interest rate limits would. As the number of questions and forms directed to a potential borrower increases, the peer-to-peer lending process may begin to resemble the more complicated and unappealing process associated with traditional lending institutions.[307]

Furthermore, the inability to utilize the exportation doctrine would undermine the platform's ability to provide credit access to a greater and more diverse number of borrowers. Because some states impose relatively stringent limits on interest rates,[308] a peer-to-peer lending platform could choose not to facilitate loans in certain states altogether, rather than comply with the state's restrictive laws. If Prosper and Lending Club restrict permissible borrowers to fewer states, fewer borrowers will have access to the credit offered on those platforms. The platforms could still provide broad access to credit in the states where peer-to-peer lending is financially viable, but if platforms are only offering loans to borrowers in a few states, that benefit is significantly diminished.

3. Certainty in the Industry

Allowing peer-to-peer lending platforms to export rates would provide certainty in the industry. Given that the Supreme Court denied Midland Funding's petition for certiorari,[309] uncertainty is likely to remain in the peer-to-peer lending industry. Because of this uncertainty, investors may be less willing to provide money through peer-to-peer lending platforms. Without a sufficient number of investors, competition could diminish and borrower interest rates could suffer, or peer-to-peer lending platforms could collapse.[310]

4. Additional Regulation and Market Forces

Additional forms of regulation and market forces can address many of the risks posed by peer-to-peer lending. As suggested in previous research, a unified regulatory approach from the CFPB could address many of the concerns associated with peer-to-peer lending.[311] For example, regulators could require platforms to verify borrower income and employment to reduce the risk of borrower fraud.[312] Regulators could also limit the amount that institutions can invest in peer-to-peer lending to address the concerns associated with large institutions circumventing rules and regulations.[313] Additionally, if platforms like Prosper and Lending Club attempt to abuse the privileges of the exportation doctrine by charging interest rates similar to those of payday loans, the platforms could also face additional regulation from a recent CFPB proposal related

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307. *See supra* text accompanying notes 100–10.
308. *See supra* note 180.
309. *See* Madden v. Midland Funding, LLC, 2016 WL 3461580 (U.S. June 27, 2016).
310. *See* Slattery, *supra* note 6, at 246–47 (noting that investor confidence is critical to the success of the platform).
311. *See* Slattery, *supra* note 6; Verstein, *supra* note 8.
312. Magee, *supra* note 126, at 171.
313. *See* Cortese, *supra* note 153.

to the regulation of payday lenders.[314]

Market forces will likely diminish many of these risks as well, including the concern of platforms abusing the exportation doctrine.[315] If peer-to-peer lending platforms abuse the exportation doctrine by changing their lending procedures and imposing higher interest rates, borrowers may simply look elsewhere. Or if investors feel that the mismatched incentives between investor and platform are compromising their returns, they will simply stop investing. Unlike payday loans and other alternative sources of credit, where lenders can take advantage of a borrower's financial desperation and lack of alternatives by charging extremely high interest rates,[316] peer-to-peer lending platforms have thrived by offering low-interest loans to low-risk individuals who could obtain loans elsewhere.[317] Because the platforms need loan transactions to generate a profit and remain financially viable, the platforms are heavily incentivized to ensure that the industry remains attractive to both borrowers and investors.

CONCLUSION

Peer-to-peer lending is a fast growing industry with the potential to change the way individuals borrow and lend money. By directly connecting borrowers and investors through an online marketplace, peer-to-peer lending platforms offer several benefits that traditional lending institutions cannot. Borrowers can receive better interest rates, greater access to credit, and the benefits of a simpler and more transparent lending process. Additionally, investors have the opportunity to diversify their investment portfolio and receive strong returns. Though there are certain risks associated with peer-to-peer lending, many of those risks are mitigated by market forces and competition, and they are significantly outweighed by the industry's unique benefits.

Thus, peer-to-peer lending platforms should be permitted to utilize the exportation doctrine through their relationship with state chartered banks and to export the interest rates of the banks' home state to loans throughout the country. Although the exportation doctrine was originally intended for traditional depository lending institutions, the broader purpose of the doctrine was to foster a strong financial market on a national level. By creating much needed competition in the consumer credit market, peer-to-peer lending serves that broader purpose. Furthermore, use of the exportation doctrine allows peer-to-peer lending platforms to preserve the unique benefits associated with the industry. Though the exportation doctrine does not address the risks associated with peer-to-peer lending, that should not deter Congress or the FDIC from

314. *See* CFPB, *Proposal*, *supra* note 292.

315. The ability of the market to significantly reduce the risks associated with peer-to-peer lending is discussed more fully in Section II.B.

316. *See* Noyes, *supra* note 274, at 1631–32.

317. *See* Slattery, *supra* note 6, at 243; Verstein, *supra* note 8, at 457–58; *see also* Prosper, Prospectus, *supra* note 14, at 49; LENDINGCLUB, *Statistics*, *supra* note 55.

permitting platforms to use the doctrine because those risks can be mitigated through additional regulation and market forces.

Ultimately, peer-to-peer lending is revolutionizing consumer credit by providing an online lending marketplace with unique benefits that traditional lending sources have failed to offer. As borrowers become less trusting of large banks, or as banks become more restrictive in the number of borrowers that are eligible for credit, it is vital that borrowers are presented with a reliable alternative source of credit: peer-to-peer lending provides that alternative. Peer-to-peer lending is an innovative industry with the ability to benefit borrowers on a national scale, but it needs the exportation doctrine in order to grow and become a part of the mainstream credit market.