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Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland

Re: Sound Practices: Implications of Fintech Developments for Banks and Bank Supervisors

The Structured Finance Industry Group ("SFIG")[1] appreciates the opportunity to respond to the request of the Basel Committee on Banking Supervision (the "Committee") for comments on the above-referenced consultative document (the "Document").

SFIG maintains the core charge of supporting a robust and liquid securitization market as an essential source of efficient funding for the real economy. In recent years, marketplace lending has been an important developing area in the United States and other countries. Marketplace lending leverages the internet, advances in data analytics and other technological innovation to provide an efficient lending product to borrowers and an investment opportunity to investors. Securitization of marketplace lending assets has expanded rapidly. Cumulative U.S. issuance to date, as of 3Q 2017, is $23.8 billion across 96 transactions since the first marketplace lending securitization was issued in 2013.[2] SFIG submits this letter in connection with its members' interest in marketplace lending.

In line with the Committee's approach described in the Document, SFIG recognizes the need for flexible regulatory frameworks, as lenders and their service providers utilize new technologies to provide funding to consumers and small businesses. Flexible regulatory frameworks are essential

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[1] SFIG is a member-based, trade industry advocacy group focused on improving and strengthening the broader structured finance and securitization market. SFIG provides an inclusive network for securitization professionals to collaborate and, as industry leaders, to drive necessary changes, be advocates for the securitization community, share best practices and innovative ideas, and educate industry members through conferences and other programs. Members of SFIG represent all sectors of the securitization market, including issuers, investors, financial intermediaries, law firms, accounting firms, technology firms, rating agencies, servicers, and trustees. Further information can be found at www.sfindustry.org.

[2] "PeerIQ MPL Securitization Tracker (3Q2017)." PeerIQ, 2017, www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0ahUKEwjzzMq_lJvXAhVJ44MKHeFACUUQFgg0MAA&url=http%3A%2F%2Fwww.peeriq.com%2Fassets%2FPeerIQ%2520MPL%2520Securitization%2520Tracker%2520(3Q2017).pdf%3Futm_source%3DPeerIQ%2BWeekly%2BMarket%2BUpdate%26utm_campaign%3Dbb9f3ca2d0-EMAIL_CAMPAIGN_2017_10_10%26utm_medium%3Demail%26utm_term%3D0_1a3ccbed26-bb9f3ca2d0-43357065&usg=AOvVaw1kSQYelfhxQ01ZPe6qkdpk.

to the continuing development of marketplace lending as a mechanism for delivering efficient funding. This letter focuses on three observations and recommendations from the Document that are most important to marketplace lending. As discussed further below, this letter observes and recommends as follows:

- There are very few differences between loans originated via marketplace lending platforms and other forms of lending. Supervisors should keep those similarities in mind when assessing the skills and knowledge needed to supervise marketplace lending.

- Supervisors should revise regulatory frameworks as necessary and appropriate to foster innovation related to marketplace lending and should, as regulatory changes are considered or pending, provide interim flexibility for sound and responsible testing.

- Innovation can foster financial stability and improve consumer protection. Thus, the goals of financial stability and consumer protection, on the one hand, and the facilitation of innovation, on the other, may be pursued in tandem, rather than necessarily requiring trade-offs between them.

SFIG members are pleased to provide these comments on three of the ten Observations and Recommendations that the Committee presents in the Document:

<u>Observation and Recommendation #7</u>

> *Observation*: Fintech has the potential to change traditional banking business models, structures and operations. As the delivery of financial services becomes increasingly technology-driven, reassessment of current supervision models in response to these changes could help bank supervisors adapt to fintech-related developments and ensure continued effective oversight and supervision of the banking system.
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> *Recommendation*: Bank supervisors should assess their current staffing and training models to ensure that knowledge, skills and tools of their staff remain relevant and effective in supervising new technologies and innovative business models. Supervisors should also consider whether additional specialised skills are needed to complement existing expertise.

The Document identifies ways in which fintech may change banking business models. From a supervisory perspective, however, marketplace lending does not represent a wholesale change from other lending businesses. Fundamentally, marketplace lending facilitates loans to consumers and small businesses. While marketplace lending loans may be marketed, sourced, executed and financed in a manner that differs from non-marketplace loans, the loans themselves are essentially the same. Similarly, the origination and execution methods and related technology may differ from the methods and technology for non-marketplace lending, but they are not unique to marketplace lending. Many non-internet based programs provide unsecured consumer loans, auto loans, student loans, small business loans and a variety of other financial products to their customers via similar underwriting processes using data analytics and other technology.

We note that the majority of marketplace loans are originated by a bank (a "Lending Bank"). Applicable supervisors have the same authority over a Lending Bank as they have over any other bank that originates consumer or business loans. Applicable supervisors also have authority over marketplace lending platforms to the same degree that they have authority over other substantial service providers to banks. In addition, marketplace lending loans that are originated by a Lending Bank are done so in accordance with such Lending Bank's credit criteria and underwriting guidelines.

Supervisors should keep in mind the similarities described above—product similarities, process similarities and credit criteria similarities alike—when assessing the skills and knowledge needed to supervise marketplace lending. Marketplace lending may be viewed, from a supervisory perspective, as evolutionary rather than revolutionary.

Observation and Recommendation #9

> *Observation*: Current bank regulatory, supervisory and licensing frameworks generally predate the technologies and new business models of fintech firms. This may create the risk of unintended regulatory gaps when new business models move critical banking activities outside regulated environments or, conversely, result in unintended barriers to entry for new business models and entrants.
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> *Recommendation*: Supervisors should review their current regulatory, supervisory and licensing frameworks in light of new and evolving risks arising from innovative products and business models. Within applicable statutory authorities and jurisdictions, supervisors should consider whether these frameworks are sufficiently proportionate and adaptive to appropriately balance ensuring safety and soundness and consumer protection expectations with mitigating the risk of inadvertently raising barriers to entry for new firms or new business models.

SFIG supports the Document's observation that supervisors should evaluate existing frameworks in order to avoid creating unintended barriers to innovation. Traditional supervisory and licensing frameworks may impede marketplace lending innovations that are of value both to individual and small business borrowers and to the real economy as a whole.

One example of an area that could benefit from increased flexibility and efficiency is document disclosure and execution. Many of the existing prescribed credit disclosure and contract forms are designed to be delivered and executed as paper copies. As borrowers have become comfortable with a loan application and approval process that occurs entirely online, supervisors should consider ways in which the prescribed forms may be adapted to a process that provides for online delivery and electronic execution. An electronic process, for example, presents the possibility for interactive disclosures and contracts that might deliver key information more effectively while reducing the burden and potential for information overload of traditional formats.

SFIG also supports the review of existing regulatory frameworks for unintended gaps. We believe that unintended regulatory gaps must be evaluated to promote innovation in addition to being evaluated to promote safety, soundness and consumer protection.

Supervisors should revise regulatory frameworks as necessary and appropriate to foster innovation. As regulatory changes are considered or pending, we would also encourage supervisors to provide interim flexibility for sound and responsible testing.

Observation and Recommendation #10

> *Observation*: The common aim of jurisdictions is to strike the right balance between safeguarding financial stability and consumer protection while leaving room for innovation. Some agencies have put in place approaches to improve interaction with innovative financial players and to facilitate innovative technologies and business models in financial services (eg innovation hubs, accelerators, regulatory sandboxes and other forms of interaction) with distinct differences.
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> *Recommendation*: Supervisors should learn from each other's approaches and practices, and consider whether it would be appropriate to implement similar approaches or practices.

Observation 10 of the Document suggests that financial stability and consumer protection, on the one hand, must be balanced against the facilitation of innovation, on the other. SFIG believes that those goals may be pursued together, rather than necessarily requiring trade-offs between them. In other words, innovation can itself foster financial stability and improve consumer protection. Marketplace lending is an example of that kind of innovation.

Marketplace lending can foster financial stability because, unlike traditional bank balance sheet lending, it does not require maturity transformation, and it thus reduces "bank run" risk.

Marketplace lending also has the potential to enhance consumer protection because platform lenders offer easy to understand loan products. Moreover, the online origination process can facilitate comparison shopping and may result in lower borrowing costs for consumers, as compared to some traditional consumer lending markets.

We believe that supervisors should aim to foster financial inclusion in addition to financial stability and consumer protection. Innovations in marketplace lending are promoting financial inclusion by making loans more accessible to borrowers in markets with few brick and mortar banks and to borrowers who do not have a home to serve as collateral.[3]

SFIG supports efforts by supervisors to facilitate innovation. We encourage supervisors that have not done so already to consider the ways in which their counterparts in other jurisdictions have promoted innovation.

[3] *See* Julapa Jagtiani & Catharine Lemieux, *Fintech Lending: Financial Inclusion, Risk Pricing, and Alternative Information* (Federal Reserve Bank of Philadelphia, Working Paper No. 17-17, 2017).

We greatly appreciate the Committee's consideration of our comments herein. If you have any questions about this response, please contact Richard Johns, Executive Director of the Structured Finance Industry Group, at Richard.Johns@sfindustry.org or (202) 524-6301.

Respectfully Submitted,

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