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New State Laws Impact Licensing Requirements for Consumer Loan FinTechs and Their Special Purpose Entities

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Connecticut and Nebraska recently adopted statutory amendments to state non-mortgage consumer lending laws that expand licensing requirements. While differing in scope, the common element in the amendments is a keen focus on third-party marketers and servicers that act on behalf of insured depository institutions in connection with the origination and servicing of certain non-mortgage consumer loans in such state. While notable to all who provide consumer financial products, these changes warrant a specific assessment of applicability in connection with the fintech/bank partnership origination model whereby a third party markets, services, and collects affected consumer loans, especially in instances where a special purpose entity (SPE) is used to obtain financing for such third-party activities.

Each state law is discussed briefly below.

Connecticut – Connecticut Substitute Senate Bill No. 1033 (effective October 1, 2023). Importantly, the bill amends the definition of "small loan" to include any loan with an amount or value of $50,000 or less. (The definition continues to retain exemptions that include residential mortgage loans and retail installment contracts.) In connection with these loans, the statutory amendment now provides that any person that acts as an agent, service provider, or *in another capacity* for an insured depository institution must be licensed if: (i) such person *holds, acquires or maintains, directly or indirectly*, the *predominant economic interest in a small loan*; (ii) such person markets, brokers, arranges, or facilitates the loan and holds the right, requirement or right of first refusal to purchase the small loans, receivables, or interests in the small loans; or (iii) the *totality of the circumstances indicate that such person is the lender* and the transaction is structured to evade certain statutory requirements.

The statute further states that the factors that "weigh[] in favor of deeming a person a lender who shall be licensed . . . include but are not limited to the person: (A) indemnifying, insuring or protecting an exempt person for any costs or risks related to a small loan; (B) predominantly designing, controlling or operating a small loan program; or (C) purporting to act as agent, service provider or in another capacity for an exempt person in [Connecticut] while acting directly as a lender in another state."

Based on these definitional requirements, a third-party loan marketer that markets consumer loans to Connecticut consumers on behalf of an out-of-state insured depository institution is generally encompassed within the licensing requirements. Still, it is unclear as to whether such marketer's affiliated SPE (which is created to finance the purchase of the bank receivables) "acts" for an insured depository institution, given that there is generally no contractual privity between the originating bank and marketer/servicer's SPE.

Nebraska – Nebraska Legislative Bill 92 (effective June 7, 2023). This bill amends the definition of "loan" set forth in the Nebraska Installment Loan Act to include any loan to a consumer with an interest rate greater than 16 percent and a principal balance of less than $25,000. The new statutory provision states that a "license shall be required for any person that is not a financial institution who, at or after the time a loan is made by a financial institution, *markets*, *owns in whole or in part*, *holds*, *acquires*, *services*, or otherwise *participates* in such loan." Unlike Connecticut's statutory amendment, the Nebraska amendment does not include a requirement that the party "act" on behalf of a financial institution nor does it require that the entity holding such interest hold the "predominant economic interest" in such loan. Thus, this language reflects an intent to clearly include both a loan marketer/servicer and its affiliated SPE.

Why It Matters

These laws require an assessment of the holders of interests in the covered consumer loans to determine whether licensing is necessary in order to comply with applicable law. Although it has long been the market's view that marketers/servicers and SPEs that hold only significant receivable interests in consumer loans (and not title to such loans nor the entire economic interest in such loans) did not generally require licensing at the state level, a prudent response to these laws would be for potentially-impacted parties to undertake an immediate assessment of *both* the marketer/servicer/nonbank partner *and* the SPE's interests to determine whether licensing is necessary. The lack of a required license may result in the related consumer loans being compromised, including but not limited to being potentially unenforceable by the parties that are expected to enforce them, diminishing the value of such loans as collateral to lenders and securitizations.

Moreover, because some states already have laws similar to those described above (e.g., Illinois), it is likely that interest in state-level regulation of bank partnership activity will continue, given the speed at which it has already been adopted in the first six months of 2023.

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