Consumer Finance Monitor (Season 5, Episode 51): A Look at the Consumer Financial Products Offered by Fintechs and the Regulatory Issues They Raise, with Special Guests Penny Lee, Chief Executive Officer, Financial Technology Association (FTA), and Gerron Levi, Senior Vice President and Head of Government Affairs, American Fintech Council (AFC)

Speakers: Alan Kaplinsky, Gerron Levi, and Penny Lee

Alan Kaplinsky:

Welcome to the Consumer Finance Monitor Podcast, where we explore important new developments in the world of consumer financial services and what they mean for your business, your customers and the industry. This is a weekly podcast show brought to you by the Consumer Financial Services Group at the Ballard Spahr law firm. I'm your host, Alan Kaplinsky. I am the former practice group leader for 25 years and now Senior Counsel of the Consumer Financial Services Group at Ballard Spahr. And I am pleased to be moderating today's program. For those of you who want even more information, don't forget about our blog, consumerfinancemonitor.com. We've hosted our blog since 2011 when the CFPB became operational. So there's a lot of relevant industry content there. We also regularly host webinars on subjects of interest to those in the industry.

So to subscribe to our blog or to get on the list for our webinars, please visit us at ballardspahr.com. If you like our podcast, please let us know about it. Leave us a review on Apple Podcasts, Google or whatever platform you use to access your podcast. Also, please let us know if you have ideas for other topics that we should consider or if you have any thoughts on speakers that we should consider as inviting as guests on our show. So we have a very special show today that I'm very much looking forward to jumping into. But first, I want to introduce each of our participants today and first of all, tell you the topic today is Fintech. And we're going to be focusing not on the what's going on in the economy, what impact inflation has had, that's for the economists to deal with. What we're going to focus on today is the regulatory environment in which Fintech exists and we're going to talk about a number of products that Fintech companies are deploying.

So let me introduce our speakers and we have two people who are extremely well qualified to discuss this topic. We have, first of all, Penny Lee. Penny is the CEO of the Financial Technology Association, a trade association dedicated to educating consumers, regulators and policymakers on the value of technology centered financial services companies. Penny has more than 20 years of communications and business experience advising public officials, Fortune 500 companies, enterprising startup companies and nonprofits, with strategic positioning, political strategy, brand identity and advocacy. She has also worked at the federal and state levels of government, serving as a senior advisor to then Senate Majority Leader, Harry Reid and communications director for former Pennsylvania Governor, Ed Rendell and I might say a former partner and colleague of mine at Ballard Spahr. So Penny, welcome to our podcast show.

Penny Lee:

Thank you so much, Alan. It is a great pleasure to be here today and really appreciate you hosting us. And yes, my former boss is one of your former law partners who have spent quite a bit of hours in the Ballers Spahr headquarters.

Alan Kaplinsky:

I'm sure you've been there. And now, let me introduce to you our other speaker, our other presenter and that is Gerron Levi. She is Senior Vice President and Head of Government Affairs at the American Fintech Council. The mission of the American Fintech Council is to promote an innovative, transparent, inclusive and customer-centric financial system. The association is focused on fostering and supporting responsible innovation. Gerron has more than 20 years as the Government Affairs executive in Washington, advising associations on a range of policy matters, including banking, finance, housing, labor and employment. She served as a senior staff on Capitol Hill and was also elected to the Maryland House of Delegates, where she was a member of the National Conference of State Legislatures and the National Black Caucus of State Legislators. So Gerron, a very hardy welcome to you too.

Gerron Levi:

Well, it's a pleasure to be with you this morning.

Alan Kaplinsky:

Well, we've got a lot to cover and I've got a number of questions I want to pose some for Penny, some for you, Gerron, and some where I'd like to get both of your thoughts on it. So let's get into it. So the first question I had, Penny, is for you. FTA, that's how I'm going to refer to your association, recently held a Fintech Summit in Washington, featuring conversations with regulators, policymakers, founders and industry leaders about the future of finance. What was your goal in convening the Summit and what were some of the themes that came up throughout the day, Penny?

Penny Lee:

It was really interesting. And so we were founded a little less than two years ago, trying to bring together the Fintech industry in a way to look and to examine, to think through what the regulatory landscape needs to be. Are there active policies that we should be pursuing all for the notion of continuing innovation in financial services and being able to bring in the overused word of democratize financial services so they're available for all consumers and small businesses. And so this was an opportunity for us. There is a lot of buzziness around this industry representing many different sectors, payment companies, lending companies, those that are in buy now, pay later, earned wage access and other things. And some of it was to educate, educate policymakers, educate legislators, lawmakers, think tanks, about, A, what these products do, demystifying anything that they don't do but also to reiterate in to, bring to life the impact that they're having.

Right now, we know nine out of 10 individuals, consumers right now use a Fintech product to be able to manage their finances. So why are they doing that? What is the benefits that they're getting out of? And then to dive into some real deep policy issues that are out there, that America, through the regulators or policymakers, should be pursuing rules that they should look at for modernizing but to also have direct conversations with regulators to understand what their concerns are, how the industry should evolve, what the industry should be paying attention to or what concerns that they might have. So it was a series of very active dialogue, a couple of panels and others and all, again, around this notion of as the country is moving to a more digital financial services, what is it that these products do?

How are they being responsible? What we need to do to ensure that this future of finance, one that will involve more digitally based, financial services is ones that's returning value back to the consumer, that has an adherence to the rules and laws for safety and soundness but also bring America forward to catch with the rest of the world and how they're dealing with these various different items.

Alan Kaplinsky:

And now Gerron, I've got a question for you that relates to something you've been involved in. And I'll refer to your trade association by AFC as distinguished from FTA. So in the past, Gerron, you've testified before the House Financial Services Committee on the Community Reinvestment Act. In the most recent inter-agency proposal that regulators have asked whether consumer lending, including auto loans should be evaluated on the main retail lending tests going forward. The tests would consider the volume of such loans relative to the bank's peers in a particular market. And I know AFC has its members, both

banks that do significant consumer lending and are evaluated under the Community Reinvestment Act, as well as non-bank fintechs that might help those banks meet their CRA obligation. How did your trade association land on how consumer lending should be evaluated under the CRA? And I'm assuming by consumer lending, we're not talking about residential mortgage loans, we're talking about other types of consumer lending, either unsecured or secured by something other than a house, like an automobile.

Gerron Levi:

Absolutely, yes, that type of consumer lending. CRA is such an important law. It gives regulators a crucial tool in addressing and remedying systemic inequities and access to credit and financial services for low and moderate income borrowers and communities, consistent with its core purpose. Those inequities could be a result of discrimination or even negative or informational externalities that have led to market failure. So more than anything we want, AFC really wants to respect the value and the importance of this law but also to see it brought into the modern era. The financial marketplace has evolved so much since the law was enacted more than 40 years ago. AFC represents a number of digital banks, banks with non-traditional business models, banks partnering with fintechs to provide consumer financial products and services. CRA's retail lending test, for example, which is about half of the current exam and would make up about 45% of the exam going forward as proposed, has really been focused mostly on mortgage and small business lending.

If a significant amount of a bank's lending isn't in those product lines, let's say the bank is doing largely personal loans and they're doing it largely digitally, not through a bank branch, then how is that bank going to measure up under the new metrics on the exam to achieve a passing grade? And for many of our AFC banks, they really want to stand out in the market and achieve an outstanding CRA rating. So how do you do it? Today, many of our member banks have elected to be evaluated under the agency's existing CRA strategic plan option. And so as a trade, we have been emphasizing to bank regulators that the CRA strategic plan is absolutely key and it's essential that it remain flexible enough to accommodate the full range of business models, delivery systems and product mixes. So that's really where we landed on this. The strategic plan option continues to be key.

Alan Kaplinsky:

Okay. So let's turn now to buy now, pay later or as we'll refer to a BNPL. That has become an enormously popular product. In a sense, a lot of people think that it's been taking a lot of market share away from credit card issuers. Just for our listeners who might not be fully aware of what BNPL is, it's a product typically offered at the point of sale of a merchant, where is an alternative to using a credit card for paying for the goods or services. An individual can sign up for a buy now, pay later transaction, which is payable in four installments.

And typically, there isn't any interest charged to the consumer on the transaction. So if it's a $100 item, the consumer would pay $25 at the date of purchase or delivery and then $25 would be paid in some incremental period of time. It could be weekly, biweekly, it could even be monthly. But there's typically not more than four installments and typically not any interests charged on a BNPL. So my question there, well, and the other thing I guess I ought to mention is that this product is being scrutinized by the Consumer Financial Protection Bureau. It's being scrutinized by a lot of state banking regulators and state attorneys general.

I guess on the basis that it sounds too good to be true that a consumer is able to actually obtain an item by only paying 25% down and assuming that the consumer pays on time, they're able to pay over a period of several weeks. And as opposed to financing with a credit card, where the interest rate could be very significant. Sometimes, for subprime credit card holders could be 25% or more. But notwithstanding that, no good deed goes unpunished, I guess, because the CFPB has written a report or a study on BNPL where they raise a lot of issues and a lot of concerns. And let's go first to you Penny and maybe you could tell our listeners, what's the CFPB concerned about or what tree are they barking up?

Penny Lee:Sure. No, and it was a great overview. And I will say we represent several different players in this industry, so companies that you might have seen when you check out Carne, Afterpay, Zip, Cecil Zilch, PayPal, some of those were asked to participate, many of them were asked to participate in the market monitoring report that the CFPB just recently issued. And we were actually pleased to see in that report that the CFPB does recognize that this does deliver consumer benefits as a lower

payment option with a lower fees, zero, as you said, zero to no interest or zero to little interest. And we're seeing consumers use it because it gives them price certainty, it allows them also to be able to manage their own finances better. Usually, they pay over a course of six weeks and this allows them for... Somebody right now, as we know, 39% of Americans cannot afford a $400 emergency.

And so having a payment option such as a BNPL to allow for you to make payments over a series of six weeks as opposed to upfront, which sometimes is not available, especially for those that can't, or paycheck to paycheck, this allows them to be able to have that safe alternative that gives them budget certainty. And so some of the things that the CFPB raised in their report are wanting to ensure that the consumers have a full understanding of the terms and conditions, that they understand if there are any late fees or any fees attached to it, that they have a full understanding. And I can say through the Financial Health Network survey, they found that 99% of BNPL users understood completely what the terms and conditions are. We did our own survey with Morning Consult, 94% of BNPL users said they understood terms and conditions.

So that is something that we have addressed with the CFPB and continue to ensure, because the thing that is, I think is different than credit cards or other payment options is, these products only work when consumers have a good experience, when they use them on a repeated basis, they are not looking to put them into a debt trap, they're not looking to put them into revolving debt situations, but they're wanting people to satisfy the purchase in the timely matter and in a way that allows them to repeat, use and over and over again. And so some of the concerns also was, are you putting people too far in debt? What we do know is that these products, when you use them, if you do not make a payment, you're cut off from services, so you can't use them again.

That is not something that these companies want. They, again, want that repeated use because they believe that it is a good alternative for payment options and be able to satisfy people. So several of the different things, we've also seen less than 3% actually incur a late fee.

Alan Kaplinsky:

Late fee's aren't all that much, right? I mean it seems like $7 for a late fee.

Penny Lee:

Depending on the different company, some charge a minimum $1, some charge as much as capped at $8. They're very, very de minimus, as to what it is, it's oftentimes like an ATM charge or even less at sometimes. It's funny, there's some that do not charge any late fees as other and I know one of our companies did not used to charge a late fee but they actually found that the incentive of just a $1 late fee actually had people that more incentivized to pay on time. So sometimes that works in a quirky, philosophical or a different philosophical different way. So the other thing that they wanted to make sure is that we understood what the risk tolerance is or what the credit availability of the different consumer is.

Again, distinctive from what the credit cards offer, which is sometimes up to $10,000, these are products that are start, people at a very low minimum, $100, $200 and then over repeated use. If they're showed that they can make on-time payments, regular payments, that they're satisfying their obligations, then they'll start to increase. So it's not that they're putting people into these high credit risk vehicles and trying to put them into an indebtedness so that they can capture fees. Very different. The fees come from their revenue, models come from merchants, not consumers, which is a very different model.

Alan Kaplinsky:

So I know one of the other things that the bureau was concerned about was something they referred to as stacking, where some of the consumers are using the product too much and there's no way for one BNPL company to determine how many other BNPL transactions are outstanding at the same time. So it's a similar issue that's been raised in the payday lending industry about consumers getting into, in over their head, getting into a cycle of perpetual debt, where they're never able to pay anything off. But do you think that's a valid concern, Penny?

Penny Lee:

Well nobody wants anybody to be overextended. But there are safeguards that these companies have put into place. What I just said was, when somebody makes a payment or they miss a payment, they're instantly stopped from incurring anymore indebtedness. They're not allowed to use the product until they've satisfied. So these are low minimum amounts. There's safety, there's consumer protections in there to stop so they don't get themselves in over indebtedness. And again, they want to be able to have customers have an experience so that it's used on repeated basis. There is a pilot, several of the member companies are doing a pilot program in New Zealand, in which they're looking to see, can you look across various different providers and understand either if someone's late on a payment or have overextended themselves. And so that pilot project is going on right now, waiting to see the results on that.

But what they're showing is, as people get used to this product, understand what the payment cycles are like, that you're just not seeing the overuse or not being able to satisfy the obligations because we've heard this a lot and I would say, many of us make multiple purchases on our credit card every month. We use it four, five times, eight times, 10 times a month. Those are all incurring. If you don't pay the full monthly balance, that is incurring anywhere from an 18 to a 36% interest charge on it, whereas if you're using three or four or five different, either same BNPL user, provider or multiple ones, same concept but with a 0% interest. And again, that consumer protection in there that if you are unable to make a payment or haven't been able to make a payment, you're stopped from using the product.

Alan Kaplinsky:

So thanks, Penny. Well, Gerron, what about your association? Do you have anything you'd like to add to what Penny has already said about BNPL and the concerns that regulators seem to be having with it?

Gerron Levi:

Well, I mean, coming back to the point Penny started with, which is that it's important that the report also acknowledges that BNPL has some advantages over legacy credit products, including lowering direct financial cost for consumers. One of the challenges for our trade and the sector in the current regulatory conversation, which is focused a lot on risk management, enhanced oversight, is to remind policymakers and stakeholders that BNPL and a lot of these financial technologies can and are providing benefits for consumers, promoting the three A's I really like to hone in on, availability, accessibility and affordability, really improving the availability of options and choices for consumers, expanding accessibility of credit and financial services across credit risk profiles and lowering the cost for all size financial institutions to provide financial products and services and lowering the price for the consumers.

Done well, that is what Fintech is and can do. On BNPL, for AFC, we have adopted principles consistent with our mission on responsible innovation. First of all, it should be deemed alone so that the consumer is getting disclosures under the Truth in Lending Act, TILA disclosures clearly stating out APR, it's underwritten and ability to repay, ascertain. Third, if late fees are applied, they are fully disclosed and do not exceed 36% APR. And fourth, the business pledges to work with the credit bureaus to avoid harming consumer credit scores and improve reporting. So we've laid out those principles, they're on our website and our biggest BNPL member is a firm and they've been a leader in the category in many ways and have really laid out on paper how their company's practices stack up to the CFPB's report in the areas like the one you mentioned on loan stacking, the areas where certain industry practices could be standardized and improved to safeguard consumers and promote their competition and transparency. So they've laid out across seven areas that the report really pointed up, how their practices line up against that.

Alan Kaplinsky:

Yeah, just so our listeners are aware, under the Truth in Lending Act then, Reg Z is currently written, technically, buy now, pay later transactions, as long as they're repayable in four or fewer installments and there's no finance charge or interest charge and I'm not referring to late fees, that's something else. But if you don't charge a finance charge and it's four fewer installments, you don't have to make disclosures under the Truth in Lending Act, although there might be some state laws that require disclosure. But what I'm hearing from you< Gerron, is that your members either are already providing TILA disclosures, similar to what they'd have to disclose if they were charging interests or if it were payable in more than four

installments. They're already doing that or they're certainly willing for the law to be changed to sweep in BNPL transactions. Have I got that right?

Gerron Levi:

Yeah, I mean, those are our principles and our members are doing that and certainly a firm is doing that.

Alan Kaplinsky:

Okay. So let me turn to another, we've been talking about what the CFPB has been up to and I don't think the second shoe has dropped yet at the CFPB, they've written a report and generally, when they do that, they don't do it in a vacuum, they do it because they intend at some point to take some action. And I don't know whether what they'll be doing will be in the enforcement arena or it'll be issuing a regulation. I tend to think it won't be issuing a regulation because they're rather allergic to issuing full blown regulations that take a lot of time and they have to consider a lot of different comments that people write to the CFPB and they'd rather decide things by fiat.

And that's how things have worked under Director Chopra. He issues guidance and advisories and changes to the exam manual, things that he can just do and not really worry about what other people are doing. But let's talk about what's happening at the state level. I'm going to ask you Gerron, I know you've been focused on state law issues, you convened a session at the National Conference of State legislatures. It includes speakers from the Federal Reserve Bank of Chicago, the Colorado Attorney General's office, the Mercatus Center, what are some of the issues, opportunities, challenges, if you will, that AFC is grappling with in the states?

Gerron Levi:

Well, the states are really active on all issues, Fintech as well. There're true lender issues out there, data privacy issues, AI and algorithms issues and the like for established Fintech and new entrants in the space, it is really a patchwork in the States, a cornucopia of opportunities in terms of new markets and customers, but also a number of potential regulatory perils and landmines on a state by state basis. One big challenge facing the consumer lenders in our trade who are lending through a bank Fintech partnership model is around how states are seeking to enforce their interest rate caps.

AFC as a trade has supported a 36% interest rate cap on consumer loans nationally, and in Illinois, for example. AFC is actually partnered with advocates on this issue. As you can imagine, that's not a popular position with other industry trades but AFC has really staked out a position of advocating for responsible partnerships and those that are sub 36%. But even for responsible bank Fintech partnerships, they can get swept up into legislation and the public debate that is really focused on all types of higher cost and predatory lending. Predatory loans originated under a whole variety of business models that are present on the ground in local communities and online, including lenders that have sovereign immunity and can't easily be captured by state law. So there's a real challenge for members providing personal loans through a bank Fintech partnership model, with anti evasion language, states are adopting to enforce their rate caps, including rate caps that fall below 36%.

Alan Kaplinsky:

That's a real, I mean, a problem that's been ongoing for years. And even before the Fintech industry developed, I, many years ago, used to do a lot of work for payday lenders and they used to... Of course, they charge much higher interest rates than most fintechs charge. Typically, they could be in the triple digits APR, but they would very often partner with the bank and to do what we used to call bank model payday lending. The regulators didn't like that, for sure, either at the state level or at the federal level. Now, you don't see bank model payday lending but you see bank model Fintech lending. And there's some litigation out in California involving opportunity finance, litigating California bank regulator. I know I for one, I'm very worried about that litigation because it's in California and the California courts are known for being very liberal, very consumer-oriented.

I don't recall off the top of my head what interest rate is being charged by opportunity but it's higher. The bank they partner with is charging a higher rate than what the usury is sealing would otherwise be in California. So I'm worried, during the Trump administration, we had a comptroller of the currency or an acting comptroller of the currency who tried to issue by

regulation something that would've dealt with the true lender issue, would've dealt with it with a very, very clear test that if the bank originated the loan in its name, that was the end of the inquiry.

And unfortunately, it got overturned under the Congressional Review Act by Congress. So we're back where we were in this very uncertain environment. And every time I look around, we have a lot of people in our firm who do state licensing work. And what we're finding is even in the states, Gerron, where there is no specific law that addresses the issue, I think Illinois has got a statute, maybe Maine or New Hampshire has one, they're a handful of them now but some of even the other states are very aggressively taking the position that the Fintech companies need to be licensed as lenders, despite the fact that there is no statute saying that they need to be licensed. So I take it you share my concern?

Gerron Levi:

Yeah, I share a number of those concerns and our lenders share a number of those concerns. And these newer provisions that are being enacted in the states are just introduce a lot of risk and uncertainties in what I call the supply chain of credit, creating challenges and getting support to finance loans into those markets. These models really rely on the secondary market, capital markets, private investors, so often, the result is reduce loan volumes or loan sizes into those markets, exiting those markets, less access in that particular market or to some credit risk profiles in those markets. So it really constrains the market. And so that's one challenge. I mean, true lender issues are not new but there is some new language that is being enacted in the state around it.

Alan Kaplinsky:

All right. Let me turn to, and this is a question for you, Penny, the Treasury Department released a report not too long ago on the impact of non-bank firms on competition. The report was the product of President Biden's July 2021, executive order on promoting competition in the economy, can you tell our listeners what were the findings of that report and what does it mean for fintechs in 2023 and beyond?

Penny Lee:

It was a fairly comprehensive, I would say very comprehensive report over a hundred pages. We had conversations with them and welcomed the conversations, as they sought through their process to learn about the individual products, the individual companies, some of the mechanics, especially as it related to AI and machine learning and how they're used in depth about bank Fintech partnerships, the positive aspects of and more understanding limitations or things like that. So we applaud the Treasury Department for releasing this and being such a thorough job in what their examination was and trying to really understand because the one thing that they did come through with the thread was that they do see that there is consumer benefits similar to the CFPB's report. There is consumer benefits to many of the Fintech products. We're seeing this greater adoption, we're seeing that people are choosing millennials and Gen Zs right now.

I think they have 30 to 40 different financial products in which they're using. They no longer what you would consider having a primary bank. And so how are they using these products? What are they doing with them? How does the Fintech engage with the banking industry? What does a bank Fintech partnership look like? And so appreciate the fact that they highlighted that need. And also acknowledge the fact that fintechs are bringing competition into the marketplace and it's changing behavior. One of the things that we saw, over 15 billion in fees for overdraft and non-sufficient funds have been collected in 2019. You have new market entrants that are offering products that do not charge for overdraft, do not charge for non-sufficient funds. And what you're seeing is the traditional banks and others changing their behavior because of it, these harmful fees that were being put onto consumers, again, collected over 15 billion, are now being waived because they understand that, that is unfair to those consumers.

And so we are seeing, and the treasury report acknowledges that the competition that fintechs are bringing are changing behaviors for the benefit of consumers. And so there was a lot to digest in there. There were several different types of recommendations, especially as they look to understanding the arrangement between bank and fintechs, wanting to make sure safety and soundness is occurring, that people understand that have that adequate choice to be able to understand who it is that they're working with and what that realm is. Other things that we also appreciated was the acknowledgement or at least the recognition on, we know the CFPB is working through what they call the 1033 open banking rule.

And that is to state that consumers have the right to be able to share their financial data. It is not owned by a traditional financial institution but it's owned by the consumers and it is the consumer's right to be able to transfer that data, to be able to get the products and services they need, that specialize for them, that fit their need, whether it be a budgeting app or whether it be BNPL or whether it be whatever an investment, a digital investment platform as well. This allows them to acknowledging that, that is that right and so we're also working with the CFPB, not working with the CFPB but they have issued and we'll be making comments as they work through their 1033 rule making to ensure that, that right is continued. So it was encouraging and we appreciate all the thought and thoroughness of which the report addressed and look forward to working on some of the concerns.

Alan Kaplinsky:

So we earlier talked about by now, pay later, there is another product in the marketplace that's becoming more and more pervasive, which I happen to think is a terrific product called earned wage access or we refer to it as EWA and was referred to a little bit earlier in our podcast show. And let me as I did with BNPL, just briefly describe how this product works. There are different ways of structuring it but it's essentially a product that allows a worker who gets paid typically on a biweekly basis to access earnings that, that consumer or employee is already entitled to. In other words, you're usually paid in arrears. If you're paid biweekly for work that you've done in the prior two weeks, under this EWA product, let's say you worked three days, you could if you were had access to an EWA product, you would be able to get whatever compensation you're entitled to, less appropriate deductions.

You would get it in advance of the day you were supposed to be paid. And very often, there's no interest charged for it, it's not something a lot of people in the industry don't really consider it to be a loan or credit because all you're getting is something that you're already entitled to, but yet, there are some consumer advocates that view it differently, think it's loan and that all the disclosures that would otherwise be applicable to consumer loan would apply. So my question for both of you, and we'll start with you Penny and then go to you Gerron, is, what concerns do regulators have about the product? Why isn't this something that everybody can embrace on a bipartisan basis? Why has it become controversial? We'll start with you Penny.

Penny Lee:

And that was a great summary. As we know, life does not happen in 2 week cycles and so people do need access to wages that they've already earned. Just because it doesn't fit into a payroll cycle doesn't mean that they haven't already earned that wage for the day in which they've worked. And so this is a good product, one, allows people to be able to access the pay in which they've already earned. And it's also not only from an employer base but also those that are 1099 workers, those that are gig workers, others that want access to be able to fund whatever needs that they might have. And it is some oftentimes a difference between being able to not have an overdraft fee or not a sufficient fund to be able to pay for those bills in a way that fits their own budgeting needs and cycles.

So for that reason, it's a product that we've enjoyed working with our industry partners on. I think the main issue that CFPB and others have is on the transparency, to make sure that terms and conditions are fully disclosed, that there's not hidden fees in there, that they're not forcing people into paying for a product, even though they say it's a zero interest and there's not some other type of hidden fee that is attached to it that hasn't been disclosed, that consumers fully understand what the payment cycle is, what the terms are required, what it is, if there is an expedited fee, for example, there are some companies that if you want to have access to your wages even earlier and in a very expedited way, they might charge a dollar fee or something for that.

That is all fully disclosed. And so I know our member companies, again, similar to a BNPL, these products work when consumers have a good experience. If they don't have a good experience, it's a competitive marketplace, they'll go to a competitor, they'll go someplace else. And so they want to ensure that consumers have a good experience with their product and that the terms are fully disclosed. There's nothing gotcha moment about it and that they can be able to provide them the service that are needed. So I think the main concern is on transparency, on terms.

Alan Kaplinsky:

Yep. Gerron, what would you like to add?

Gerron Levi:

Well, it's not credit and that's one of the issues that frequently comes up around earned waged access or on-demand pay. These are wages that workers have earned and it's just a matter of getting them earlier. Listen, it is really filling a very important need in the marketplace and it's just a better alternative than so many worse options. It helps consumer avoid and replace payday loan fees, banking, credit union, overdraft fees, bill late fees and loan payment late fees. So it really is an innovation in the marketplace that is really meeting the needs of consumers in a better way. So totally agree, I mean with Penny, really framed a lot of the issues and concerns around.

Alan Kaplinsky:

I guess one of the other things that I've heard the regulators are concerned about are the automatic payments by which the consumer repays the, well, I'm going to call it in advance, it's not really considered to be credit. But let's move on to something else and that is, I think you mentioned this Penny a short while ago, the growing use of artificial intelligence or AI or it's sometimes referred to as machine learning and companies are using it in a lot of different ways. I think the principle use is probably in credit underwriting, it's a different way of determining whether a consumer is creditworthy or not. And there are a number of companies that are out there that have put together AI software that they are making available to not only FinTech companies but traditional lenders, banks, credit unions. But again, the regulators are very suspicious of the use of AI. And so Penny, what's the problem that they're worried about there?

Penny Lee:

Well, before I go into the problems or perhaps the perceived problems, I might talk about the benefits. And that is, we are seeing traditional credit underwriting has not served all Americans. It has not represented a full swath of who would be deemed creditworthy. They're using archaic metrics, metrics that don't necessarily capture the full capability of a consumer's ability to either repay or to be able to have affordable credit. And so by using different models, by using different subsets, by using the different metrics in which people are able to examine and look at how a consumer, what their credit worthiness is, you're opening up just incredible different avenues for affordable accessible credit. And so being able to use AI, machine learning, which you have 30 different subsets, 300 different modeling algorithmic type subsets or data points, instead of just using a monthly pool of, does somebody have a mortgage or do they have a car from a one month pool that people that are not homeowners aren't necessarily properly captured.

So using a fully different dataset, ones in which that can be fully transparent, fully understood, you can get and work with financial institutions such as credit unions, CDFIs, MDIs and others to be able to expand that pool of those that would be deemed financially capable or being able to change the underwriting. At CFBP, I venture to say, over half the complaints that they receive on a monthly basis or around credit reporting, did somebody get an accurate picture? Was it erroneous? Did they capture wrong data? And so moving into the ability for machine learning and others to be able to expand that, to be able to think through in a different algorithmic way, ways in which you can capture that I think is really important. And some of the hesitation around regulators is, some of it is just trying to understand what these new models are doing, to make sure that they're being honed in a way that is not more discriminatory or isn't putting biasness into it.

And so we have seen a real evolution as the industry evolves and as it matures, they only get better as far as their modeling is concerned to be less discriminatory, less biased in and of themselves. And so these are things I think you're going to see a greater adoption. And to applaud Gerron and her organization, they're working on... They've launched a thing called More Than Fair, which really does address this issue too, working across the institution to be able to think through how we do underwriting in a very different way to allow more people access to affordable credit.

Alan Kaplinsky:

Gerron, what does your trade association... What's their position on AI and machine learning?

Gerron Levi:

I mean, among other things, artificial intelligence and machine learning really gives a second look for consumers that traditional models alone might not qualify for a personal loan or to buy a home or car. It can also improve the terms of the loan, the price of the credit. So one of our members collaborated with the Harvard Business School on important research around, quote-unquote, 'invisible' prime consumers that might be overlooked or overpriced by traditional scoring models alone. AI is also helping to reduce friction and cost in financial transactions.

On the question around bias, it's important and concern about bias in AI, I think it's important to start by level-setting on where we are today. There is plenty of bias built into how credit decisions are made today, plain and simple. Average credit scores really are deeply correlated to race in many ways. The real question is how credit scoring and how financial institutions can use AI and alternative data to help make credit decisioning fairer, more predictive, more accurate than today, how we can reduce bias in today's system.

So for example, one of our members, FairPlay AI released great research looking at adverse impact ratios across 30 years of HMDA data, home mortgage data. Finding that mortgage fairness has not really improved meaningfully for Black and Native American applicants. So how do we improve that through the use of AI? I think the White House has been leading important work here with their blueprint on an AI Bill of Rights. NIST has been collaborating with stakeholders on an AI risk management framework. And we were talking about the treasury report earlier but I think they commanded something very important to encourage consumer beneficial innovations.

Regulators should support innovations in consumer credit underwriting designed to increase credit visibility, reduce bias and prudently expand credit to underserved consumers. That's a quote from the report. So I think that command is very important. I think it would help the sector if regulators really coordinated to provide clarity through their risk management, fair lending and third party oversight guidance so that banks and their service providers can understand how to comply with expectations around the use of AI and ML in consumer lending, for example. As Penny mentioned, we're doing a lot of collaborations with consumer... Many of our members are doing great collaborations with consumer advocacy groups around the uses and standards, uses of AI and standards around AI, ML. So those are producing some great results.

Alan Kaplinsky:

Well, we're getting close to the end of our program, but I did want to, in our remaining couple of minutes, just go back to something that was alluded to a little bit earlier. And that is the rule making the CFPB has begun under, pursuant to Section 1033 of Dodd-Frank, which some people have referred to as open banking or open finance. At least Congress intended 1033 of Dodd-Frank to give consumers access to their own data. So the consumers, if they wanted to, could share data that a financial institution has on them as a result of the institution's experience with the consumer, with other companies, Fintech companies, that the consumer wants to be able to give that company access to the data because that company might be able to help tell the consumer, he or she is overpaying for an interest rate on a credit card or some other financing that they have and they could get a better deal by paying off that credit and getting some other type of cheaper credit or they could help with budgeting for consumer.

There's an endless number of things and companies that are out there that want to help consumers in that space. So I'm wondering, the CFPB, it's hard to tell exactly what direction they're going in. The only clue we have is not so long ago, they issued their so-called SBREFA outline, that is they're required before they can adopt a rule to convene a panel of companies, small businesses to advise the CFPB on the impact that the rule is going to have on small business. And in that instance, the CFPB is seeking a lot of information from the small businesses and they identified a whole bunch of questions, hired to read the T leaves there exactly on where they're going. And I talked to a number of clients and some of them don't seem to like the questions they're asking, others don't seem that troubled by it. So this will be our final question of the podcast, first you Penny, what's your reaction to what you've seen so far from the CFPB on that 1033?

Penny Lee:

Well, first, we're glad that the process is starting, as you know, this was part of the original Dodd-Frank, so this is a rule that has been waiting to be promulgated for about 13 years. And so we're just thrilled that the process is starting in earnest and that there is a timeline and a pathway towards getting this into completion. So yes, the first step was the outline around the

SBREFA, the small business panel. They're raising some issues around data portability, privacy, some important questions that need to be asked and need to be addressed because we want to ensure that if a consumer is sharing their data, that it's done in a safe manner and believe that the safety and security around that data being transferred is done without fault. And so there are some important questions that they raise, some ones that we will be addressing in our comment periods, back to them, but it's this notion and we're pleased to see it go forward.

As I said earlier is, and what you just alluded to is that consumers do have the right to be able to transport their data as to what they feel is best for their purpose. It also gives companies better insights, how to better underwrite, how to better assess them for their budget needs, how to better advise them if they're doing investment options or things like that. So it just gives a more complete picture as to who the consumer is, what their needs are, what products and services that might best fit them and their needs. And we see this in other jurisdictions globally. The United States is behind on this notion. You see it being much used in places all over the world with great efficiency and that the consumers aren't having to wait, the financial institutions aren't putting gateways and so they're not having the overdraft fees because financial data wasn't shared in a timely manner.

They're able to get qualified for auto loans because again, in real time, they were able to get the information needed and been able to get that interest rate for a mortgage or other things. So we see true value in having the United States lead on this issue or go forward on this issue, hopefully catch other European and another jurisdictions on this notion, to be able... Again, it's for the outcome of the consumer. They will only benefit from this, from having this ability to be able to have this data shared in a responsible manner, in ways in which that best meet their own individual outcomes.

Alan Kaplinsky:

How about you, Gerron? What can you tell us about how you think the process is going?

Gerron Levi:

Well, I think Penny captured a lot of it very well. I think we're in the process of reviewing and discussing the CFPB's outline but this rulemaking really is a critical step forward in really promoting innovation and competition, ensuring consumers can access and port their own data to use the full range of financial products and services from both new entrants to the financial marketplace and incumbents alike. It will incentivize a variety of companies to compete, to develop and innovate data-driven, customer-centric services for variety of use cases that address a wide range of consumer finance challenges. So I mean, we're pleased to see it moving forward and we really welcome the conversation around it because this is a conversation, where as you've heard both Penny and I talk a lot about during this podcast, where we can really talk about the benefits of these technologies and ensuring that consumers can access them and can exercise their rights around their consumer data.

Alan Kaplinsky:

Yeah, sure. Well, we have come to the end of our program and first, I want to thank our guests today, Penny Lee, Gerron Levi. It was really indeed a pleasure having you on the program to give us an inside view on what the Fintech industry is up to these days, what are the main regulatory concerns and what are the benefits of the various products that the industry is now offering to consumers.

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