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NASAA

September 30, 2015

Submitted electronically via www.regulations.gov

Laura Temel
Attention: Marketplace Lending RFI
U.S. Department of the Treasury
1500 Pennsylvania Avenue NW
Room 1325
Washington, DC 20220

RE: Marketplace Lending RFI / TREAS-DO-2015-0007-0001 / 80 FR 42866

Dear Ms. Temel,

The North American Securities Administrators Association, Inc. ("NASAA")[1] welcomes the opportunity to comment on and work with the Department of the Treasury ("Treasury") regarding the Request for Information, issued on July 20, 2015, entitled "Public Input on Expanding Access to Credit Through Online Marketplace Lending" ("Request for Information" or "RFI"). We appreciate Treasury's efforts to obtain data and information related to online marketplace lending and note that state blue sky law serves an important role in the overall regulatory framework, through the regulation of online platforms and the sale of peer-to-peer notes to investors. As state securities regulators, we have long-standing experience in applying federal and state securities laws and look forward to working with Treasury to achieve the goal of expanded access to credit and support of small businesses and consumers, while promoting safe growth of the industry, including protecting investors.

Securities regulation is a complementary regime of both state and federal securities laws. State securities regulators are responsible for enforcing state securities laws by pursuing cases of suspected investment fraud, conducting investigations of unlawful conduct, licensing firms and investment professionals, registering certain securities offerings, examining broker-dealers and investment advisers, and providing investor education programs and materials. States are also leaders in criminal prosecutions of securities violators.[2] State securities regulators focus on

[1] NASAA is the association of the 67 state, provincial, and territorial securities regulatory agencies of the United States, Canada, and Mexico. NASAA serves as the forum for these regulators to work with each other in an effort to protect investors at the grassroots level and to promote fair and open capital markets.
[2] In 2014 alone, state securities regulators conducted 5,005 investigations, leading to nearly 2,000 enforcement actions, including 271 criminal actions. Moreover, in 2014, 3,585 licenses of brokers and investment advisers were withdrawn, denied, revoked, suspended, or conditioned due to state action.

protecting retail investors, and also serve as the primary regulators of many small or novel offerings.

State securities regulators regularly work with and assist small and local businesses seeking investment capital. States regulate various capital raising ventures, including peer-to-peer lending, state crowdfunding and crowdfunding portals, alternative investment programs including business development companies and real estate investment trusts, and online lenders including accredited-investor focused private placement platforms. As new types of investment products develop and industry evolves, state securities regulators possess the flexibility to craft regulation in the interest of investor protection.

As the RFI explains, online marketplace lending is a rapidly developing and fast-growing sector that creates options for potential borrowers that may not otherwise exist. It is also a relatively small market, as compared to traditional banking, and an evolving market that involves new products and many new, untested companies. As this market grows, it also has the potential to redistribute investment risk and create new risks for investors with various levels of sophistication and risk tolerance. Many participants design their products for retail investors, as alternatives to investments in the stock market and traditional fixed return investments.

The RFI divides online marketplace lending into three categories, including online platforms "formerly known as peer-to-peer." The focus of this letter is on online marketplace lending when securities and/or investment capital is involved, including loans in the form of borrower payment dependent notes.[3] The term "security" is defined broadly under both state and federal law. A "security" includes debt instruments such as notes or other evidence of indebtedness, stocks, and investment contracts.[4] Federal and state securities laws provide regulatory oversight of transactions and dealings in securities. A major component of those laws is to protect investors by ensuring sufficient disclosure of important and material financial information, and to prevent fraud, deceit and misrepresentation in the sale of securities. State securities regulators, unlike the SEC, also have the authority to develop substantive requirements to address new issues with securities offerings as they may arise.

Peer-to-peer lending, as one facet of online marketplace lending, is a growing but opaque market. Investors make blind investments to acquire interests in the profits on loans that are made to unidentified borrowers and receive unsecured, non-recourse notes issued by the intermediary company (i.e., the "peer-to-peer" lender). In other words, investors do not know the actual borrower and rely only on financial and other information provided by the intermediary company. Additionally, only the intermediary has full recourse against the borrower, through the note issued by the borrower to the intermediary company. In this sense, it is not a true "peer-to-peer" transaction. Rather, this transaction is a speculative investment for the investor. The investor relies on an intermediary to conduct due diligence, provide an accurate assessment of the loan, collect payment on the loan, and enforce the borrower's

[3] *See In re Prosper Marketplace, Inc.*, File No. 3-13296 (SEC Nov. 24, 2008).
[4] Securities Act of 1933, § 2(a)(1), 15 U.S.C. § 77b(a)(1); Securities and Exchange Act of 1934, § 3(a)(10), 15 U.S. Code § 78c(a)(10), 15 U.S.C. § 77b(a)(1); UNIF. SEC. ACT § 102 (2002); *see also SEC v. Edwards*, 540 U.S. 389 (2004) (holding that "an investment scheme promising a fixed rate of return can be an 'investment contract' and thus a 'security'").

obligations under the loan. The intermediary ranks the borrowers' credit worthiness based on proprietary algorithms not disclosed to the individual investor. There are substantial risks to the investor, including transfer of the majority of risk of delayed payment or even non-payment to the investor through decoupling of the loan transaction. The investor assumes not only the risk of non-payment or default by the borrower but any poor performance or stressed financial condition of the intermediary, which is not subject to traditional bank safety and soundness regulation.

As with any other type of security, investment in peer-to-peer lending involves regulatory oversight. State securities regulators review these offerings and impose disclosure standards and investor protection requirements. Those provisions may include "suitability" standards such as investor concentration, net worth and/or income requirements. States also exercise anti-fraud authority to protect distressed investors. In our experience, online offerings present unique challenges such as creating a dispersed investor base that can be hard to communicate with or manage. They also present certain licensing requirements for intermediaries.

In order to facilitate investor, and borrower, confidence in peer-to-peer transactions and online offerings, a robust financial and securities regulatory framework is critical. This is particularly important in light of the investors' risk of non-payment under non-recourse notes and the harm that may be incurred by retail investors attracted to fixed rate returns. Moreover, securities purchased in peer-to-peer offerings are not traded on recognized national securities exchanges and thus investors generally must hold their investment until maturity as there is no liquid resale market. While alternative resale marketplaces exist, they are highly illiquid and have reduced disclosure standards. This presents investor protection concerns, particularly with respect to older investors, who may be attracted to higher advertised fixed rate returns than traditional fixed rate investments that are more secure and liquid. Federal and state securities laws address applicable resale exemptions.

NASAA and state securities regulators look forward to working with Treasury to understand and address the changing landscape of marketplace lending and to determine the impact on retail investors. NASAA reiterates its support towards the Department's goal of studying the potential for online marketplace lending to expand access to credit and how the financial regulatory framework can support the safe growth of this industry.

Should you have any questions regarding the comments in this letter, please do not hesitate to contact Joseph Brady, NASAA's Executive Director, at jb@nasaa.org, or Anya Coverman, NASAA's Deputy Director of Policy, at ac@nasaa.org, or 202-737-0900.

Sincerely,

Judith M. Shaw

Judith M. Shaw
NASAA President
Maine Securities Administrator