February 15th, 2016

Mark Pearce
Division of Depositor and Consumer Protection
Federal Deposit Insurance Corporation
1701 “G” St., NW
Washington, DC 20006

Dear Mr. Pearce:

We would like to express our concerns over two new products offered by Republic Bank of Kentucky.

The Elastic Line of Credit

Our first concern is the Elastic Line of Credit. Elastic Lines of Credit are originated by Republic Bank but marketed to consumers through Elevate. Elevate is a Texas non-bank lender. It has three products ("Rise," "Sunny," and "Elastic") with interest rates of as high as 1,200 percent.

An Elastic Line of Credit can extend between $500 and $3,500 to a borrower. Borrowers make either bi-weekly or semi-monthly payments for a period of up to 10 months. The table that appears at the end of this letter details the repayment schedule for an $800 advance. We sourced this schedule from Elastic’s web site. Because the borrower pays an upfront origination fee, the total cash extended to the borrower at the time of issuance is only $760. In lieu of interest, the borrower pays a “minimum charge fee.”

While different estimates have been applied to evaluate the cost of the ELOC, all conclude that it is very expensive. The OCC’s interest rate tool puts the APR of this loan is 118.6 percent. An alternative calculation is to use an internal rate of return. The product’s internal rate of return is 169 percent. An IRR calculation is actually more appropriate for this loan, as the payment amounts are not the same in all periods. Elevate uses a third calculation, the weighted average effective APR, which characterizes the product at 88 percent. Regardless, this is clearly a loan whose cost is well beyond 36 percent. While loans at this interest rate would be illegal under many state laws, Elevate is avoiding those restrictions by partnering with a bank. This description was recently published in the Financial Times:

> *Republic Bank and Trust Company, the Kentucky bank, lends to the public and pays Elevate a fee for its underwriting and branding. These partnerships are not uncommon for the simple reason that while non-bank lenders have to obey state usury laws in the US, banks are granted the right to avoid local interest rate caps and instead abide by the rules of their home state*[1].

This is reminiscent of the rent-a-charter model that was once used to fund payday loans.

Following the Money

Three financial institutions work together to offer this product: Republic Bank, Elevate, and Chicago hedge fund Victory Park Capital.

Consumers understand the Elastic Line of Credit to be a product of Elevate. Elevate is responsible for marketing. It screens the applicants and operationalizes underwriting. It is Elevate that pre-approves and solicits new accounts through direct mail marketing.

Once the consumer has completed the application, the loan is originated by Republic. Republic holds on to a portion of the loan after origination. The rest flow into a stream of payments and obligations in a complex supply chain that involves hedge funds, variable interest entities ("VIEs"), special purpose vehicles ("SPVs"), credit default swaps, and securitized loans.

Victory Park Capital is the financier to Elevate. Victory Park Capital Management, LLC, a subsidiary of Victory Park Capital, has issued a $335 million credit facility to Elevate. Those funds are used across all of Elevate's operations.

Victory Park Capital Advisors, described by Elevate as "an affiliate" of Victory Park Capital, has also issued the loan that funds Elastic SPV. That loan is referred to as the ESPV (Elastic Special Purpose Vehicle) credit facility. Victory Park Management LLC charges interest of 13 percent plus a spread based upon the 3-month London Inter-Bank Overnight Rate to Elastic SPV.

Elastic SPV is a stand-alone special purpose vehicle. Elastic SPV bases itself in the US Cayman Islands in order to qualify for lower tax liabilities. The performance of its loan portfolio impacts the financial performance of both Victory Park and Elevate.

With dollars loaned to it from Victory Park Capital Advisors, Elastic SPV buys the participation rights to 90 percent of the proceeds from Elastic Line of Credit accounts. They are purchased from Republic Bank. Republic Bank holds the right to 10 percent of future cash flows.

Elevate then enters into a credit default protection agreement with Elastic SPV. Effectively, Elevate is insuring Elastic SPV against higher-than-expected loan losses. Indirectly, Elevate's assumption of the risk acts as a credit enhancement to Victory Park Capital Management (the lender to Elastic SPV). In exchange for that downside risk, Elevate earns a premium from Elastic SPV.

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[1] Shubber, Kadim. "Why This Subprime Lender Funds Loans through the Cayman Islands." Financial Times. January 19th, 2016. http://ftalphaville.ft.com/2016/01/19/2150488/why-this-texas-subprime-lender-routes-loans-through-the-cayman-islands/

While Republic is not the only responsible party to this process, it is fulfilling a necessary role. Without the regulatory privilege afforded to the bank by the virtue of its charter, the other players would not be able to do business at these rates of interest. We believe that their role is essentially a new iteration of the "rent-a-charter" model.

Concerns over the Outsourcing of Underwriting to a Third-Party

We believe that the underwriting associated with the loan may not be appropriate for an FDIC-regulated institution. Elevate does not use traditional tools like credit scores. Rather, Elevate incorporates a variety of alternative data points into its scoring model. In their most recent filing, Elevate does provide some description of their unusual approach:

> *We assess over 10,000 data inputs while developing our segmented credit models and are currently using the 11th generation of our proprietary credit scoring model...We have built a team of over 35 data analysts in our Risk Management department including 25 staff members with advanced degrees and ten with PhDs. Our Advanced Analytics team is primarily focused on analysis of new (typically non-traditional) data sources and analytical techniques.*

But this must prompt the question of how these practices interact with rules like the Fair Credit Reporting Act, the Equal Credit Opportunity Act, and perhaps the Bank Secrecy Act.

Elevate acknowledges that it falls under regulatory supervision for each of those laws. But we believe that the FDIC should explore the question of how Republic Bank's participation in the Elastic Line of Credit fits within these laws. We are concerned that the use of Elevate's underwriting information puts Republic in the position of violating these rules.

The 2015 Advisory on Effective Risk Management Practices for Purchased Loans and Purchased Loan Participations[2] would seem to support these concerns. The Advisory holds banks accountable for the credit analysis used by third-party underwriting. The FDIC said

> *"Financial institutions that purchase loans or participations should perform the same degree of independent credit and collateral analysis as if they were the originator… This assessment and determination should not be contracted out to a third party. To the extent the purchasing institution relies on a third party's credit models for credit decisions (such as for consumer credits), the institution should perform due diligence to assess the validity of the credit model."*

This suggests that it is not possible to firewall a lender from expectations for compliance with rules governing the provision of credit.

Further, we ask the FDIC to review how Republic's role in the product conforms to other pre-existing regulatory standards:

Interagency Guidelines Establishing Standards for Safety and Soundness (2000): Institutions are accountable for loan documentation, credit underwriting, and asset quality. This guidance is specific that banks should verify that a borrower has the ability to repay a loan.

[2] https://www.fdic.gov/news/news/financial/2015/fil15049a.pdf

Guidance for Managing Third-Party Risk (2008): Institutions that enter into arrangements with third-parties should make sure that policies are in place to control risks. This has been applied in the past to relationships between banks and independent tax preparers, where those preparers were facilitating refund anticipation loans originated by banks.

Final Joint Guidance on Leveraged Lending (2013): Institutions that purchase participations in loan portfolios should conduct a "thorough and independent examination before committing funds."

The use of social media is a related area that may be of concern. In 2013, the FDIC and other bank regulators published a guidance on the use of social media in underwriting[3]. The report noted that the use of social media could conflict with consumer protection, compliance, and reputational risk rules. Elevate does not reveal the contents of its model. However, they have disclosed that they advertise on Facebook.

It would set a dangerous precedent to allow banks to avoid responsibility for complying with existing law if they could merely outsource their underwriting to a third party.

Easy Advance Tax Refund Related Loan

Republic Bank has also created a new refund loan product for tax refunds. It is slightly different than past approaches, as the new pricing system generates fees not from consumers but instead from tax preparers. The preparer pays a fee of $35 to facilitate the distribution of an advance of up to $750 to the filer

Republic describes the product as a "tax-refund related loan," but not "the actual tax refund."

Tax preparation pricing has become far more opaque. Consumers may believe that they are now accessing a free advance product. But businesses do not provide services for free. Banks do not take risk for free. These loans are not free. Republic has redeployed a product in a deceptive package, using a la carte pricing as a means of evading the law.

To our point about deception, consider how one service bureau described the free tax refund advance product that they were offering in conjunction with a non-bank lender:

> *With our free bank products, we're confident that even after this fee, your clients will save an average of $20 to $60 per return when compared to your current software provider's bank product fees, state bank fees, transmission fees, technology fees, and other junk fees. This is money you can stick directly into your own pocket by increasing your own prep fee $20 to $60 per return, while keeping the overall cost to the client the same as last year.*

This is a communication intended for tax preparers, but it shows how consumers are being duped by deceptive pricing.

As well, this product undermines the safety and soundness of the bank. Republic takes between 24 and 48 hours before disbursing an advance. This means that advances will be made before the IRS has approved the return. If it happens that the IRS subsequently rejects the refund or reduces the size to less than the amount of the advance, then Republic Bank takes the loss.

We believe that the FDIC should act to prevent Republic from continuing its role in these programs.

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[3] http://www.occ.treas.gov/news-issuances/bulletins/2013/bulletin-2013-39.html

We appreciate your ongoing concern for the needs of consumers.

Sincerely,

Reinvestment Partners
110 E. Geer St.
Durham, NC 27701

Woodstock Institute
29 E. Madison St., #1710
Chicago, Illinois 60602

New Economy Project
121 W. 27th St., Suite 804
New York, New York 10001

California Reinvestment Coalition
474 Valencia St., Suite 230
San Francisco, California 94103

Elastic Line of Credit Loan Repayment Schedule

Date	carried over principal	principal payment amount	Plus minimum charge fee	remaining principal	Borrower Cash Flow
1-Jan			$40 cash advance fee	$ 800	$760
15-Jan	$ 800	$40	$40	$ 760	-$80
29-Jan	$ 760	$40	$35	$ 720	-$75
12-Feb	$ 720	$40	$35	$ 680	-$75
26-Feb	$ 680	$40	$30	$ 640	-$70
12-Mar	$ 640	$40	$30	$ 600	-$70
26-Mar	$ 600	$40	$25	$ 560	-$65
9-Apr	$ 560	$40	$25	$ 520	-$65
23-Apr	$ 520	$40	$25	$ 480	-$65
7-May	$ 480	$40	$20	$ 440	-$60
21-May	$ 440	$40	$20	$ 400	-$60
4-Jun	$ 400	$40	$15	$ 360	-$55
18-Jun	$ 360	$40	$15	$ 320	-$55
2-Jul	$ 320	$40	$12	$ 280	-$52
16-Jul	$ 280	$40	$12	$ 240	-$52
30-Jul	$ 240	$40	$12	$ 200	-$52
13-Aug	$ 200	$40	$8	$ 160	-$48
27-Aug	$ 160	$40	$6	$ 120	-$46
10-Sep	$ 120	$40	$4	$ 80	-$44
24-Sep	$ 80	$40	$2	$ 40	-$42
8-Oct	$ 40	$40	$ -	$ -	-$40
Totals		$800	$371		$1,171