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New Avenue for a Taxi Banker: Online Lending

By Allison Prang and Kevin Wack
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Another small bank is turning to the online lending sector in an effort to boost profits.

Benefits of being a bank: "We don't believe that the marketplace lenders will get national charters," said Andrew Murstein, Medallion's chief executive.

Medallion Financial Corp., which operates a $1.1 billion-asset bank, recently announced plans to start originating loans on behalf of digital lenders. The firm joins a crowded field of small banks that already compete for this business, including WebBank, Cross River Bank and Celtic Bank.

Medallion, which has long specialized in financing the purchase of taxi medallions, has been seeking to diversify its business model. In many cities, taxi medallions have lost value as ride-sharing apps like Uber and Lyft have grown popular.

Weakening loan performance is what hurt Medallion in the taxi lending business. And from the standpoint of credit quality, issuing loans on behalf of online lenders, which are sometimes called marketplace lenders, is a low-risk endeavor.

Salt Lake City-based Medallion Bank plans to hold onto the loans only for a single day or so. The firm will reap a fee from each transaction.

"We're not going to take the risk," said Andrew Murstein, Medallion's chief executive officer. "In a way, this is just a service to the online lending community."

But joining the online lending party does bring another kind of risk — specifically, the chance that the rules of the road will change.

Online lenders pursue these partnerships because banks have a unique regulatory advantage: they have the right to export their home states' interest rate rules across the country, rather than having to adhere to state-by-state rate caps. By purchasing their loans from banks, online lenders avoid having to get licensed in every state where they make loans.

However, a 2015 court decision has sparked doubts about whether the online lending sector's efforts to avoid state interest-rate caps by partnering with banks will be allowed to continue.

Furthermore, if online lenders eventually obtain national charters, an idea that has recently been floated by the Office of the Comptroller of the Currency, those firms will have less reason to partner with banks.

Finally, banks that enter this line of business can expect heightened scrutiny from their regulators, said Brian Korn, a partner at Manatt, Phelps & Phillips. "I think there are certainly risks involved in starting a new third-party funding platform," he said in an email.

But for now, New York-based Medallion sees an opportunity.

"We did a lot of research into it," Murstein said. "We don't believe that the marketplace lenders will get national charters."

With regard to the much-ballyhooed court case, Murstein noted that the final outcome has yet to be determined. He also said that Medallion plans to keeps a small part of each loan on its own balance sheet, which should make the bank's partnerships less vulnerable to legal challenges.

Medallion first expressed interest in dipping its toes into marketplace lending five years ago, but at that time the sector was still too new for regulators, according to Murstein.

More recently, the market has grown, and the regulators have calmed, he said. Medallion's regulators include the Federal Deposit Insurance Corp. and the Utah Department of Financial Institutions.

Earlier this month, Medallion publicly announced its plans to enter the sector. Since then, seven online lenders have expressed interest in working with the company, according to Murstein.

Medallion has accepted only two customers — Murstein did not name the firms because of confidentiality agreements — and wants to start originating loans in January.

The bank plans to tread into this new market slowly, which is why it is only working with a small number of potential customers, Murstein noted.

"We want to just take it step by step and be cautious," he said. "The regulators did tell us you have to be very careful and concerned about compliance issues and not to slip up … we want to make sure that all of our systems are in place so we don't make any mistakes along the way."

Medallion hopes to convince online lenders to sign exclusive agreements, Murstein said. But he also noted that Medallion could serve as a pinch hitter for web-based lenders that are unable, for whatever reason, to get loans through their primary bank.

"A lot of these companies need back-up banks … even if they're working with WebBank, they've expressed interest in working with us as a back-up," he said.

Banks that partner with marketplace lenders do not typically release information about the fee income they collect from this line of business. But there are indications that banks already in the business are profiting handsomely.

WebBank reported a 49.9% return on equity as of March 31, while Cross River Bank reported a 24.2% return on equity. The average return on equity for banks with $100 million-$1 billion in assets was 9.5%.

Murstein said that he expects Medallion's online lending business to earn $10 million before taxes in 2018, which would increase the firm's earnings by 25 percent.