

Michigan Reverses Longstanding Ban on Loan Referral Payments

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For many marketplace lenders, loan referrals are an important source of new customers. But Michigan has for some time banned some lenders from paying for loan referrals. Nonbank financial institutions licensed under Michigan's Regulatory Loan Act are subject to Rule 493.20 of the Michigan Administrative Code, which provides that a licensee "shall not pay any person for loan applications or recommendations."

Some have argued that the inability to pay for loan referrals in Michigan has kept the state out of the modern lending marketplace. This appears to have moved the Michigan legislature to ease the prohibition against loan referrals by enacting amendments to the Regulatory Loan Act that would permit licensees to pay for loan referrals, subject to certain limitations.

Michigan's Senate Bill 238 amends the Regulatory Loan Act by adding a new provision that permits a licensee to pay a fee for locating or referring a potential borrower to the licensee, provided that both of the following conditions are met:

1. The potential borrower is not directly or indirectly charged for all or any part of the fee, if he or she enters into a loan with the licensee, and
2. The amount of the fee does not exceed \$500.

While the new law is a significant improvement of the current rule, there are some elements that are not ideal. The condition that a potential borrower may not be "directly or indirectly charged" any part of the fee suggests that a lender cannot pass the cost of loan referrals on to the borrower through the finance charge or other fees. Prudent lenders will want to keep records demonstrating that the pricing of their loans to Michigan residents does not change based on whether compensation was paid to a referral source. In addition, the flat \$500 cap on fees may not work well with referral programs in which fees are based on loan amount or volume. Accordingly, Michigan lenders may need to adjust their referral programs in order to take advantage of the new opportunity to use paid referral sources.

The provisions of Senate Bill 238 will be codified into Michigan Compiled Laws § 493.12(6). The bill was enacted into law on November 20, 2017 and takes effect as of February 19, 2018.

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