

California Court Rejects DFPI Fintech True Lender Challenge

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Stemming from a case filed in 2022 against the fintech Opportunity Financial, LLC (“OppFi”), the Central District of California issued a decision on May 19 finding that OppFi’s bank partner, FinWise Bank, was the true lender with respect to consumer loans made through their bank-fintech partnership. The California Department of Financial Protection and Innovation (DFPI) is one of several state banking agencies that have sought to establish when a bank actually is a “true lender” for loans that are made, usually to consumers, through programs managed by a bank-fintech partnership. This opinion provides additional insights into what kinds of arrangements in a bank-fintech partnership are necessary to demonstrate that the bank is operating as the true lender, including some useful commentary parsing through the common practice of the fintech recommending loans for approval by the bank and whether that practice usurps the bank’s independence in underwriting loans.

In the partnership between FinWise Bank and OppFi, [as described in the opinion](#), “OppFi’s platform allows banks to provide access to simple short-term lending products for consumers whom traditional lenders may otherwise turn away in light of their credit profile.” Further, “[t]he loan products offered by the Bank provide transparent pricing, have no origination or late fees, are fully amortizing with no balloon payments, and allow borrowers to prepay at any time with no penalty.” These loans have a higher credit risk and therefore “charging higher interest rates is necessary to make small-dollar lending . . . economically viable” and so the banks that want to serve this market are often located in state that “do not set low-interest rate caps relative to credit risk.” In other words, FinWise Bank exports its home-state interest rate into other states, such as California, that have lower interest rate caps.

The DFPI alleged that the arrangement between FinWise Bank and OppFi constituted a “rent-a-charter” arrangement so that the bank “appears on paper to be the ‘lender’ on high interest loans . . . while the non-bank lending company (here, OppFi) performs the actual duties of a real lender such as marketing, underwriting and servicing. [And a]lthough the . . . bank purports to originate the exorbitant interest loan, it immediately sells the loan to the non-banking lending company or the bulk of the receivables.” In other words, DFPI claimed that OppFi was the true lender for these loans and because the loans carried a higher APR than permitted in California, the loans were usurious.

To defend against these charges, the Court describes OppFi’s arguments as being “independently sufficient.”

The first argument is that FinWise validly made these loans, demonstrated by all of the following facts: 1) The promissory notes were between the consumer and FinWise; 2) FinWise funded the loans; 3) FinWise held the loans for a couple of days; 4) sold a portion of the loan receivables; 5) held title to the loans for 30, 60 or 180 days after they were funded; 6) assigned a portion of the loan receivables to OppFi; and 7) retained a portion of the loan receivables after fund the loan for 60 or 180 days.

The second argument was that because FinWise was the originator and funder of the loans, and not OppFi, the loans were not subject to the interest rate caps dictated by California law.

The third argument was that FinWise was demonstrably the “true lender” of the loans and was “not a dummy or sham lender.” On this last argument, the court found that FinWise was the true lender for all of the following reasons -- FinWise: 1) controls the application and underwriting processes; 2) independently underwrites the loans and actually rejects some loans that are recommended by OppFi for approval; 3) oversees OppFi’s proprietary credit models; 4) uses its own funds to originate the loans; 5) retains title and ownership of the loans and only sells receivables; 6) gains a financial benefit from the loans; 7) has material risk of loss from the loans; 8) controls the marketing of the loans; and 9) oversees legal compliance of the loans.

In terms of the question regarding whether the loans could be deemed usurious, the Court hearkened back to a 1932 California Supreme Court case that found that the loan “contract must in its inception require a payment of usury or it will not be held” to be usurious and clearly stated that there is no authority for the DFPI’s argument that “the assignee of an exempt lender becomes thereby a usurer” because they are not also exempt. Citing a different California case from 1979, the Court also re-stated that “a contract, not usurious in its inception, does not become usurious by subsequent events.”