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MONEY & INVESTING

California Probes Online Lenders

Requests are sent to 14 companies for details about their lending practices

By Ruth Simon

State regulators in California have launched an inquiry into the fast-growing marketplace lending industry.

On Thursday, the **California Department of Business Oversight**, which oversees securities and lending activity in that state, sent requests to 14 companies for details about their lending practices, investors and business models, a person familiar with the inquiry said.

Firms receiving the requests include **Kabbage** Inc., Prosper Marketplace Inc., Avant Inc., **On Deck Capital** Inc. and **Social Finance** Inc., according to representatives for those companies. Representatives for Avant and OnDeck Capital declined to comment further, while the others said they planned to respond to the requests. The full list of companies receiving the letters couldn't be determined.

The information will be used to help determine whether these firms and others are operating with appropriate licensing and supervision under California law and whether changes to state securities and lending rules are needed, said an official with the Department of Business Oversight.

CHRIS RANK/BLOOMBERG

The leadership of Kabbage at their offices in Atlanta.

Marketplace lenders originated roughly $14 billion in consumer and small business loans in the U.S. in 2014, according to Morgan Stanley, which estimated that marketplace originations of unsecured consumer loans alone would total roughly $15 billion this year.

Plans for the California inquiry began well before investigators discovered that one of the shooters in the San Bernardino, Calif., attack took out a loan from Prosper, the San Francisco-based online lending platform, in the weeks before the shooting.

In a statement released after the shooting, Prosper said that, "all loans originated through the Prosper platform are subject to all identity verification and screening procedures required by law, including U.S. antiterrorism and anti-money laundering laws."

Marketplace lending is facing increased scrutiny, amid concerns that some business owners and consumers may not fully understand the terms of the loans they receive and questions about whether the industry is being appropriately regulated.

In a study released in August, researchers at the Federal Reserve Board and the Federal Reserve Bank of Cleveland found that small-business owners have difficulty comparing credit products offered online by alternative lenders. Some lenders, for instance, provide customers with the amount to repaid daily, rather than an annualized interest rate.

Lenders contacted by The Wall Street Journal said they look forward to responding by the state's March deadline. "At SoFi, fairness and transparency are critical factors in our partnership with our members, and we strive to have an equally transparent approach with regulators," said Debra Jack, a Social Finance vice president.

"We welcome the opportunity to engage with regulators to ensure that small businesses have access to the products and services they need to grow," said Rob Frohwein, chief executive of small business lender Kabbage.

A Prosper spokeswoman said the lender is, "happy to work with the Department to understand our company and the industry."

Separately, this summer, the U.S. Treasury Department requested comments on the benefits and risks associated with new online lending platforms.

Treasury officials are still analyzing the nearly 100 responses to that request from individuals, businesses, advocates and trade groups.

Unlike the Treasury study, the California inquiry asks for specifics about the lenders' operations, both in the state and nationally.

DEBT

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sifying fears among analysts and traders that the worst could yet be ahead. Its shares fetch less than $5 and many of its bonds between 30 and 40 cents on the dollar, down from close to 80 cents just three months ago.

The decline in oil and gas prices this week has renewed concerns among investors that Chesapeake and other U.S. energy producers will be unable to repay bondholders if commodity prices don't recover.

Bonds from other low-rated producers have fallen, too: Through Wednesday, Oasis Petroleum Inc. bonds are down 9.1 cents over the past week to about 78 cents on the dollar, and bonds from EP Energy LLC are down 10.5 cents to 67, according to data from MarketAxess Holdings Inc. A bond from California Resources Corp. is trading around 45 cents, down about 15 cents since the start of December.

Production firms aren't alone. Bonds from utilities including Dynegy Inc., AES Corp. and NRG Energy Inc. have declined in recent days, reflecting concerns that falling natural-gas prices will drag down electricity prices. "We're flirting with credit-crisis energy prices, and we're probably flirting with credit-crisis bond prices to some degree in these sectors," said Henry Peabody, who helps oversee the $1 billion Eaton Vance Bond Fund.

To reduce debt, Chesapeake is offering investors a bond swap for up to $1.5 billion of new debt. Investors who agree get hit with a principal reduction but also get a lien on the company's assets, increasing the odds they will ultimately get much of their money back. It is a tactic analysts say more companies likely will be forced to attempt. Some already have completed similar deals, such as SandRidge Energy Inc. and Halcon Resources Corp.

Many analysts don't think it will be enough. On Dec. 3, a day after Chesapeake's exchange offer was announced, analysts at research firm CreditSights said they expected the company to file for bankruptcy in 2018 barring a significant improvement in commodity prices. They changed their view on Chesapeake bonds to "sell" from "hold," and reaffirmed the "sell" recommendation in a note on Wednesday.

Chesapeake declined to comment.

Not all are downbeat. Jason Wangler, managing director at Wunderlich Securities, has a "buy" rating on the stock and a price target of $13. The exchange offer should reduce the firm's debt load, giving it more flexibility to weather the oil-and-gas environment. Mr. Wangler said the firm still had some options, including selling assets when energy prices recover, a strategy management had been pursuing before prices dropped.

But others doubt energy-company investors will get out unscathed. The losses in the junk-bond market are "a precursor of a period of substantial defaults," said Matt Freund, chief investment officer and portfolio manager at USAA Mutual Funds, which has been underweight bonds from junk-rated energy producers. "There are absolutely going to be a lot of defaults baked in the cake here."

Treasury Auction Suits Filed Against Banks Go Forward

By Aruna Viswanatha

A string of investor lawsuits accusing major banks of manipulating Treasury-debt auctions moved forward this week, as the cases were consolidated before a federal judge in New York. The legal battle has major stakes for one of the world's largest financial markets.

The cases are moving on a parallel track to related government investigations by federal prosecutors and the top U.S. commodities regulator, who have asked banks to turn over information in connection with the probe.

The U.S. Judicial Panel on Multidistrict Litigation on Tuesday moved at least 39 private-investor cases—filed in districts including New York, Chicago and the Virgin Islands—to the jurisdiction of Manhattan federal Judge Paul Gardephe, who was already overseeing the bulk of the complaints.

The panel said the actions had common questions of fact and centralizing the cases in New York would be convenient for the parties and witnesses.

The suits allege that primary dealers conspired to manipulate the pricing of both U.S. Treasury securities at auctions overseen by the New York Fed as well as a derivative tied to those prices.

The banks haven't responded in court to the allegations.

The next main step for the suits is expected to be a decision by Judge Gardephe to appoint a law firm from one of the investor cases to serve as lead counsel in the consolidated cases. That process that is likely to take several months.

The $12.8 trillion Treasury market has emerged as the latest focus for law-enforcement officials, regulators and plaintiffs' attorneys looking for evidence of misconduct by Wall Street banks.

Many of the world's largest banks have rung up billions of dollars of fines and settlements in the wake of accusations they manipulated interest-rate benchmarks and foreign-exchange markets.

The government probes of the Treasury market remain in the early stages, and investigators are unsure yet whether they can substantiate the private allegations, people familiar with the matter said.

The Treasury market is arguably the deepest in the world and the baseline for pricing a wide range of other assets.

Treasury prices influence rates on everything from mortgages to car loans, and they act as a barometer of economic health. During market routs, investors flock to Treasurys because they are typically bought and sold more easily than other securities.

VALERIAN MAZATAUD/BLOOMBERG NEWS

A Glencore zinc mine in Canada. The firm says lower costs from its trading arm will buoy earnings.

MINER

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The company also is looking at further sales of precious metals, copper and possibly even infrastructure, he said.

Glencore has been hammered, along with other miners, by a slump in commodity prices stemming from an economic slowdown in China, the world's largest consumer of raw materials, and a sudden ramp up of supplies following years of investment in mine expansion.

The price of copper, Glencore's largest earnings driver, hit a more than six-year low last month and is down 27% this year at $4,854 a metric ton as of Thursday. Still, Mr. Glasenberg said the company had free cash flow of $2 billion a year and could generate cash even if copper prices fell to $3,500, a level even the most bearish analysts haven't predicted.

"We have many levers we can pull in this company," he said. "We will pull them when required."

Glencore said it is still generating positive cash flow at current spot prices at all of its assets that are fully operational except for two. The company is deciding whether to close its unprofitable Murrin Murrin nickel operations in Australia and its Sherwin alumina operations in the U.S. It is still trying to turn around its Koniambo nickel operations in New Caledonia, but Mr. Glasenberg said the company has "no intention to...burn cash." Glencore also said it would further reduce capital expenditures this year and next.

BOFA

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deficiencies. But it also said the bank must continue to improve before the next stress-test submissions in April. The Fed didn't issue the same exhortation to **J.P. Morgan Chase** & Co. and **Goldman Sachs Group** Inc. when they went through a similar resubmission process in 2013.

Bank of America noted the Fed's approval in a statement, but didn't provide further comment. The lender's shares rose 10 cents, or 0.6%, to $17.20.

The bank's next stress test will be run by Andrea Smith, a longtime human-resources executive who was elevated to chief administrative officer by Chairman and Chief Executive Brian Moynihan this summer. Terry Laughlin, who ran this year's resubmission and has extensive regulatory experience, will move to running the wealth-management division. The bank says that Mr. Laughlin will help with the transition.

The bank's capital levels in this year's test, which measures how banks would fare in a severe recession, were above regulators' requirements. But the Fed had raised concerns about the quality of the bank's process, including the level of detail in the risk models the bank was using, according to people familiar with the situation.

For example, with some loans the bank used the same models to calculate potential risks and losses for both domestic and international loans, according to these people. In other cases, the bank relied too heavily on intuition rather than computer models when making loss predictions, some of these people said.

The Fed also had voiced worry that the bank's internal auditors weren't sufficiently overseeing or reviewing the main stress-test process, according to these people.

Regulators also had concerns about a decentralized stress-test process, with various units in the bank calculating their own potential losses with their own methodology, according to some of these people.

The bank's capital levels were above regulators' requirements.

Regulators also told top bank executives they weren't "forward looking," and should have anticipated problems with their stress-test submissions, The Wall Street Journal previously reported.

Mr. Moynihan has acknowledged that the bank's stress-test processes had "plateaued."

The bank has worked on making sure all its business lines are regularly involved in assessing how their actions might affect the stress test, rather than viewing it as a once-a-year exercise, and trying to bring their own risk models in line with what they believe the Fed measures.

At a Wednesday conference, Mr. Moynihan said the lender had also worked on "getting the data flows nailed down," which can be a challenge in a bank stitched together from multiple acquisitions.

"For our commercial real estate, we have to go back and get data from previous companies' files that we wouldn't have kept because the loans kind of were out of the system," Mr. Moynihan said.

He also said BofA "wanted to be more careful to make sure we really nail this thing."