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THE END OF RELATIONSHIP BANKING? EXAMINING THE CFPB'S 'SMALL BUSINESS LENDING DATA COLLECTION' RULE

HEARING

BEFORE THE

SUBCOMMITTEE ON ECONOMIC GROWTH, TAX, AND CAPITAL ACCESS

OF THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES
HOUSE OF REPRESENTATIVES

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THE END OF RELATIONSHIP BANKING? EXAMINING THE CFB'S 'SMALL BUSINESS LENDING DATA COLLECTION' RULE

TUESDAY, MARCH 28, 2023

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
SUBCOMMITTEE ON ECONOMIC GROWTH,
TAX, AND CAPITAL ACCESS,
Washington, DC.

The Subcommittee met, pursuant to call, at 10:01 a.m., in Room 2360, Rayburn House Office Building, Hon. Dan Meuser [chairman of the Subcommittee] presiding.

Present: Representatives Meuser, Williams, Luetkemeyer, Van Duyne, Alford, LaLota, Landsman, Velázquez, Chu, and Davids.

Chairman MEUSER. All right. This hearing will come to order. Thank you. Thank you. This is the Subcommittee on Economic Growth, Tax, and Capital Access. This meeting has now come to order.

Without objection, the Chair is authorized to declare a recess of the Committee at any time.

I will now recognize myself for my opening statements. The title of this hearing is "The End of Relationship Banking: Examining the CFBP's Small Business Lending Data Collection Rule."

Again, good morning, and welcome to this hearing, examining the Biden Administration's continued regulatory overreach and its very harmful impact on America's small business economy.

First, I want to thank our witnesses very much for being here today. We appreciate you taking the time to join us and sharing all of your insights.

Today's hearing addresses a vital part of our country's economy, small community lending institutions and the role they play in assisting our small businesses. As we meet here today, the financial institutions across the country are actively engaged as we know in lending to main street America and our nation's entrepreneurs who are in the process of starting their own businesses.

As our witnesses will discuss with the Subcommittee, the relationships between local lenders and the businesses in their communities takes years to build and refine. These community lenders are also the ones best suited to determine the structure of the loans that provide to their customers personal touch, knowing the customer, that it is impossible for a large national institution to replicate.

Unfortunately, President Biden's Consumer Financial Protection Bureau (CFPB) is poised to throw another wrench into this vital aspect of our economy. The CFPB is proposing to implement a new rule, the Small Business Lending Data Collection Rule, that will impose burdensome new reporting requirements that would harm small business lending. This rule will alter the behavior of small financial institutions and make them hesitant to continue lending to small businesses based on their long-established relationships with main street America.

This rule was born out of an obscure provision in Dodd-Frank almost 13 years ago. Most Members of Congress were too busy debating too-big-to fail to even pay attention or realize it was in there.

Making matters worse, this rule will add an even larger regulatory cost burden to these small financial institutions that are already struggling to keep up with the Biden administration's costly regulatory agenda. According to the SBA's Office of Advocacy, this rule, "may be unnecessarily burdensome to small entities, may impact the cost of credit for small businesses, and may lead to a decrease in lending to small, minority- and women-owned businesses." This is from the Office of Advocacy. The Office of Advocacy also estimates that the rule will have an initial $126 million impact on small financial institutions, and then going forward, an annual impact of $153 million. Unlike mega-banks that can absorb such costs, these will crush smaller institutions that do not have the budget to absorb such new regulatory burdens. The Office of Advocacy also expressed concern that this rule failed to properly consider alternative, less burdensome alternatives to the rule. These alternatives should have included exempting the smallest lenders but were never seriously considered.

The rule also creates racial profiling issues, privacy concerns, an unrealistic implementation window, and mandates excessive data collection of small business owners. In the digital age we live in, such personal information in the hands of so many different entities should give all of us, especially the CFPB, pause on such requirements.

At a time when main street America is dealing with unprecedented levels of inflation, interest rates that are being raised at the fastest pace since the 1980s, supply chain disruptions, and a prolonged labor shortage, adding more burdens to our country's job creators, and our banks, is the last thing the CFPB should be doing, but that is exactly what the Bureau and the Biden administration seem determined to do. Our small businesses and local community lenders deserve so much better.

Without objection, I would like to enter into the record letters detailing the impact this rule would have on small business lending from the National Association of Federal Credit Unions, International Community Bankers Association, the Consumer Bankers Association, and the American Bankers Association. It seems this rule has brought community banks and credit unions together. So I guess there is a silver lining here somewhere.

With that I will yield to our Ranking Member from Ohio, Mr. Landsman.

Mr. LANDSMAN. Thank you, Mr. Chairman, for holding this very important hearing and examining the CFPB's small business

lending role and examining ways to create a much more fair and successful equitable lending system. For far too long, women- and minority-owned small businesses have experienced obstacles to accessing capital. Part of the reason is the lack of data and transparency related to small business lending.

The scant data that exists continues to show that these businesses lack the same access to external financing when compared to traditionally owned firms. And during hard economic times, the barriers to access capital are even greater. According to the CFPB, minority- and women-owned small businesses were disproportionately hurt by the pandemic because they had fewer cash reserves and faced deeper hurdles to accessing capital.

The Paycheck Protection Program highlighted the disparities between these white-owned businesses and businesses of color. The Federal Reserve Bank of New York found that the PPP loans only reached about 20 percent of the eligible firms in states with the highest densities of black-owned firms. The report confirmed what we already suspected, the presence of racial disparities in banking relationships and significant gap and credit access in underserved communities.

Section 1071 of Dodd-Frank passed over a decade ago attempts to remedy this situation by requiring financial institutions to simply collect and report on the demographics of small business owners applying for financing. Doing so facilities the enforcement of fair lending laws and identifies business and community development needs for small businesses.

I am encouraged that the CFPB will be issuing a final rule in the next few days. It has been a long 12 years to get to this point which included a lawsuit to prevent the previous administration from intentionally delaying this rule. The CFPB has conducted considerable outreach to small firms which included convening of the Small Business Regulatory Enforcement and Fairness Act panel in October 2020 to hear suggestions and recommendations for small entity representatives. This, in addition to adhering to the required APA notice and comment process where the agency considered thousands of comments from the public. There are going to be discussions today that this rule discourages small financial institutions from making loans to small firms. I for one do not agree with that conclusion. Just like the data requirements for HMDA do not negatively impact the mortgage lending industry, this rule will not be detrimental to small businesses' lending market. It is my hope that this rule will actually increase lending to small businesses in general.

With that said, Mr. Chairman, I would like to request to enter into the record a report titled "Addressing the gap in consumer protection for small business consumer through multiple research program," which includes the data collected is essential to combat institutional systemic discrimination and the costs associated with the rule far outweighed by the need to create a more transparent system for small business lending in this marketplace.

So this is a motion to enter this into the record.

Chairman MEUSER. Without objection.

Mr. LANDSMAN. Thank you, Mr. Chairman, and I yield back.

Chairman MEUSER. Thank you again.

I now recognize Mr. Williams of Texas, the Chairman of the Full Committee for his remarks.

Mr. WILLIAMS. Good morning. I want to thank all the witnesses for being here today. And I want to thank my colleague, Dan Meuser, my friend also, for holding today's Small Business Subcommittee on Economic Growth, Tax, Capital Access hearing on the CFPB's 1071 rule.

Today's hearing is critical to examining the future of main street America. Banks are the lifeblood for small businesses looking to grow or expand their operations, and I can tell you as a small business owner for over 52 years, I can tell you there has not been a day in my life where I have not owed a community bank money. And I do not think there is another agency in Washington that brings and causes more anxiety and nervousness to small businesses than the CFPB. This agency is quick to issue fines and enforcement actions against businesses and financial institutions without ever telling them the rules of the road before they are penalized. This regulation by enforcement is detrimental to main street businesses that crave certainty.

So this 1071 rule looks to make this problem even worse. Financial institutions are going to have to dedicate significant time and resources in order to comply with this overly burdensome new data reporting regime. We need more loan officers in our lending institutions and credit unions and not more compliance officers, and we are looking to get more money into the hands of job creators instead of needing to hire more compliance officers like I said that are nothing but a drain on our bottom lines.

So with that, I am looking forward to today's discussion, and I hope we can shine a light on the most harmful aspects of this very harmful rule that will be finalized any day now.

So Mr. Chairman, thank you, and I yield the time back.

Chairman MEUSER. Thank you very much, Mr. Chair. I appreciate you being here with us this morning.

So I will now introduce our witnesses.

Our first witness today is Mr. Troy Peters. He resides in my district. Mr. Peters is the president and CEO of Jonestown Bank and Trust, which is celebrating its 150th anniversary this year. Headquartered in Jonestown, Pennsylvania, which is in my district, the bank's primary focus is on lending to small businesses and retail banking. Mr. Peters knows firsthand how vital banks like his are to the local community and being readily able to provide a line of credit, and by extension, a line of opportunity for someone to pursue their dream of opening small businesses. And what will be a common theme in today's hearing, the CFPB's Small Business Lending Data Collection Rule will have a major adverse effect on both Mr. Peters' bank and the local communities he has dedicated himself to serving. With a career spanning over 30 years, Mr. Peters has indispensable knowledge of the community banking industry and will provide firsthand experience of how this rule will be another blow to our country's small banks and main street America. Mr. Peters, thank you for joining the Committee today.

It is now also my honor today to introduce our next witness, Mr. Lucas White. Lucas White is a fourth generation community banker and an active Member of his community. He has served as presi-

dent of The Fountain Trust Company since 2016, a $600 million community bank with five locations in Fountain County, Indiana. Mr. White is also Chairman-elect of the Independent Community Bankers of America (ICBA), a national trade association focused on advocating on behalf of more than 5,000 community banks across the United States. At ICBA, Mr. White is a Member of the executive committee and a board of directors and is Chairman of the Federal Delegate Board. He is also a Member of the ICBA's Policy Development Nominating Committee. So thanks very much for being here with us. Also, while graduated from Indiana University with a bachelor's degree in philosophy and Indiana University-Bloomington, Morris School of Law years later, Mr. White still actively practices law in the family firm of White and White Attorneys today. Community banks channel local deposits into main street America and help spur job creation, foster innovation, and assist in fulfilling the American dream for many entrepreneurs. Mr. White's extensive career knowledge in community banking makes him well informed about the issues facing small businesses in main street communities today. Mr. White, again, thank you for making the trip and being with us.

It is now my honor to introduce our next witness, Mr. Mike Wilson, to today's hearing. Mr. Wilson is the chief experience officer for Members First Federal Credit Union headquartered in Enola, Pennsylvania, just outside my district. Members 1st over a half million Members, 60 branch locations across 9 counties in Central Pennsylvania, including in the great 9th District of Pennsylvania. Mr. Wilson's role is crucial as he is responsible for ensuring exceptional Member experience on behalf of the entire credit union. He does this through providing leadership and direction for the credit union's retail operations, customer service areas, we well as public relations, marketing, community outreach, internal and external communications, and financial literacy. Mr. Wilson, you sound like you are kind of a busy guy. Mr. Wilson graduated from Central Penn College with a bachelor of science in business and went on to earn his MBA from Eastern University. Through his passion for people and entrepreneurial thinking, Mr. Wilson has been recognized for his professional accomplishments with numerous business awards, including Emerging Business Leader of the Year to the Harrisburg Regional Chamber and Capital Region Economic Development Corporation. Mr. Wilson's extensive career and dedication to his community through local banking makes him as well informed as anyone about the issues facing small businesses and main street communities today. Mr. Wilson, we thank you for joining the Committee today and we are looking forward to your testimony very much.

I now recognize the distinguished Ranking Member, Mr. Landsman of Ohio, to introduce his witness for today's hearing.

Mr. LANDSMAN. Thank you, Mr. Chair.

Our final witness today is Ms. Luz Urrutia, CEO of the Accion Opportunity Fund, which is a nonprofit CDFI located in California focused on national microlending strategy to meet the needs of small businesses. She has spent her career in banking and financial services, particularly in underserved markets. Prior to joining Accion Opportunity Fund—I think it is Accion. Did I get that—

sorry, my fault. She worked for Dollar Financial Group as CEO for the Americas. In this role she helped transform the organization into a responsible consumer finance business for underserved communities. She has served on the CFPB's Consumer Advisory Board, the Consumer Advisory Council of the Federal Reserve Bank, and the Board of the Financial Health Network. And on the SBREFA panel that examined the CFPB Small Business Lending rule which is the top of the hearing today. Recently, she received the Latino Leadership Award for the Silicon Valley Business Journal. Ms. Urrutia received a bachelor of science in Business administration and finance and an MBA from Georgia State University. Thank you for joining us. We look forward to hearing your testimony.

Chairman MEUSER. Thank you, Ranking Member Landsman. Nice to have you with us.

So before I recognize our first witness, I remind the witnesses that oral testimony is restricted to 5 minutes in length. When the light in front of you turns yellow you have 1 minute remaining. When the light turns red, you are over time and need to conclude your testimony as quickly as possible.

I do now recognize Mr. Peters for his 5 minute opening remarks. Troy?

STATEMENTS OF TROY PETERS, PRESIDENT AND CEO, JBT; LUCAS WHITE, PRESIDENT, THE FOUNTAIN TRUST COMPANY; MICHAEL WILSON, CHIEF EXPERIENCE OFFICER, MEMBERS 1ST FCU; LUZ URRUTIA, CHIEF EXPERIENCE OFFICER, ACCION OPPORTUNITY FUND

STATEMENT OF TROY PETERS

Mr. PETERS. Chairman Meuser, Ranking Member Landsman, Chairman Williams, and Members of the Subcommittee, I am Troy Peters, President and CEO of Jonestown Bank and Trust Co. (JBT) headquartered in Jonestown, Pennsylvania. I testify today on behalf of the Pennsylvania Association of Community Bankers, and I also am a Member of ICBA. My bank is celebrating its 150th anniversary this year. Our name has never changed. We have nearly $900 million in assets, 11 full-service branch locations, and 160 employees. Our focus is on small business and retail banking. We are also active in indirect auto lending, and we serve the legal cannabis related businesses throughout Pennsylvania and surrounding states.

Community banks like mine provide the bulk of all small business loans in America. We are different than large banking institutions that operate under a contrasting business model that focuses on large companies and loan sizes. Main street businesses, like my customers, prefer to work with a local community bank because we are relationship lenders. We intimately know our markets and our customers.

The CFPB's Small Business Lending Data Collection rule is unfortunately squarely aimed at smaller banks like mine. We are disproportionately disadvantaged to take on additional system and personnel costs associated with compliance to this rule. Now, although much of the costs would need to be passed on to the borrower, it continues to promote further bank consolidation, which

means fewer local community banks to serve the small business segment.

When my career began, this country had over 12,500 banks. Today there are just over 4,000. Now, due to consolidation, a small business's access to capital is being pushed into metropolitan markets where relationship banking just does not count for much.

I also worry about the integrity of the data to be collected. In most cases, when a small business is seeking financing, they are looking for the best solution and talking to multiple lenders. Five banks could be collecting this data, but only one will fund the loan. Each bank would be reporting the data, which would make drawing any meaningful conclusion difficult at best.

Small business loans are tailored to the specific business's needs and it would be very difficult or impossible to collect the exact data points to tell the entire story of the structure, pricing, or counteroffers. There are just too many variables to these loans. They are not as homogeneous as, say, car loans. Making application and loan data public would certainly be objectionable to my clients and it is quite concerning. Publicly displaying sensitive information, like how much money they applied for, what the purpose of the loan is, and their revenue number is not the kind of information they want or expect to be made public from a private transaction.

This disclosure could also create a competitive disadvantage for them, such as revealing a planned business investment. Even worse, publishing information that a sole proprietor's loan request was denied in a small community like ours, is akin the posting a bounced check to the wall behind the store cash register. The public humiliation shouts, "Do not do business with this person; they are a deadbeat!" My customers adamantly do not want this.

I have customers like Jay. Jay came to our country seeking opportunity, and after years of hard work and savings, he was able to open his own small business near our town of 1,900 people where my bank is headquartered. A few years ago, when the qualified mortgage (QM) rule was implemented, Jay was ready to build his modest dream home. As a long-time customer, I would have loved to help him achieve this dream, but his mortgage request did not comply with the QM rules. And without access to the traditional banking system, Jay turned to an unregulated, hard money lender. His interest rate was higher the loan did not come with complete disclosure, flexible terms, or collection practices.

I feel like this rule will cause similar unintended consequences and will not be in the best interest of my clients and the communities that we serve. My hope is that the CFPB will not go beyond the statutory requirements intended for this rule. They should not add additional data points. They should exempt smaller banks like mine, reduce the revenue thresholds, and not breach the privacy of my customers.

I love the community banking industry and I love helping my customers, and I thank you for convening today's hearing and the opportunity to offer the community bank perspective. Thank you.

Chairman MEUSER. Thank you, Mr. Peters.

I now recognize Mr. White for his 5 minute opening remarks.

STATEMENT OF LUCAS WHITE

Mr. WHITE. Chairman Meuser, Ranking Member Landsman, and Members of the Subcommittee, I am Lucas White, President of The Fountain Trust Company in Covington, Indiana. I testify today on behalf of the Independent Community Bankers of America (ICBA) where I am Chairman-elect. Thank you for this opportunity.

Community banks are committed to meeting the credit needs of all small businesses in compliance with fair lending laws. However, we believe the CFPB's forthcoming rule under Section 1071 of the Dodd-Frank Act will have serious, unintended consequences. If finalized without significant changes, the rule will have a chilling effect on customized lending, compromise borrower privacy in the rural and small-town markets I serve, and reduce access to credit for certain borrowers.

As described in my written statement, ICBA is urging the CFPB to stay the effective date until the Supreme Court has ruled on the constitutionality of the agency.

Is this rule "the end of relationship banking," as the hearing title suggests? I absolutely believe that it puts relationship banking at risk and should be amended by the Bureau or by Congress at the earliest opportunity. Relationship banking is the key value proposition that community banks like mine offer.

Relationship banking is our competitive advantage against the larger financial institutions and nonbank lenders.

The Fountain Trust Company has served markets in West Central Indiana since 1903 with small business, agricultural, and consumer lending. Relationship banking is the foundation of our success. It explains our resilience through numerous economic and agricultural crises.

When it comes to serving small business, we form partnerships that go well beyond lending. Community banks provide practical, real world business counseling that is especially important to small businesses. Customized lending is key to these relationships.

Small business lending is not and should not be a commodity. Underwriting is based on numerous borrower characteristics and market variables. Loans are typically customized to suit borrowers' needs and preferences and give them the best chance of success. The data collected under 1071 will not reflect the full scope of underwriting and may suggest discrimination where none exists.

Fortunately, our examiners are best positioned to make this judgment and application of fair lending laws.

Section 1071 is simply the wrong tool for the job. Lenders will respond by standardizing loan features to protect themselves from charges of discrimination. As a result, small business customers will not have access to credit that is customized to their needs. Importantly, minority and women borrowers whom this rule is supposed to help often benefit from customized lending.

This was the outcome of the qualified mortgage rule which was also a provision of the Dodd-Frank Act. It effectively forced residential mortgages into a box.

As I discuss in my written statement, QM effectively undermined our mortgage lending. Section 1071 without needed accommodations threatens to do the same to our small business lending.

A recent loan will illustrate my point. We worked with a local farmer who wanted to open a butcher shop, a vertical integration that made good business sense. We offered him two customized loan options, a fixed rate and a variable rate. I personally walked him through the benefits and drawbacks of each and how future interest rates could affect his loan payments and cash flows. This personalized customer service is what community banks do best and what sets us apart from the competition.

Unfortunately, Section 1071 would make customized multiple option lending difficult. It is impossible to compare loan data across customers who have chosen different options and demonstrate that lending is not discriminatory. Thus, Section 1071 will limit the scope of loan choices available to small businesses.

On top of that, the publication of my borrower's loan data under 1071 would surely compromise his financial privacy. He is the only butcher in town. In the small communities I serve, businesses are readily identifiable. Loan offers contain critical business information and reflect the business owner's personal financial position as a guarantor of the loan.

I discuss additional objections to 1071 in my written statement, but the effect on customization and the compromise of borrower privacy are our primary concerns. The rule could be greatly improved by recommendations described in my written testimony that would exempt more banks and borrowers from the rule. ICBA thanks the Members of this Subcommittee and Committee who have introduced legislation to make the rule more workable.

Thank you again for the opportunity to testify. I look forward to your questions.

Chairman MEUSER. Thank you, Mr. White.

I now recognize Mr. Wilson for his 5 minute opening remarks.

STATEMENT OF MICHAEL WILSON

Mr. WILSON. Good morning, Chairman Meuser, Ranking Member Landsman, and Members of the Subcommittee. My name is Michael Wilson, and I am testifying today on behalf of the National Association of Federally Insured Credit Unions (NAFCU). I currently serve as Chief Experience Officer of Members 1st Federal Credit Union, headquartered in Enola, Pennsylvania. While small businesses only make up 4 percent of our total membership, we are very proud of our work in the community as a small business lender over the last 20 years in 9 counties across Central Pennsylvania where relationships mean everything.

We appreciate the opportunity to participate in this discussion regarding the 1071 rulemaking process at the CFPB. Section 1071 requires financial institutions to report data about small businesses and their owners in order to facilitate enforcement of fair lending laws. While NAFCU lauds this goal, there is widespread concern about how the CFPB is proposing to carry out its authority in this area. We outline our concerns with the proposed rule in detail in our written statement but would like to highlight a few of our major points here.

The definition of a covered financial institution. Establishing a 25 loan threshold for reporting is a lower level than even well-established home mortgage disclosure act or HMDA limits. Such a

low threshold could drive smaller lenders out of small business lending all together due to the compliance costs, a fact that the Bureau acknowledges in the proposed rule.

The small business definition. While the CFPB has a proposed $5 million threshold, NAFCU believes it should be consistent with the SBA's $1 million standard.

Covered credit transactions. NAFCU recommends that the Bureau establish a de minimis threshold consistent with the NCUA's $50,000 call report threshold. Congress has excluded Member business loans under $50,000 from the credit union business loan cap and the NCUA has recognized this and excluded such loans from call reports. We believe the CFPB is vastly underestimating the number of credit unions that would be impacted by the new burdens of this rule because it used the call report data that excludes these loans in its analysis but the Bureau did not account for the de minimis threshold by proposing its own in the rule. By not recognizing this distinction, the CFPB threatens to compound the compliance burdens of this rule for credit unions.

Protected demographic information and visual observation. Under the proposed rule, an employee could be forced to determine the ethnicity and race of a small business applicant via visual observation. NAFCU unequivocally opposes any requirement that an employee of a credit union make visual observations concerning the race, gender, or other sensitive data about a small business owner. Not only is this an unconscionable idea but it also threatens the integrity of any Section 1071 data collected.

One-time and ongoing compliance costs. NAFCU is significantly concerned that the Bureau, as happened with its HMDA proposal, has materially underestimated the one-time and ongoing costs credit unions are likely to face under the rule.

Mandatory compliance schedule. The proposed rule's 18-month mandatory compliance schedule will be aggressive, even for the largest, most tech-savvy credit unions. The vast majority of credit unions will be forced to rely on multiple IT vendors to come into compliance. Past experience with the Bureau's implementation of HMDA suggests that the Bureau is likely underestimating the time required for IT venders to adapt their products to comply with major rulemaking. NAFCU has encouraged the Bureau to adopt a phased, mandatory compliance schedule based on loan volumes that begins no sooner than 3 years following the Bureau's adoption of a final rule. We are supportive of efforts to address concerns about the compliance deadline, such as the Small Lender Act offered by Representative French Hill.

In conclusion, with the final Section 1071 rule set to be released, NAFCU urges the CFPB to exercise its discretionary authority to exempt smaller institutions from this rule as the compliance costs outweigh any benefit. If such an exemption is not granted under the CFPB Section 1022 authority, we would hope to see significant changes to the proposed rule as outlined above. Even though small businesses make up a small percentage of our membership, the cost associated with complying would have a negative impact on our Members and their access to credit. Should the bureau not address our concerns, we urge Congress to step in with your oversight authority and to consider statutory changes such as enacting the

small lender act. Failure to do so will threaten access to credit for many of our nation's main street small businesses who rely on community lenders like credit unions to meet their capital needs.

I thank you for the opportunity to testify today and look forward to answering your questions. Thank you.

Chairman MEUSER. Thank you for your compelling testimony, Mr. Wilson.

I now recognize Ms. Urrutia for her 5 minute opening remarks.

STATEMENT OF LUZ URRUTIA

Ms. URRUTIA. Good morning, Chairman Meuser, Ranking Member Landsman, and Members of the Committee. Thank you for the opportunity to testify and discuss CFPB Section 1071.

My name is Luz Urrutia and I am the CEO of Accion Opportunity Fund, the leading CDFI nonprofit providing access to loans, business advising, and networks to underinvested entrepreneurs.

I spent my entire career in for-profit financial services which included nearly two decades at Wachovia, then as co-founder and CEO of a community bank and a CEO of a payday lending company where I helped to ensure that they provide responsible financial services to their customers. I joined AOF as its CEO because of my experience as a lifelong for-profit banker and my passion for providing responsible financial services to underinvested communities. I know for a fact that business and lenders can generate profit and do the right thing investing in all communities.

As CEO, I am very proud of the impactful work AOF has done to provide capital to entrepreneurs that are often left behind by our financial mainstream system. Today, we have deployed over $700 million to more than 25,000 entrepreneurs, and 80 percent of our borrowers are people of color, women, and immigrants. In fact, women make up one out of every three clients we serve. It is because of the entrepreneurs we serve that I have advocated for rules like 1071 which will allow our entire financial services system to fully see and better serve all of our entrepreneurs.

And this transparency is not just about fairness. It is also about strengthening the economy. A recent study shows that minority- and women-owned small businesses employ nearly 20 million people and generate over $2 trillion in economic activity.

I know this to be true, personally and as the CEO of AOF, because I think about clients such as Reign Free from Oakland, who started and scaled her catering business after repeatedly being told that she did not qualify for a loan. We were her first lender to say yes. I also think about Alicia Villanueva from Hayward, who took $5,000, bought her first van, and now she has the most burgeoning tamale business nationwide.

I am proud that we provide loans to everyone—Black, White, Latino, Asian, and low-income, but I am especially proud of our investment in Black and Latina women who are starting up more businesses in this country than any other group. I am proud that AOF supports these entrepreneurs and the businesses that they found, the employees they hire and train, and the economic activity they generate.

However, for decades, entrepreneurs like these women have not been seen by our financial system. While I am on here to defend

or promote every letter of Section 1071, I recognize that this rule will accomplish three important things: It will help small business lenders. It will help entrepreneurs that desperately need access to capital, and help policymakers that want to invest in our economy without creating new direct entitlement programs.

First, this rule would help the market to better address both the lack of access to affordable capital, and the rise of irresponsible lending. For the first time, everyone in financial services would be able to see which business models are successful at reaching minority-owned, women-owned, and other small businesses. This transparency would attract investment capital and partnerships into models that really work. We can have a market-based model and pro-innovation approach to regulation, one that will actually help lenders expand customer acquisition, something that all community banks and lenders really want and need to do. But we need clarity on who the businesses are, who is serving them, and what capital are they getting, because we cannot manage what we do not measure.

Second, as lenders, the better we understand these businesses, it will help tailor products and services to meet their needs. The more knowledge we gain about our markets, our customers, and their needs, the better equipped we are to building long-term profitable relationships.

Finally, this rule helps spur additional investments in small businesses, which is the best way to reduce inequities without having to create new government programs. Instead, it will allow all of us to do what our organizations have successfully done for years—expand access to capital for underserved entrepreneurs by leveraging existing public and private sector partnerships.

For these reasons, I am very pleased to testify on how we can ensure that Section 1071 accomplishes its goals of spurring additional investment in all our entrepreneurs.

I will conclude by saying that access to capital for small businesses is a bipartisan priority. There are Mom and Pop stores in communities that are rural and urban; red and blue; Black and White, Hispanic, and Asian, and they are all powering our economy. But we cannot do that without Section 1071 to shine light on these small businesses' credit applications.

Because as I said before, we cannot manage what we do not measure, and sunlight is the best disinfectant. As we implement this rule well, we will finally will be able to increase access to capital for small businesses and create a more transparent, bipartisan, and successful financial system.

Thank you, and I look forward to your questions.

Chairman MEUSER. Thank you, Ms. Urrutia, I appreciate that.

We will now move to the Member questions under the 5-minute rule. And I recognize myself for 5 minutes.

Mr. White, I will start with you. And really, to all of our witnesses. The CFPB's mission statement is as follows. I am going to summarize.

We aim to make consumer financial markets work for consumers, responsible providers, and the economy as a whole. We protect consumers from unfair, deceptive, or abusive practices and take action against companies that break the law. We arm people with the in-

formation, steps, and tools that they need to make smart financial decisions.

Mr. White, do you think that this rule will help the CFPB to accomplish this mission?

Mr. WHITE. Mr. Chairman, thank you.

I do not believe this rule will help CFPB achieve its mission. The first part of the mission statement was something along the line of having markets help consumers. And I would reference the QM rule that came into effect as part of Dodd-Frank. As I said in my testimony, customized lending is absolutely key to small business lending. We had that type of lending with consumer mortgages prior to the QM rule. As a result of the QM rule, we now have all of our consumer mortgages in a matrix. We had a customer prior to QM. Her name is Mae. She owns a local Chinese restaurant. We had a consumer mortgage with her. After QM, we could not verify enough income and we had to turn her down when she wanted to buy a new house. And so that is an example of where a rule like this can undermine what the CFPB's mission is.

Chairman MEUSER. Sure. So, will the CFPB's 1071 reporting rule in any way improve your lending practices and make them fair? Will you have more businesses in some way because this rule is in effect? And I will also ask, and I am going to ask Mr. Peters this and as well Mr. Wilson, is it fair to compare a mortgage loan to a business loan?

Go ahead, Mr. White. You go first.

Mr. WHITE. they are completely different. Each business is different. Their cash flows are different. Their needs are different. And that is the reason we tailor our loan products specifically to what that customer needs. And so you cannot compare consumer lending at all to small business lending in my eyes.

Chairman MEUSER. Mr. Peters?

Mr. PETERS. Yeah, I would agree. They are two different situations. I mean, small businesses are unique. They are at different stages in their lifecycle. Oftentimes you are counting on pro forma income or projections, whereas in consumer lending it is documented past. So I think it is two different types of lending.

Chairman MEUSER. And continuing, Mr. Peters, will this have any effect in extending relationships with small businesses in your community? I mean, let's face it. We are talking about expanding lending here, not what occurred with the PPP where fraud came into play. Now, we all know that knowing the customer within the PPP reduced potentiality of fraud immensely; right? I mean, it did not happen with knowing the customer. But would this help you accentuate and enhance your business base in any way in your view and change your proactive practices to outreach to your community?

Mr. PETERS. I do not believe so. I think we are only as strong as our communities as a community bank. And we want to build stronger communities. So, I do not think that it would help that or change the outlook at all.

Chairman MEUSER. Well, it is certainly your reputation.

Mr. Wilson, let me ask you, can you explain how your employees are going to feel about having to potentially guess the racial information of customers based upon appearance, surname, when it is

not self-reported by the small business which is their right and as this rule would require?

Mr. WILSON. I would imagine that would put our associates in a very uncomfortable situation. I think about the 19- or 20-year-old teller who is in their entry-level role and being, you know, put in a very awkward situation like that would be very difficult for them. In addition to that, it could really compromise the data which could undermine exactly what the attempt is here to help.

Chairman MEUSER. All right. Thanks.

And I am going to go back to you, Mr. Peters. Would this rule require you to increase employees, increase your costs for compliance, add additional burdens to your ability to be a thriving lender in your community?

Mr. PETERS. Yes, it would. I mean, you are talking about systems and when systems are put into place what a lot of people do not think about is there needs to be somebody to run that system. The care and feeding of it, in addition to compliance, to the checking, the double checking, the software, to gather and report it. I would say something like this would touch at least 15 different people in our bank and probably add in the neighborhood of $500 to $800 per loan in the startup year.

Chairman MEUSER. Thank you. My time has expired. Thank you for your testimony.

I now recognize the Ranking Member for 5 minutes for questions.

Mr. LANDSMAN. Thank you, Chairman.

So I appreciate everyone being here. The fact that we have a community bank and a credit union, a CDFI, part of this hearing is to better understand what is a proposed rule. Right? You know, the rule is still being finalized, input is being gathered, information from everybody is collected. And so it will be important for us to, I think, wait to see what this proposed rule is, though it does seem to me that this is a very straightforward thing. And Mr. Wilson touched on this which is although it may have been Ms. Urrutia, sorry, who said it but this is about collecting data and trying to better understand who does this best. And not an entitlement program which is I think a really important thing to keep in mind. And you know, to do it in a way that does not overburden folks obviously is important and clearly the testimony today suggests that, you know, for some of our banks it does. I will just way of background and then I will ask my question, I represent a district with a large number of smaller businesses, women-owned businesses, Black-owned businesses. We have a lot of childcare providers, most of whom are run by Black women, owned by Black women. And their ability to access capital has been tough. And you know, post-pandemic it has been even tougher because of the cost of capital; right? So accessing affordable capital. And so it does seem to me very straightforwardly that, you know, the more data that we are able to collect, the better it is that we will be able to understand what is working and what is not. And I think the question is how you do that in a way that is not overly burdensome and does not lead to this situation where folks are being left out or you cannot provide loans.

So I guess my question first Ms. Urrutia, sorry, I am struggling with that one, is do you believe that this will undermine, you know, small banks, their ability to provide these loans?

Ms. URRUTIA. I think it would be the opposite. I think that, this rule is going to lead actually to more small business lenders wanting to get into the market because everyone is going to become more aware, more knowledgeable, and more informed about the scope and scale of small businesses and the impact that they have on our economy. And frankly, how much they are growing and how profitable they are for institutions that want to serve them responsibly. You know, we saw this development with HMDA. It did not pull lenders away. In fact, as more data was reported, more competition emerged, better products were developed, and everybody won, the consumer and the lenders.

The CFPB issued a lender survey and developed cost estimates that were then reviewed by lenders, and many smaller financial institutions were asked this question during the rulemaking process and responded to say that it would not force them out of the market. The Bureau also estimated the cost per application would range anywhere between $7 for the larger banks with more technological capabilities to $28 for the smaller banks. And so, you know, for the first time I think everyone in financial services would really have access to see what the market is made up of and to be able to reach successfully more minority-owned, women-owned, and other small businesses. And I think once again, the transparency is going to attract quality responsible business models to want to serve a very burgeoning, growing, and profitable market which is the small business lending community.

Mr. LANDSMAN. You have been able to do a lot and this has helped you better understand the impact. What is your recommendation or suggestion, advice in terms of managing the data collection and pursing the intent of the rule which is to increase lending to folks that have struggled to get lending, to get the capital?

Ms. URRUTIA. Yeah. So just, our own perspective, last year we did about 3,000 loans to small business entrepreneurs. That is an enormous amount of lending. And you know, like every other CDFI, we are required to collect and report data on a variety of data points—interest rates, fees, origination cost, race, gender, ethnicity. And CDFIs do that.

Mr. LANDSMAN. I have run out of time and I apologize. I spoke a lot. But as the hearing continues I think just getting that sense as to what advice, recommendations would be great.

Thank you, Mr. Chair.

Chairman MEUSER. Thank you. The Ranking Member's time has expired.

The Chair now recognizes Mr. Luetkemeyer from Missouri for 5 minutes.

Mr. LEUTKEMEYER. Thank you, Mr. Chairman.

Mr. White, when Congress passed Dodd-Frank 12 years ago it included Section 1071, which requires companies to inquire whether customers are a small business, woman-owned business, or minority-owned business at the credit application stage. However, in the 1970s, Congress passed the Equal Credit Opportunity Act which

prohibits race as part of lending criteria. If the CFPB's proposed rulemaking would make financial institutions essentially guess the applicant's ethnicity if an applicant does not want to provide such information it would appear to me that would be racial profiling if I am not mistaken.

Mr. Wilson, does that proposed rule go against the Equal Credit Opportunity Act which has been in law since the 1970s? Mr. White, I am sorry.

Mr. WHITE. As Mr. Wilson actually said earlier, we are concerned with having to guess the race of our customers. We have to do that under HMDA currently but through PPP we learned that a substantially higher number of small businesses declined to provide that information than homeowners. And so as a result of that, our employees are going to be guessing that information a lot more than what they do under HMDA. And that will eventually kind of erode the data. As we say in the banking industry, "garbage in, garbage out." With models, it will be very hard to analyze the data.

Mr. LEUTKEMEYER. Okay. The Equal Credit Opportunity Act is a law though, is it not?

Mr. WHITE. Yes. We cannot discriminate, period.

Mr. LEUTKEMEYER. This is a rule by the CFPB; right?

Mr. WHITE. Yes.

Mr. LEUTKEMEYER. Does a law overrule a rule?

Mr. WHITE. No.

Mr. LEUTKEMEYER. No?

Mr. WHITE. The statute rules.

Mr. LEUTKEMEYER. They are equal in substance? Equal in importance? One does not overrule the other?

Mr. WHITE. Statute technically I think overrides a rule but we have to follow both. And as long as they do not conflict——

Mr. LEUTKEMEYER. Well, does this not conflict here because you are basically racially profiling with the way the new rule is proposed versus the Equal Credit Opportunity Act that says you cannot do that?

Mr. WHITE. It certainly opens up the risk to that.

Mr. LEUTKEMEYER. So, okay, as an attorney, would you not be concerned by your officers opening yourself up to a lawsuit in this situation? If you comply with one rule here, are you against, are you doing something in contradiction to the law?

Mr. WHITE. It certainly increases our risk of opening ourselves up to litigation. That is correct.

Mr. LEUTKEMEYER. How would you advise your customers, your clients in this situation? If you were a bank attorney—not the CEO now. If you are a bank attorney for a group of banks, what would you advise them to do here?

Mr. WHITE. When the rule requires our employees to guess, there is not much more we can do than say give it your best guess.

Mr. LEUTKEMEYER. So as long as you are guessing according to what the rule tells you to do you are going to be okay?

Mr. WHITE. Well, hopefully. I will say as a community bank we know our customers.

Mr. LEUTKEMEYER. Is that away to do business, Mr. White?

Mr. WHITE. No, it is not.

Mr. LEUTKEMEYER. To guess what is going to happen?

Mr. WHITE. We do not prefer to guess when it comes to doing business.

Mr. LEUTKEMEYER. Okay. Thank you for that.

Mr. Peters, you made a statement a minute ago that each bank has to collect the data and report it even if you do not make the loan. It would seem to me that is going to skew your data if you are going to have to continue to report it. Somebody who is not a worthwhile individual, he goes to seven different institutions and gets turned down, that is going to skew the data, is it not?

Mr. PETERS. Yeah. I think definitely so. You know, most times a small business is not going to just go to the first lender. They are going to shop their deal and try to talk to a number of banks about it. The banks are also going to help them put together the structure of that loan. So it may look different in different applications in different spots and only one bank will fund the loan but they will all be reporting the data and I think it would be very difficult to find meaning in that kind of data.

Mr. LEUTKEMEYER. Mr. White, CFPB wants to collect a series of personal and detailed data from small businesses but refuses to release which information they will publicize or share how they plan to make that determination. My bill, the Business Loan Privacy Act will require the CFPB to do a separate notice and comment rulemaking to determine what information will be published by the Bureau.

Mr. White, do you believe the CFPB should have a separate rulemaking for this, allowing small businesses and lenders to be part of the conversation?

Mr. WHITE. Absolutely. And on behalf of ICBA, I would like to thank you for that legislation that you have introduced. Small businesses and community banks should have a voice in what data is made public because that is where our privacy concerns come up for our customers.

Mr. LEUTKEMEYER. Well, it looks to me like your clients', your customers' information is going to be much more public than what it is now if this goes through. Do you have concerns about that information being made public and having some ramifications of that to your customers?

Mr. WHITE. We do. Small businesses prefer their information to remain confidential. And when our customers realize that their data is being made public it provides an incentive to go to a larger bank where their information can basically be hidden in the data. And if they come to our bank like that butcher I talked about, everybody is going to know who it is but if he goes to a big bank he may not.

Mr. LEUTKEMEYER. So what you are saying is instead of being able to do business with your local community bank, if you prefer not to have everybody in the community know what you are doing and what your business is you may go down the road to some bigger bank or some other community and as a result you are not doing business with your own community bank any longer.

Mr. WHITE. That is exactly right.

Mr. LEUTKEMEYER. And so it will hurt the community banks by doing this.

Mr. WHITE. Highly likely. Yes.

Mr. LEUTKEMEYER. Okay. Thank you very much for your testimony today. Mr. Chairman, I yield back.

Chairman MEUSER. The gentleman yields.

The Chair now recognizes the Ranking Member of the Full Committee, Ms. Velázquez from New York for 5 minutes.

Ms. VELAZQUEZ. Thank you very much. And thank you to all the panelists for your insightful information.

Ms. Urrutia, you said, you stated that we cannot fix what we cannot measure. And so when we were going through the pandemic and we issued the first tranche of money to provide relief to small businesses, anecdotal data was telling us that the smallest of the small businesses and Black and Latino and Asian businesses were left behind no matter how hard they try. Do you know why? Because the banks did not proactively help anyone but their customers. So I requested when I was consulted by the leader in the House to sign onto another tranche of money I said, no, I want to see the data. I want to see if everyone, every small business that is in need of help has been provided by the banks. And the Secretary of the Treasury Mnuchin refused. And then when he saw that definitely we will not be part of providing more relief unless we saw the data, what the data told us was exactly what the anecdotal data was telling us, anecdotal stories was telling us. And so, we added money for nation lenders to be able to provide relief to small businesses.

Ms. Urrutia, you were a Member of the CFPB and the notice of the proposed rulemaking provides that the applicants themselves do not have to provide their information. But, if the applicants do not provide the information, the financial institution must provide it based on visual observation or surname. In fact, those SBREFA panels were conducted by former Director Kraninger, who was appointed by President Trump. Is that not correct, Ms. Urrutia? And so it is also fair to say that the CFPB under both the Trump and the Biden administration thought that crafting and finalizing this rule was necessary to protect small businesses.

Ms. Urrutia, can you explain why the data collection requirements being proposed by the CFPB are not overly burdensome on small depository and non-depository institutions?

Ms. URRUTIA. Yeah. So as I explained earlier, you know, my previous experience as a banker and my current experience as the CEO of the largest nonprofit CDFI, I do not believe that the data collection being proposed under 1071 is overly burdensome. As I was stating earlier, we do on average 3,000 loans, small business loans a year. And like every other CDFI, we are required to collect and report comparable data to Section 1071 on small businesses on an annual basis and report that data to the CDFI fund. Many of the CDFIs that report with us are also small, community-based organizations and the information reported includes transaction-level data, such as interest rate, origination fee, points, terms, amounts, payments, race, ethnicity, age, and gender.

Ms. VELAZQUEZ. Thank you for that answer.

Can you expand on why you believe the work done by the CFPB is necessary to small businesses as consumer?

Ms. URRUTIA. Well, if you look at the small businesses, you know, they are often called Mom and Pop businesses. And that is

because they are small and they are run by the same consumers that the CFPB is trying to protect. These businesses do not have CPAs or CFOs making financial decisions for the family-run businesses and they have the same level of sophistication as the average American household. And these Mom and Pop stores are in rural and urban communities and are powering our economy. And their success is our success but they need capital to grow. And unfortunately——

Ms. VELÁZQUEZ. But are you not concerned about the potential upfront or ongoing compliance costs?

Ms. URRUTIA. I can tell you that our compliance cost up front was $35,000 and annually it is $10,000, regardless of number of loans that we are doing. And so I think that the costs are manageable compared to the benefits of having access to data that is going to help all of us better serve small businesses in America.

Ms. VELÁZQUEZ. Thank you. I yield back.

Mr. LALOTA. Thank you.

The Chair recognizes himself for 5 minutes.

I am Nick LaLota. I represent a Long Island district, the 1st District of New York. We are about a couple hours east of Manhattan. We are a suburban district with many Mom and Pop businesses. They are struggling under the high inflation, high interest rates, excessive regulations, and labor shortages just to name a few. Members of this Committee from both sides of the aisle agree that these challenges are real and persistent throughout the country. And with that in mind, it is troubling to me and other Members on the Committee that the Consumer Financial Protection Bureau is using resources at its disposal to create rules to add to these very real pressures instead of mitigating them. Hopefully at a future hearing we can have a representative from the CFPB to explain to us the timeliness of this rule. Thankfully, you, as today's witnesses, have beyond a doubt demonstrated that these new regulations would have duplicative measures and would cost millions per year to comply with and would irreparably harm our relationship banking.

My first question is to you, Mr. White. Sir, thank you so much for being here.

As you stated in your testimony, you have 130 employees across many locations. How difficult would it be for your business to create a firewall as has been described today?

Mr. WHITE. Any time when you have a bank our size with our number of employees, any new regulation is hard to figure out how are we going to do this with the employees we have. And I will explain what we do on HMDA because it is fairly similar to what will happen with 1071. Our loan processor enters the data. We then have three separate people review that data before we file it or report it. And we still have the random mistake after three levels of review. And so when you consider last year we did approximately 770 loans that would be subject to 1071, you are looking at HMDA on steroids basically in terms of the amount of manpower and time that it would take.

Mr. LALOTA. Thank you. And following up on that, you also illustrated problems with the scope of the data collection. For example, the 25 loan threshold is far too low and the borrower gross an-

nual revenue threshold is too high, meaning the data collection requirements would apply to a majority of community banks. In your opinion, what should the threshold be?

Mr. WHITE. ICBA is advocating for a $1 billion asset threshold. Banks below $1 billion would be exempt. If the CFPB or the government stays with a number of loans we would support French Hill's bill which has a 500 loan limit. Twenty-five loans a year is so low it is honestly a little bit offensive that that is considered an exemption.

Mr. LALOTA. Thank you so much.

And Mr. Peters, in your testimony you talked about the decline of community banks and the resulting consolidation. And I share these concerns, sir. How do you think small businesses like the ones in my district on Long Island and throughout the country will fare if there are fewer choices when it comes to lenders?

Mr. PETERS. Well, I think we have the best financial system in the world, and I think part of that is having choices as businesses and consumers in competition. And I think in this case if you are concerned about the privacy of the data you may want to go to a larger lender where your data could be harder to find by the public. If I was denied the loan, I do not want my community to know that so I think it does not play in favor of our small business clients and communities.

Mr. LALOTA. Thank you, Mr. Peters. And following up with that, you discussed that making application loan data public will be opposed by your clients for a variety of legitimate reasons. Do you think that this will make your clients less likely to apply for those loans?

Mr. PETERS. I think in some cases it could push them to other lenders that will not follow those rules such as I mentioned in my testimony with hard money lenders that fall under these thresholds and can ensure privacy of data. And that is something that is very important to my clients.

Mr. LALOTA. Thank you. And thank you for all the witnesses being here. I yield back the balance of my time.

I now recognize Ms. Chu from California for 5 minutes.

Ms. CHU. Thank you.

Ms. Urrutia, we know that women- and minority-owned small businesses still face significant barriers in access to capital. These gaps were particularly clear during the Paycheck Protection Program and the initial PPP application did not ask for demographic information. And so there were shocking results. In fact, because the SBA was not gathering this data, investigators at the LA Times in my area published a report in 2021 and they have to use census track data in order to look at majority ethnic census tracks. And they determined that businesses in majority White neighborhoods received loans at twice the rate that majority Latino census tracks received the loans, 1.5 times the rate of businesses in majority Black areas, and 1.2 times the rate in Asian areas. And so we clearly need it, that data transparency. What happened with PPP shows us why we have to have this information. And as a result, we did this $60 billion set aside for the mission-based lenders to provide loans to those in minority and women-owned areas. And

this problem was ameliorated tremendously and now the loans were shown to be given to those in those underserved areas.

So Ms. Urrutia, can you speak to the lessons of the PPP and why the data transparency like this required by Section 1071 is needed to both understand and address discrimination and disparities in small business lending?

Ms. URRUTIA. Sure. I can share my own personal experience about discrimination in the financial system. When I started working for a bank, I was turned down because I did not have credit. And so the fact that I was an immigrant and I had limited credit history made me invisible and unbankable. Fast forward 18 years, that experience led me to find a community bank and then I wanted to raise capital. And I kept on hearing no, no, no at every turn of the way until I show up with a couple of male board Members and then the capital to form the bank started flowing. Twenty-one years later things have not changed. Two percent of venture capital goes to women. Four percent of commercial loans goes to women. In the meantime, it is women that today are building small businesses at a higher rate than any other demographic in this country. So the problems persist, and unless we put sunshine in this problem we are never going to solve the problem that women and communities of color face accessing capital from financial institutions.

Ms. CHU. Thank you for that.

And Ms. Urrutia, well, for one thing we do know that the CFPB Home Mortgage Disclosure Act rule has been in place for more than 40 years and has been instrumental in giving the CFPB the data they need to identify and root out discriminatory lending practices. And even more importantly, mortgage lending activity has not decreased or been otherwise negatively impacted due to compliance costs.

Now, there was some discussion earlier about, well, mortgage loans are different from business loans and so that is why with business loans you should not look at demographic data. How do you answer that?

Ms. URRUTIA. You know, I think this can be very much compared to HMDA. There was anecdotal evidence that underbanked populations were not being served and that capital flows were falling short when reaching certain communities. But without the data there was no proof and HMDA was that data. The result really was real access to capital for those communities, and really great benefits were achieved for both the individuals and the institutions that were providing the capital. As a result, lenders got into mortgage lending because they thought it was profitable, it was growing, and they could really do great work. There is plenty of evidence following the HMDA data expansion between 1993 and 1999, the number of home purchases made. For Latino consumers, it increased over 120 percent. For Native Americans, 119 percent. For African Americans, by 91 percent. And plenty of more statistics that show that increase in the flow of capital happened to underserved communities. There were certainly other factors that contributed to this but HMDA was a key part of that expansion. So it has been done before.

Now, we do have some recommendations. Having a national database, and one thing I want to focus is on privacy. If you look at 40 years of HMDA's existence, not a single home loan has been identified. And the CFPB also contends that the publication of HMDA, which has similar data points to Section 1071, has not resulted in any measurable increase in fraud or identity theft.

Ms. CHU. Thank you.

Mr. LALOTA. The gentlelady's time has expired.

I now recognize the gentlelady from Texas, Ms. Van Duyne, for 5 minutes.

Ms. VAN DUYNE. Thank you very much, Mr. Chairman. thank you for holding this important hearing on a very concerning rule coming from the Biden administration which once again will hamper growth and create additional regulatory burden in an already difficult environment.

As we have already talked about in this hearing multiple times, the inflationary environment created by this administration has led to the rise of interest rates, which has limited the access to capital for small businesses. This rule is confusing to interpret, and it will be confusing to implement, which will lead to higher compliance costs from what we have understood today and will once again be passed along to small business owners further increasing the cost of capital. We have heard a couple of strange statements today.

Mr. Peters, I am going to ask you, do you have any clients who you have given loans to that are women?

Mr. PETERS. Absolutely. Quite a few.

Ms. VAN DUYNE. Do you have any minority clients?

Mr. PETERS. I do.

Ms. VAN DUYNE. Mr. White, do you have female and minority clients that you have actually given loans to as well?

Mr. PETERS. Yes. Absolutely.

Ms. VAN DUYNE. I am going to ask you, Mr. Wilson?

Mr. WILSON. Absolutely. In fact, we were the ninth largest provider of small dollar PPP loans in the credit union space in the country.

Ms. VAN DUYNE. That included women and minorities?

Mr. WILSON. Absolutely.

Ms. VAN DUYNE. And then I am going to ask you as well, you have women and minority clients as well?

Ms. URRUTIA. Absolutely.

Ms. VAN DUYNE. Mr. Peters, does every small business who applies for a loan qualify?

Mr. PETERS. No.

Ms. VAN DUYNE. Why?

Mr. PETERS. We are relationship lenders so we are not just looking at a scorecard or a matrix. You know, the foundation of relationship lending is the five Cs of credit. We are looking at character. We are looking at capacity, collateral, capital, and conditions. You need to find the story behind the applicant and you cannot do that with a check box.

Ms. VAN DUYNE. Okay. I am going to ask you, Mr. White, the same question.

Mr. WHITE. I agree with Mr. Peters. One thing I will add is that I mentioned the relationship banking and counseling our business

customers and giving them real-world business advice is part of what a community bank does. When we have small business owners that do not qualify for one reason or another we work with them to show them what they need to do to qualify in the future, whether that is improve their cash flow, improve their collateral or whatever it may be, we work with our customers to get them to a point where they can qualify.

Ms. VAN DUYNE. Mr. Wilson, does every single small business, even if they need the capital that comes to your bank, are they able to qualify?

Mr. WILSON. Well, in addition to following a similar process to Mr. Peters and Mr. White, we also take it a step further and assign every small business their own personal concierge. So even if they cannot qualify, we would provide them with a continuum of services, and even individuals who may be able to help them down the road.

Ms. VAN DUYNE. Are you required to do that by law?

Mr. WILSON. Absolutely not.

Ms. VAN DUYNE. So why do you do it?

Mr. WILSON. Because it is the right thing to do in our communities that we serve.

Ms. VAN DUYNE. Thank you.

Mr. Peters, you had mentioned that per cost of loans if this regulation were to go through, it would possibly increase between $500 and $800 per loan. Can you define what you think would be adding to that increase?

Mr. PETERS. Well, there is a number of systems costs. One, banks are relying on their core vendor. So there would have to be that integration to the core. There would have to be additional software to capture and report the data. There would be somebody that runs that system. There would be audit of that system. There would be compliance. There would be training the lenders on how to tactfully try to gather that information accurately. So it is going to affect at least 15 people and a number of systems. And as my IT group continually reminds me, systems do not run on their own.

Ms. VAN DUYNE. So is your company, is your bank going to just go ahead and take those costs or will those be reflected in the costs that you charge your small businesses?

Mr. PETERS. I think it would have to be reflected into the rate and fees that are charged to the small businesses.

Ms. VAN DUYNE. And Mr. White, I am going to ask you the same question. Do you see that happening?

Mr. WHITE. Yes, I do. When the examiners come in and examine us, one of the things they look at are our earnings. And so banks have to be profitable to get good ratings. If we do not make money at some point we will go out of existence. And so at some point as the regulations get added onto and added onto, those costs do have to be passed on to the customers.

Ms. VAN DUYNE. Thank you.

And Mr. Wilson, do you think that this additional regulation will make loans cheaper for your small businesses or do you think it is going to make it more expensive?

Mr. WILSON. It would certainly be an adverse impact. We have 60 branches in the communities that we serve so think of that as

60 individuals that then have to be completely retrained. All of those systems that go into place, much like Mr. Peters was saying, the domino effect of all of these things is extensive. Just by comparison, we have been working on CECL for nearly 5 years so it is no small undertaking. It is not like simply flipping a switch and wallah, there is the data.

Ms. VAN DUYNE. Thank you. I really appreciate all of your input today and I think it is pretty clear that this additional regulation is bad for small businesses, will increase the costs, and it takes the personal touch that you offer all of your small businesses. So thank you for your testimony here today and I yield back.

Mr. LALOTA. Thank you.

The Chair now recognizes the gentleman from Missouri, Mr. Alford, for 5 minutes.

Mr. ALFORD. Thank you, Mr. Chairman and Ranking Member for holding this important hearing. And thank you to our witnesses for being here today.

Small businesses are supported by community banks and credit unions for their day-to-day business needs. And we have seen a lot on the news lately about our financial system. But what we really do not see in the news cycle and the headlines is how strong our community banks are and our credit unions and how they are still a fortress for our communities.

Since the onset of the bank collapses earlier this month, my team and I have been in touch with a lot of community bankers and credit unions around the district and around the state. Since day one, it has been crystal clear to me that our financial institutions and Missouri stand ready to serve customers' needs just as they have been doing for decades. What they truly do is relationship banking. And I want to give you a personal example.

Just today, I have several accounts, one at a very large national bank that you would recognize the name, and several community banks. And I have a mortgage with a community bank and I did not have enough money in my checking account to cover the mortgage payment due today. My banker, who I had a relationship with before I even thought about running for office texted me this morning and said, hey, Mark, we need to move some money over from one of your accounts to cover your mortgage. Large banks will not do that, folks. Large banks will not do this. It is this Committee's job to allow small businesses to thrive. To do that we have to make sure that community banks and credit unions that serve small businesses and individuals are not overburdened by needless regulation from the unconstitutional Consumer Protection Bureau simply to appease the Biden's far left agenda.

So I want to get in with my question with you, Mr. Peters, Mr. White, and Mr. Wilson. Community banks and credit unions do not have large legal and compliance departments.

Mr. Peters, will the 1071 rule put you at a competitive disadvantage compared to institutions that have larger departments to handle such needs?

Mr. PETERS. Certainly, it would be a heavier lift for us. We do not have the robust systems or the program capabilities internally to build this, report this data as a much larger organization would have.

Mr. ALFORD. Mr. White?

Mr. WHITE. We do not have thousands of employees like the mega banks. We do not have dozens or hundreds of people in our compliance department. Up until just 8 or 10 years ago it was actually the Dodd-Frank Act that required my bank to hire a chief compliance officer. Prior to that, my dad and my brother, who are also with the bank, they were primarily responsible for compliance. So we do not have the people or the means to spread this over.

Mr. ALFORD. Mr. Wilson, I feel you would probably say pretty much the same thing. You are going to have to pick up the slack from somewhere else. How is that going to affect your customers in general?

Mr. WILSON. Sure. Similar to what I said previously, we would have to make this up in infrastructure, staffing costs, retraining. These things have to be passed along somewhere. That is bad for the consumer. And if it makes it too burdensome for small institutions that means less competition which ironically is bad for the consumer. So think about that for a minute.

Mr. ALFORD. Mr. Wilson, my friend from Missouri, Mr. Luetkemeyer touched on this a little bit earlier. I want to delve a little bit deeper into it. The rule that calls for the collection of all sorts of data including race, if race is not evident, is it true that a teller has to assume or I guess, I know Mr. Peters you said that they are going to be tactfully gathering the information. It seems it could be rather sensitive. How do you go about this, Mr. Wilson?

Mr. WILSON. I mean, the thought of putting our entry level folks in this situation is extremely uncomfortable. We have made so much progress socially, you know, and such a focus on diversity, equity, inclusion, belonging, programming, but to do something like this would quite frankly set us backwards and it is not something that we would want to put our entry level associates in that situation of having to guess whether it is in person or over the phone, it is just not right. In addition to that, it could seriously compromise the data if they are wrong based on assumptions.

Mr. ALFORD. Thank you so much again for being here today. This is very important and, you know, we do not need more regulation. We need community banks to support our businesses and our individuals to make us successful in America.

Thank you, and I yield back.

Mr. LALOTA. The gentleman yields.

The Chair now recognizes the Chairman of the Small Business Committee, the gentleman from Texas, Mr. Williams for 5 minutes.

Mr. WILLIAMS. Thank you, Chairman. And I want to, in full disclosure, before I get started, I am a car dealer. That is what I do. When I am not here I own car dealerships in Texas so it makes me kind of a halfway banker. And I have seen a lot of this through a lot of years and we seem to be going back to where ewe were back in the 1960s, and it is not good. And I want to thank all of you again, our witnesses for being here today. And before I ask them more specific questions about this rule I want to take advantage of having some experts in our community banking system in this room.

So Mr. Peters, you being an expert, okay, I want to get your opinion on how small businesses have been adjusting to this high

interest rate environment we now are in, something that did not have to happen, and the general health of small businesses looking to access capital.

Mr. PETERS. Well, certainly, the cost of capital, the cost of loans on a variable rate basis is increasing which puts strain on cash flow and reduces the ability to expand and to hire. And I think the sentiment in many areas where I bank and in the market is that this could lead to recession and that we had better prepare for that and reduce our spending.

Mr. WILLIAMS. Well, and small businesses, you know, interest, again, I am a car dealer, interest in my business tears everything apart from margins to so forth. And when you have a situation like this you are going to have businesses lay off people, are you not? They are going to try to cut costs and people are the highest expense in most businesses. And then the idea that they can raise prices to cover that cost is ridiculous because we have got inflation now so we are going to raise prices. So, this high interest rates we are in is causing just a lot of problems. I tis going to be hard for small businesses to recover. We know that. That is why I am a big tax cutter.

I think everyone in this room shares the objective of making it easier for viable small businesses to get a loan and start working towards the American dream. I believe if we want to make this a reality, imposing a significant new regulatory cost is not the way to do it. We talked about that. Most of the time these people we are hiring, they add no value to our business as far as what they sell. They are an expense. And these new costs will have to be passed along to consumers. There is a point that you cannot do that any longer; right? You just cannot keep passing costs on. And small business loans will get more expensive. All of you have said that. They are already now. So instead we should be examining the regulatory hurdles that are disproportionately harming community banks and credit unions. And not by imposing an expensive new government mandate is going to fix it because once you get the mandate it is hard to back it off.

So Mr. White, can you give this Committee some suggestions of things we should be examining to make it easier for your institutions to get money into your community? So what should we be doing to help you and in the end we help you, you help your borrower?

Mr. WHITE. In general, I would say let us do what we do best, which is help our customers. Do not dictate how we have to do business to help our small businesses. In particular, on 1071, I would say we talked some about the exemption for banks under $1 billion in assets. We would also encourage the revenue threshold to be reduced from $5 million to $1 million. That is still going to cover the vast majority of small businesses in the country. We would also support a mission-based exemption for NDIs and CDFIs as well. But fundamentally, community banks, we know how to help our customers. We have done it for generations. We are stable and successful at doing that. And we just need to be allowed to do it.

Mr. WILLIAMS. Yeah. If the government would get out of your life it would be pretty good, would it not? And maybe we could in-

sert the customer to tell you if you are doing a good job or not and let you compete.

Mr. WHITE. As I said earlier in my testimony, we often, to small business customers and our ag customers, give them an option, whether it is an ag line of credit, do you want a fixed rate for a year, do you want a variable rate based off of prime? We walk them through the differences and we let them pick and they appreciate that.

Mr. WILLIAMS. I have some time left. Mr. Wilson, do you want to add to that? What can we do to help you?

Mr. WILSON. Well, our whole philosophy is built around people helping people. We started 73 years ago when nine people put money into a pot to lend each other money for appliances during the war. So we are very good at what we do. We want to continue to serve our Members. We want to continue to make our associates happy because then they serve our Members well and that in turn makes our communities a thriving place. I think it is critical to mention that it is not 1071 or nothing. There are already incredibly extensive rules, data collection, things that are being provided on a quarterly and annual basis. So at a minimum what NAFCU is asking for is consistency. You have three different definitions. You have what the NCUA has. You have what the SBA has. You have what the CFPB has. That makes it incredibly burdensome for institutions.

Mr. WILLIAMS. My time is up, Mr. Chairman. I yield back.

Mr. LALOTA. I would like to thank all of the witnesses for participating today, to the Members for their thoughtful questions.

And without objection, Members have 5 legislative days to submit additional materials and written questions for the witnesses to the Chair which will be forwarded to the witnesses.

If there is no further business, without objection, the Committee is adjourned.

[Whereupon, at 11:26 a.m., the subcommittee was adjourned.]

APPENDIX

Testimony of

Troy Peters

President and CEO of the Jonestown Bank & Trust Co.

On Behalf of the

Pennsylvania Association of Community Bankers

Before the

United States House of Representatives

Committee on Small Business

Subcommittee on Economic Growth, Tax, and Capital Access

Hearing on

The End of Relationship Banking? Examining the CFPB's 'Small Business Lending Data Collection' Rule

March 28, 2023

Washington, DC

Chairman Meuser, Ranking Member Landsman, and members of the Subcommittee, I am Troy Peters, President of Jonestown Bank & Trust Co. (JBT) headquartered in Jonestown, Pennsylvania. I testify today on behalf of the Pennsylvania Association of Community Bankers. I also am a member of the ICBA.

My bank is celebrating its 150th anniversary this year. Our name has never changed. We have nearly $900 million in assets, eleven full-service branch locations, and 160 employees. Our focus is on small business and retail banking. We are also active in indirect auto lending, and we serve legal cannabis related businesses throughout Pennsylvania and surrounding states.

Community banks like mine provide the bulk of all small business loans in America. We are different than large banking institutions that operate under a contrasting business model that focuses on large companies and loan sizes. Main street businesses, like my customers, prefer to work with a local community bank because we are relationship lenders. We intimately know our markets and our customers.

The CFPB's Small Business Lending Data Collection rule is unfortunately squarely aimed at smaller banks like mine. We are disproportionately disadvantaged to take on the additional system and personnel costs associated with the compliance to this rule. Although much of the costs would need to be passed on to the borrower, it continues to promote further bank consolidation—which means fewer local, community banks to serve the small business segment.

When my career began, this country had over 12,500 banks. Today there are about 4,200. Gone are many of the local banks that were vital to their small towns. Now, due to consolidation, a small business's access to capital is being pushed into metropolitan markets where relationship banking doesn't count for much.

I also worry about the integrity of the data to be collected. In most cases, when a small business is seeking financing, they are looking for the best solution and talking to multiple lenders. Five banks could be collecting this data, but only one will fund the loan. Each bank would be reporting the data, which would make drawing any meaningful conclusion difficult – at best. Small-business loans are by their very nature not cookie cutter. They are tailored to the specific business' needs. It would be very difficult or impossible to collect the exact data points to tell the entire story of the structure, pricing, or counteroffers. There are just too many variables to these loans. They are not as homogeneous as, say, car loans.

Making application and loan data public will certainly be objectionable to my clients and is quite concerning. By publicly displaying sensitive information like how much money they applied for, what the purpose of the loan is, and their revenue number, is not the kind of information they want or expect to be made public from a private transaction. This disclosure could also create a competitive disadvantage for them, such as revealing a planned business investment. Even worse, publishing information that a sole proprietor's loan request was denied, in a small community like ours, is akin the posting a bounced check to the wall behind the store cash

register. The public humiliation shouts "don't do business with this person, they're a deadbeat!" My customers adamantly do not want this.

I have customers like Jay. Jay came to our country seeking opportunity. After years of hard work and savings, he was able to open his own business near the small town of 1,900 people where my bank is headquartered. A few years ago, when the qualified mortgage (QM) rule was implemented, Jay was ready to build his modest dream home. As a long-time customer I would have loved to help him achieve his dream, but his mortgage request didn't comply with the QM rules. Without access to the traditional banking system, Jay turned to an unregulated, hard money lender. His interest rate was higher the loan didn't come with complete disclosure, flexible terms, or collection practices.

I feel like this rule will cause similar unintended consequences and will not be in the best interest of my clients and the communities that we serve.

My hope is that the CFPB will not go beyond the statutory requirements intended for this rule. They should not add additional data points. They should exempt smaller banks like mine, reduce the revenue thresholds, and not breach the privacy of my borrowers.

I love the community banking industry and I love helping my customers. Thank you again for convening today's hearing and for the opportunity to offer the community bank perspective on the CFPB's small-business lending data collection rule.

I'm happy to answer any questions you may have.



Testimony of

Lucas White

President

The Fountain Trust Company

On behalf of the

Independent Community Bankers of America

Before the

United States House of Representatives

Committee on Small Business

Subcommittee on Economic Growth, Tax, and Capital Access

Hearing on

"The End of Relationship Banking? Examining the CFPB's Small Business Lending Data Collection Rule"

March 28, 2023

Washington, D.C.

Chairman Meuser, Ranking Member Landsman, and members of the Subcommittee, I am Lucas White, President of The Fountain Trust Company, a $700 million asset community bank in Covington, Indiana. I testify today on behalf of the Independent Community Bankers of America where I am Chairman-elect. Thank you for the opportunity to testify at today's hearing, "The End of Relationship Banking? Examining the CFPB's Small Business Lending Data Collection Rule."

Community banks are committed to meeting the credit needs of all small businesses in compliance with fair lending laws. ICBA strongly supports the intent of Section 1071 of the Dodd-Frank Act to expand access to credit for minority-owned, women-owned, and small businesses. However, we believe the Consumer Financial Protection Bureau's (CFPB's) forthcoming rule under Section 1071 will have serious unintended consequences. If finalized without significant changes, the rule will have a chilling effect on customized lending, compromise borrower privacy in the rural and small-town markets I serve, and reduce access to credit for certain borrowers. ICBA's comment letter on the proposal provides a more detailed assessment of the impact of the proposal.

Because of the high stakes of this rule for America's small businesses, ICBA is urging Director Chopra to stay the effective date until the Supreme Court has ruled on the constitutionality of the agency. As you know, in October 2022 the U.S. Court of Appeals for the Fifth Circuit ruled that the Bureau's funding structure violates the Appropriations Clause of the U.S. Constitution. The U.S. Supreme Court subsequently agreed to review the Fifth Circuit's decision. A stay of the small business data collection rule would preserve the *status quo* until the Supreme Court can provide small businesses and community banks with more certainty as to the final disposition and validity of the Section 1071 rule before they incur the significant expense and business disruption of compliance.

Is the small business lending data collection rule "the end of relationship banking," as the hearing title suggests? I absolutely believe that it puts relationship banking at risk and should be amended by the Bureau or by Congress at the earliest opportunity. Relationship banking is the key value proposition that community banks like mine offer and our competitive advantage against larger institutions and non-bank lenders.

The Fountain Trust Company has served markets in west-central Indiana since 1903 and has been in my family since 1937. I am a fourth-generation community banker. We have 16 locations and 130 employees, serving rural areas as well as small and mid-sized towns. Our loan portfolio of $328 million consists of commercial, agricultural, and consumer loans, 85 percent of our loans would be subject to the small business lending data collection rule. Relationship banking is the foundation of our success and explains our resilience through numerous economic and agricultural crises.

The CFPB Proposal

Section 1071 of the Dodd Frank Act requires financial institutions to collect certain data regarding applications for credit from women-owned, minority-owned, and small businesses, and to report that data to the Bureau on an annual basis. In September 2021, the Bureau issued a proposed rule to implement Section 1071. Absent a stay, as we have requested, we expect the final rule to be published this week.

While the governing statute requires the collection and reporting of 13 pieces of data in connection with credit applications made by small businesses, the CFPB is using its discretionary authority granted by statute to propose the collection of an additional eight data points not required by statute. These discretionary data points have little to do with a borrower's credit risk but will increase the costs of originating loans and pose a privacy risk to small business applicants.

The Bureau has the authority to exempt community banks from compliance with this rule but has proposed only to exempt lenders that originate fewer than 25 qualifying small business loans per year. A small business is defined as a business with less than $5 million in gross annual revenues. The 25-loan threshold is far too low, and the borrower gross annual revenue threshold is too high, meaning that the data collection requirements would apply to a majority of community banks. My bank, for example, originated 771 commercial and agricultural loans in 2022. Virtually all of these borrowers had less than $5 million in gross annual revenues.

If the Bureau fails to exempt more community banks and business borrowers, the result will be increased compliance costs for community banks and a higher cost of credit for small business borrowers.

The Proposal Would Jeopardize Customized Small Business Lending

Perhaps the most troubling impact of the proposal is the chilling effect it would have on customized lending. Small business lending is not and should not be a commodity. Underwriting is based on numerous borrower characteristics and market variables. Loans are typically customized to suit borrowers' needs and preferences and give them the best chance at success. Because the data collected under 1071 will not reflect the full scope of the underwriting, it may indicate discrimination where none exists.

Fortunately, bank examiners are best positioned to determine whether a loan is discriminatory in application of fair lending laws. Section 1071 is simply the wrong tool for this job. Lenders will respond by standardizing loan features to protect themselves from charges of discrimination. As a result, small business customers will not have access to credit that is customized to their needs. Importantly, minority and women borrowers often benefit from customized lending.

This was the outcome of the Qualified Mortgage rule, also a provision of the Dodd-Frank Act, which effectively forced residential mortgages into a box. Before the QM rule took effect in 2013, our residential mortgage lending was $40 million and constituted nearly one third of our portfolio. Today, residential mortgage lending remains at $40 million, which is about 12 percent of our total loan portfolio of $328 million. QM effectively undermined our in-house mortgage lending by raising regulatory hurdles to loans that do not qualify for the secondary market that were common in the rural markets I serve. I can assure you that the impact has been felt among rural mortgage borrowers. Section 1071, without needed accommodations, threatens to do the same to our small business lending.

A recent loan will illustrate my point. We worked with a local farmer who wanted to open a butcher shop, a vertical integration that made good business sense. We offered him two customized loan options: a fixed rate and a variable rate. I personally walked him through the benefits and drawbacks of each and how future interest rates could affect his loan payments and cashflows. This personalized customer service is what community bankers do best and what sets us apart from the competition. Unfortunately, Section 1071 would make customized, multiple-option lending infeasible. It is impossible to compare loan data across customers who have chosen different options and demonstrate that lending is not discriminatory. Thus, Section 1071 will limit the scope of loan choices available to small businesses.

Borrower Privacy

The breadth of the data required to be collected and potentially published under the CFPB's initiatives may make it possible to identify an individual borrower. Even if individual borrowers are not identified, the perception of that risk is sufficient to drive small business borrowers to larger banks, larger cities, or online lenders where the inclusion of their data in a larger pool will potentially protect their anonymity.

Above I use the example of a butcher/farmer my bank worked with. He's the only butcher in his small town. In the small communities I serve, businesses are readily identifiable. Loan offers contain critical business information and reflect the business owner's personal financial position as a guarantor of the loan.

What's more, as a lender, I consider the loan pricing and other credit terms I offer to be confidential business information. Exposure of this information to competitors would put my business at a disadvantage. Borrower and lender confidentiality are serious concerns that must be addressed in the final rule.

Compliance Expense Will Make Small Business Credit More Costly

Regulatory compliance costs disproportionately impact community banks because they do not have the resources of larger banks, such as dedicated legal and compliance teams and information technology, as well as a larger asset base over which to amortize costs.

Recent years have seen a sharp increase in regulatory burden, which we are still trying to absorb. The small business lending data collection rule, if not amended, will significantly add to the cumulative burden of compliance, and increase the cost of credit for small businesses. My bank's small business lending is carried out through a completely manual process, with all of the analysis done by hand.

Recommendations for Improving the Section 1071 Rule

The harmful impacts described above could be significantly alleviated by amendments to the rule that would exempt more banks and more borrowers and give community banks more time to comply with the rule once it is finalized. Below are ICBA's recommendations.

Replace the loan-volume exemption with an asset-based exemption

The proposal's 25 small business-loan exemption is almost wholly ineffective in providing relief for smaller lenders. An asset-based exemption would ensure that smaller community banks with fewer employees and other resources, for which compliance is disproportionately costly, are exempt. ICBA recommends that banks with assets of $1 billion or less be exempt.

More accurately define "small business"

In defining which businesses are covered applicants, ICBA urges the Bureau to use a threshold of $1 million of gross annual revenue or less. This is a simple, bright-line definition that will make compliance more efficient and straightforward.

A threshold of $5 million is too high. In many regions of the country, a $5 million business is relatively large. According to the U.S. Census Bureau, a $1 million revenue threshold would cover 95 percent of all businesses.

Mission-based exemption

ICBA believes that mission-based banks, such as minority depository institutions (MDIs) and community development financial institutions (CDFIs), should be excluded from coverage under the rule because they have already demonstrated and received special recognition for serving the small business applicants prioritized under Section 1071.

MDIs and CDFIs play important roles in serving the needs of historically underserved communities or primarily serving low-to-moderate income consumers. For this reason, they have been granted special accommodations, such as an exemption from the Qualified Mortgage rule for CDFIs. An exemption from the Section 1071 rule for mission-based banks would help these institutions preserve resources to dedicate to their communities.

Implementation timeline

ICBA recommends a staggered implementation date for the final rule so that smaller community banks are among the last entities required to collect and report the data. In addition, any actions under the Fair Lending Act should be based on data collected under 1071 for a period of at least three years. This delay will allow community banks to refine data collection systems and procedures and will allow regulators to observe trend data.

Support for Legislation

ICBA thanks the Members of Congress who have introduced legislation to make the rule more workable.

The Small Lenders Exempt from New Data and Excessive Reporting Act, sponsored by Rep. French Hill, would:

- Define a "financial institution" as one that originates at least 500 covered credit transactions for small businesses in each of the two preceding calendar years.
- Define a "small business" as one with gross annual revenues of $1 million or less in the most recently completed fiscal year. (The NPRM gross revenue threshold is $5 million or less.)
- Extend the effective compliance date with the final rule to three years after publication in the Federal Register plus a 2-year grace period. (The NPRM has a compliance date of 18 months with no grace period.)

The Business Loan Privacy Act, sponsored by Rep. Blaine Luetkemeyer, would require the CFPB to conduct a rulemaking on proposed modifications and deletions to data the Bureau will publish. The purpose of the proposed modifications or deletions would be to protect the privacy of credit applicants.

Financial institutions as well as small business credit applicants should have a voice in this important determination and should understand what data will be made public before it is collected.

The Preventing Racial Profiling in Lending Act, sponsored by Rep. Roger Williams, would eliminate the proposed rule's requirement that loan officers guess the race or ethnicity of a small business credit applicant based on their last name and physical appearance. This requirement would undermine the right of a credit applicant not to disclose their race or ethnicity. A loan officer's arbitrary guess would too often be mistaken, thus compromising the collected data.

Taken individually or together, these bills would significantly ease the burden of compliance with Section 1071 for community banks and small businesses in pursuit of credit and better protect the privacy of loan applicants.

Conclusion

Thank you again for convening today's hearing and for the opportunity to offer the community bank perspective on the CFPB's small business lending data collection rule.

I'm happy to answer any questions you may have.



Testimony of

Michael Wilson
Chief Experience Officer
Members 1st Federal Credit Union

On behalf of

The National Association of Federally-Insured Credit Unions

Hearing: "The End of Relationship Banking? Examining the CFPB's "Small Business Lending Data Collection" Rule"

Before the

House Small Business Subcommittee on Economic Growth, Tax, and Capital Access

March 28, 2023

Introduction

Good morning Chairman Meuser, Ranking Member Landsman, and Members of the Subcommittee. My name is Michael Wilson, and I am testifying today on behalf of the National Association of Federally-Insured Credit Unions (NAFCU). I currently serve as Chief Experience Officer of Members 1st Federal Credit Union, headquartered in Enola, Pennsylvania. With nearly $7 billion in assets, over half a million members, and 60 branch locations across nine counties in Central Pennsylvania, my role is ensuring an exceptional member experience on behalf of the entire credit union in all interactions and delivery channels—including its branch operations, online banking, customer service, business development, and mobile app. In this role, I provide leadership and direction for the credit union's retail, operations, and customer service areas as well as public relations, marketing, community outreach, internal and external communications, and financial literacy. As you may know, NAFCU is the only national organization that exclusively represents the interests of the nation's federally-insured credit unions at the federal level. NAFCU and the entire credit union community appreciate the opportunity to participate in this discussion regarding the 1071 rulemaking process at the Consumer Financial Protection Bureau (CFPB or Bureau).

My credit union's story began over 72 years ago when nine people put money into a pot, evolving into Naval Supply Depot Mechanicsburg Credit Union with a desk and small counter at the Naval Supply Depot, to what is today a full-service financial institution that exists to help families flourish and better the communities we serve. As a credit union, our "people helping people" philosophy is at the core of everything we do. We build personalized, meaningful relationships and provide unparalleled experiences to our members—from advice and support to a full suite of financial tools designed to help our members live well financially. Members 1st has always been a place where members come first.

The credit union proudly serves nine counties—Adams, Berks, Cumberland, Dauphin, Lancaster, Lebanon, Lehigh, Perry, and York—with nearly 60 branch locations across its footprint. Within the very mission statement of Members 1st is the importance of personal relationships: *We serve*

our members, associates and communities through support, empowerment and meaningful relationships. Because our members span five generations, we offer a variety of choices to suit their lifestyles and transaction preferences. Over the past 72 years, the credit union has perfected its in-person experience for members. As the digital space continues to evolve, so does our commitment to delivering an unparalleled digital experience to our members. In addition to our 24/7, robust digital banking platform, which features online banking and our mobile app—giving members the ability to manage their finances anytime, anywhere—our innovative MyConcierge™ service provides an added layer of convenience. Through MyConcierge™, members have direct access to a personal, local, dedicated point of contact who makes it their goal to help our members achieve their financial goals. Whether you are in one of our branches, on our app or website, or talking to one of our associates on the phone, you will experience the same level of personalized member service.

Corporate social responsibility and community involvement are of paramount importance to Members 1st. In the very fabric of Members 1st's principles are cornerstone values related to supporting community engagement and diversity. There is an entire team at Members 1st dedicated to meeting the outreach needs of the community. Members 1st feels a moral obligation to support the community—not only with logos and sponsorships, but also with significant involvement, presence, and support from its associates to help make Central Pennsylvania a better place to live and work. To further expand upon serving its members, associates, and communities, Members 1st launched the Members 1st Charitable Foundation in 2021 to further its commitment to help communities at the grassroots level after seeing the impact of COVID-19 on consumers, businesses, and non-profits. Members 1st is grateful for the opportunity to serve its members, associates, and communities. We appreciate the opportunity to share our views on the impact the CFPB's 1071 Small Business Data Collection rule will have on small financial institutions like mine.

Background on Credit Unions

Credit unions serve a unique function in the delivery of necessary financial services to Americans. Established by an act of Congress in 1934, the federal credit union system serves to promote thrift and make financial services available to all consumers, many of whom would otherwise have limited access to financial services. Every credit union is a cooperative institution organized "for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes" (12 § USC 1752(1)). Congress established credit unions as an alternative to banks and to meet a precise public need, and today credit unions provide financial services to over 135 million Americans. Since President Franklin D. Roosevelt signed the Federal Credit Union Act (FCU Act) into law nearly 89 years ago, two fundamental principles regarding the operation of credit unions remain every bit as important today as in 1934:

1. Credit unions remain totally committed to providing their members with efficient, low-cost, personal financial services; and,
2. Credit unions continue to emphasize traditional cooperative values such as democracy and volunteerism.

The nation's approximately 4,800 federally-insured credit unions serve a different purpose and have a fundamentally different structure than traditional banks. Credit unions exist solely for providing financial services to their members, while banks aim to make a profit for a limited number of shareholders. As owners of cooperative financial institutions, united by a common bond, all credit union members have an equal say in the operation of their credit union—"one member, one vote"—regardless of the dollar amount they have on account. These singular rights extend all the way from making basic operating decisions to electing the board of directors, something unheard of among for-profit, stock-owned banks. Unlike their counterparts at banks and thrifts, federal credit union directors generally serve without remuneration, epitomizing the true volunteer spirit permeating the credit union community. Credit unions continue to play a very important role in the lives of millions of Americans from all walks of life. Since the Great Recession, consolidation of the commercial banking sector has progressed at an increasingly

rapid rate. At a time when for-profit banks are deemphasizing the human touch for financial services, credit unions are second-to-none in providing their members with quality personal financial services at the lowest possible cost.

Credit Unions as Small Business Lenders

Credit unions have a long history of helping underserved communities due to their cooperative structure, and nothing demonstrates this better than response to the COVID-19 pandemic, when NAFCU members extended loans through the Paycheck Protection Program (PPP) to small businesses that had been turned away by for-profit banks. According to a NAFCU survey of our members, 87 percent of respondents had small business members join their credit union to secure PPP funding in 2020 and 2021.

Unfortunately, credit unions have an artificial barrier to being able to do all that they can to help small businesses. When Congress passed the Credit Union Membership Access Act (CUMAA) (P.L.105-219) in 1998, it put in place restrictions on the ability of credit unions to offer member business loans. Credit unions had existed for nearly 90 years without these restrictions. Congress codified the definition of a member business loan and limited a credit union's member business lending (MBL) to the lesser of either 1.75 times the credit union's actual net worth or 1.75 times the minimum net worth of a well-capitalized credit union (12.25 percent).

CUMAA also established, by definition, that only business loans above $50,000 count toward the cap. This number was not indexed and has not been adjusted for inflation in the nearly 25 years since enactment, eroding the de minimis level. Where many vehicle loans or small lines of credit may have been initially exempt from the cap in 1998, many loans that meet the needs of small business today are now included in the cap due to this erosion. To put this in perspective relative to inflation, what cost $50,000 in 1998 costs over $92,000 today, using the most recent consumer price index data. That is more than an 80 percent rate of inflation that is completely ignored by current law and greatly hamstrings a credit union's ability to meet its members' needs.

It should be noted that the government-guaranteed portions of Small Business Administration (SBA) loans do not count toward the member business lending cap, but the non-guaranteed

portions do. This could ultimately lead to a situation where a credit union may be an excellent, or even preferred, SBA lender and ultimately have to scale back participation in Small Business Administration (SBA) programs as it approaches the arbitrary cap. This would likely hit SBA Express loans first, as those have lower guarantees and, thus, may have a bigger impact on money available below the cap.

As such, we would urge Congress to support legislation to modify or remove the arbitrary cap on credit union member business lending. At the very least, Congress should update the $50,000 threshold to reflect inflationary changes over the last quarter century. This was proposed as part of H.R. 5189, the Member Business Loan Expansion Act, a bipartisan bill by Representatives Vincente Gonzalez and Brian Fitzpatrick in the 117th Congress.

While some on the banking side may say that credit unions unfairly compete, we would note that a 2011 study commissioned by the SBA's Office of Advocacy found that bank business lending was largely unaffected by changes in credit unions' business lending, and credit unions' business lending can actually help offset declines in bank business lending during a recession (James A. Wilcox, *The Increasing Importance of Credit Unions in Small Business Lending*, Small Business Research Summary, SBA Office of Advocacy, No. 387 (Sept. 2011)). The study shows that during the 2007-2010 financial crisis, while banks' small business lending decreased, credit union business lending increased in terms of the percentage of their assets both before and during the crisis.

Members 1st FCU's Role as Small Business Lender

Members 1st is proud of its work as a small business lender. We started our member business lending program in 2003, and last year we did $350 million in business lending. We hold $90 million in business deposits. We have over 3,600 business loans on the books with nearly $1 billion in balances. We are proud of our work in Central Pennsylvania. During the pandemic we were the 9th largest PPP lender in the credit union space, in addition to helping our members through a trying financial time. We are also a participant in the 7(a) loan program through the SBA.

Concerns with the Current Rulemaking

The 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was enacted to respond to the 2008 financial crisis. One of the key provisions of this act was the creation of the CFPB. The Bureau was established to protect consumers from another financial crisis, with institutions below $10 billion exempted from its oversight and enforcement. Everyone agrees that credit unions did not cause the 2008 financial crisis, and that is why NAFCU expressed concerns about the increased regulatory burdens that credit unions would face being subject to new rules from another regulator (the CFPB) in addition to the National Credit Union Administration (NCUA). Unfortunately, our concerns have proven true, as the number of credit unions has declined by over 37 percent since the passage of the Dodd-Frank Act with regulatory burden being the number one reason given for credit unions disappearing.

Included in the Dodd-Frank Act was Section 1071, which amended the Equal Credit Opportunity Act (ECOA) to require financial institutions to report information concerning credit applications made by women-owned, minority-owned, and small businesses. The legislative purpose of Section 1071 is to facilitate enforcement of fair lending laws and to enable communities, governmental entities, and creditors to identify business and community development needs and opportunities of women-owned, minority-owned, and small businesses. NAFCU and credit unions support this goal. However, we have concerns about how the CFPB is choosing to carry out its authority. As the Subcommittee looks at the issue of how these new requirements could restrict access to credit for small businesses, especially from smaller lenders, we would like to take this opportunity to share our concerns with the CFPB's notice of CFPB's proposed rulemaking (Proposed Rule) under Section 1071 of the Dodd-Frank Act.

NAFCU has a series of concerns about the proposal and its impact on access to credit from credit unions for small businesses that we have shared with the Bureau. These are outlined below:

Covered Financial Institutions

While Section 1071 defines "financial institution" to include a reasonably expansive list of different types of entities that may engage in small business lending, Section 1071 establishes neither a metric nor a threshold by which to identify those from whom Congress anticipated the Bureau would collect small business lending data. Under the Proposed Rule, any entity meeting Section 1071's definition of a financial institution that originated at least 25 covered credit transactions for small businesses in each of the two preceding calendar years would be a covered financial institution. The Proposed Rule's 25 loan-volume threshold was the lowest, non-zero loan volume threshold considered by the Bureau in prior Section 1071 rulemaking exercises. The Bureau anticipates it could lower one-time Section 1071 compliance costs by roughly $120 million and still collect Section 1071 data for approximately 94 to 95 percent of all small business loans made by depository institutions if it establishes a 100 loan-volume threshold. However, it is obvious that a 100 loan-volume threshold is much too low still. For decades, mortgage market stakeholders have drawn statistically significant conclusions about the health and fairness of the mortgage market from data collected and reported subject to the Home Mortgage Disclosure Act (HMDA), which, the Bureau has estimated, captures something just shy of 90 percent of all available mortgage data. Establishing a 100 loan-volume threshold or any other loan-volume threshold that operates to capture more Section 1071 data than is necessary at the expense of small business borrowers runs counter to the Bureau's Section 1071 responsibilities.

Compounding this concern is the Bureau's reliance on NCUA 5300 Call Report data and similar banking industry data. A great deal of small business lending occurs below the relevant $50,000 reporting thresholds. The Bureau may welcome larger covered financial institutions' being required to report even more Section 1071 data than the Bureau now projects. However, the Bureau should be deeply concerned that its overreliance on Call Report data risks the Bureau materially underestimating how many credit unions would likely be covered financial institutions under artificially low 25 and 100 loan-volume thresholds. NAFCU encourages the Bureau to adopt a covered financial institution loan-volume threshold not lower than 500 covered credit transactions.

Chilling Effect on New and Modest Small Business Lenders

The Bureau acknowledges that some credit unions, faced with the Proposed Rule's significant onetime and ongoing compliance costs, may simply be forced to exit small business lending altogether. Other credit unions, the Bureau anticipates, will attempt to manage their small business lending activities so as to narrowly avoid crossing whatever loan-volume threshold the Bureau ultimately adopts. This is bad for small business and shows a lack of understanding about credit unions.

While it is theoretically possible that a credit union or bank could manage its small business lending activity in such a way as to avoid crossing a loan-volume threshold, the theory quickly erodes when one considers the fluidity and iterative nature of most small business lending. Small business lending, particularly at credit unions, is often the product of a lengthy, relationship-intensive process that unfolds over weeks, months, and, sometimes, years. Credit unions and entrepreneurs work diligently alongside one another to understand small businesses' strengths and capital needs and identify appropriate small business solutions. Consider the simplest context, one in which a credit union has never engaged in a credit transaction covered by the Proposed Rule. Aware that not all credit applications are approved and not all approved credit applications result in a member accepting the approved terms, the credit union would rationally work to cultivate small business relationships in excess of its targeted loan-volume. During years-long periods in which application approvals and borrower acceptances are above average, or emergencies press a credit union to redouble its commitment to its community, can the credit union truly be expected to abandon or stall its small business members the moment it unexpectedly meets its target loan volume? Next, consider one of the thousands of credit unions that may wish to better support its small business members by beginning to offer an affordable small business credit card product. If a credit union was simultaneously managing its small business lending activity to ensure it is not exposed to Section 1071 compliance costs it is unable to afford, every new small business credit card account would represent one fewer traditional small business loan it could make, irrespective of a small business member's need. Similar examples are not in short supply, but the effect of each is the same. Credit unions' reliably

managing small business lending activity to a specific loan volume is simply implausible, if not impossible. More likely, these credit unions, too, would be forced to avoid or exit small business lending altogether.

In conversations with members, NAFCU has observed that anxiety regarding Section 1071's future costs may already be having a chilling effect on future plans to expand small business lending operations. After the passage of the Coronavirus Aid, Recovery and Economic Security Act (CARES Act), credit unions expressed optimism that public awareness of the PPP's funding might enhance general demand for SBA loans. Credit unions that had never previously sought to promote small business loan products also expressed interest in sustaining small business lending even after the PPP was exhausted. However, after the Bureau's Section 1071 rulemaking efforts were more widely publicized in September 2020, some credit unions expressed hesitancy about pursuing small business lending due to uncertainties surrounding the costs of Section 1071 compliance. According to a 2011 study from the SBA, while banks tend to reduce lending during economic stress, credit unions continue to lend to small businesses. During the Great Recession, credit union lending offset a proportional reduction in bank lending. The Bureau's January 2020 data point found the number of credit unions offering small business lending products doubled since 2004, from 10 percent to 20 percent. As big banks continue to avoid historically-disadvantaged communities and desert short-lived efforts in others and as community banks continue to merge, the Bureau must be keenly aware of the Proposed Rule's ability to chill small business lending by credit unions, sometimes the only in-community option remaining for small businesses.

Covered Applications

NAFCU appreciates the Proposed Rule's providing that "a financial institution has latitude to establish its own application process or procedures." Small business lending, particularly at credit unions, is often an iterative process tailored to borrowers' unique needs and not a rote walk-through of a fill-in-the-blank template. NAFCU is, however, concerned by the Proposed Rule's not adopting Regulation B's definition of a "complete application." The Bureau's adopting a

"complete application" definition, as opposed to the Proposed Rule's comparatively open-ended definition of an application, would alleviate the significant burden covered financial institutions would have in collecting Section 1071 data from unengaged applicants that have no intention of completing the application process. Unnecessary compliance costs that would in short order translate to higher small business borrowing costs would be avoided, and the integrity of valuable Section 1071 data on the most important small business lending activity would be protected. While it may be convenient for the Bureau to have data regarding incomplete applications when it explores fair lending issues related to borrower discouragement, there is no indication that Congress intended for Section 1071 to mirror the requirements found in the HMDA and Regulation C. Furthermore, it appears plausible that many incomplete applications could be the product of borrower confusion regarding the need to supply unfamiliar, deeply personal data points rather than the product of borrower discouragement. To the extent that borrower discouragement intersects with more easily measurable fair lending concerns, the Bureau will have more than sufficient Section 1071 data, in addition to its existing examination authorities, to investigate ECOA violations involving small business lending products.

Small Business Definition

The Proposed Rule would define a small business as any business with prior-year gross annual revenue of $5 million or less. NAFCU supports regulation that enables credit unions to more quickly and confidently support their communities' small businesses. Also, as previously expressed, NAFCU appreciates the obvious benefits of any easy-to-apply small business definition based on gross annual revenues. However, as discussed more fully in other sections, credit unions generally anticipate being forced to pass along their Section 1071 compliance costs to small business borrowers in the form of higher fees. Small business lending fees are, like many sales taxes, regressive in nature, disproportionately expensive for small businesses borrowing the least. It is altogether possible that fees for the smallest dollar small business lending products could increase to such a proportion that the smallest dollar products altogether disappear from the small business lending market or are offered only by the least scrupulous, least regulated small business lenders. A gross annual revenue threshold must, therefore, operate to cost-

effectively capture only the data reasonably necessary to enable stakeholders to draw statistically significant conclusions about the health and financial needs of truly small businesses. Based on the underwriting experiences of its members and the SBA's relevant standards, NAFCU recommends that the Bureau adopt a small business definition based on a $1 million prior-year gross annual revenue threshold.

Covered Credit Transactions

The Proposed Rule broadly defines a covered credit transaction to include any extension of business credit other than trade credit, public utilities credit, securities credit, and incidental credit, which are expressly excluded. The Bureau anticipates explaining in the Official Commentary that factoring, leases, consumer-designated credit used for business purposes, and credit secured by certain investment properties are not covered credit transactions. Under the Proposed rule, credit unions' small business loans, lines of credit, and credit cards would all be covered credit transactions. If a credit union offers its small business members a merchant cash advance (MCA) product, that too, would be a covered credit transaction under the Proposed Rule. To gauge the size and distribution of the small business lending market comprised of these products, the Bureau relied on 2019 NCUA Call Report data and similar banking industry data. However, the Proposed Rule offers no de minimis threshold below which an otherwise covered credit transaction would not count toward a financial institutions' loan-volume threshold.

NAFCU recommends that the Bureau put its assumptions into practice and establish a *de minimis* threshold applicable to all covered credit transactions that tracks the NCUA Call Report threshold, currently $50,000. Congress's decision to exclude member loans under $50,000 from credit unions' MBL caps and the NCUA's corresponding decision to exclude such loans from Call Reports reflect a general, reasoned understanding that burdensome reporting requirements frustrate very small businesses' access to affordable, high-quality small dollar loans. Small dollar loans are particularly important to sole proprietorships. As the Bureau makes extensive note, the majority of women- and minority-owned businesses are sole proprietorships. In the alternative, NAFCU recommends that the Bureau delay any further Section 1071 rulemaking until the Bureau is

prepared to present a more transparent methodology describing the likely coverage of financial institutions based on lower covered credit transaction thresholds. NAFCU also recommends that the Bureau expressly exclude small business credit cards from the Proposed Rule's definition of a covered credit transaction. An informal survey of a cross section of NAFCU members suggests that the vast majority of credit unions' new small business credit card account limits are well below the NCUA 5300 Call Report threshold – with median limits hovering tightly around $10,000.

NAFCU understands from other industry stakeholders that similar trends persist in nearly every identifiable sub-section of the banking industry. Under the Proposed Rule, as written, a credit union's approving even marginal small business credit card account limit increases would push the credit union closer toward whatever loan-volume threshold the Bureau ultimately adopts. It seems likely, therefore, that absent the Bureau either establishing a meaningful *de minimis* threshold or expressly excluding small business credit cards from the Proposed Rule's definition of a covered credit transaction, every credit union that offers even a single small business credit card product will ultimately become a covered financial institution on that basis alone.

Furthermore, the Bureau estimates that roughly three-quarters of credit unions do not yet offer a small business credit card product. Any one of that number that subsequently offers its small business members an alternative to high-fee, high-interest small business credit card products pushed by big banks and fintechs would likely find itself soon exposed to the Proposed Rule's extraordinary compliance costs, irrespective of any other small business activities. NAFCU supports the Bureau's exclusion of consumer-designated credit transactions from the Proposed Rule's definition of a covered credit transaction and recommends that the Bureau further clarify that it will not challenge a credit union's designating an otherwise covered credit transaction to be a consumer-designated credit transaction. NAFCU believes that preserving such discretion is critical to mitigating overall Section 1071 compliance risks given covered financial institutions have no reliable method for validating a latent business purpose in an application for a consumer-designated credit transaction.

Finally, because NAFCU believes it is unlikely Congress intended to include commercial real estate loans made to investors within the scope of Section 1071, NAFCU again recommends that the Bureau consider expressly exempting such loans from the Proposed Rule's definition of a covered credit transaction rather than rely on the Official Commentary's operation. It is often the case that these loans' relevant data are already reported under the HMDA. Additionally, commercial real estate loans made to investors are typically made to business entities with complex ownership structures that make it difficult for financial institutions to determine even the identity of all a borrower's principal owners.

Mandatory Data Points

Credit Purpose: NAFCU recommends that the Bureau further clarify how covered credit transactions should be reported when they are made directly to the sole proprietor of a business, not to the business itself. Credit unions engaged in small business lending to sole proprietors individually may find it confusing to report a loan purpose that implies that the business itself is the recipient.

Amount Applied For: NAFCU recommends that the Bureau grant financial institutions the discretion to report an "amount applied for" that is determined at a later stage, rather than at the first request of the applicant, because reporting the first initial credit request could inaccurately represent the lending process. Particularly in transactions involving real estate or equipment, many small businesses will request a much higher loan amount than what is ultimately approved after evaluation of collateral. For startups and sole proprietorships, a lack of sophistication can also lead to similarly unrealistic initial requests. In these cases, credit unions work diligently with applicants to arrive at a more reasonable amount, but such education could take place over a period of weeks or months.

Census Tract: The geocoding requirement will be a source of significant burden for many credit unions, the vast majority of which do not collect census tract information for small business loans.

Although some Community Financial Development Institution (CDFI) credit unions collect census tract information, many are completely unfamiliar with how to collect this information—particularly those that are exempt from the HMDA's reporting requirements. Those credit unions that do not use the Federal Financial Institutions Examination Council's (FFEIC) geocoding tool to collect census-tract information will need to acquire a separate software license from a vendor to implement geocoding. There may also be separate related costs for periodic system upgrades. The FFIEC geocoding tool also does not permit batch inputs, which further slows more manual application processes at credit unions. For credit unions with limited staff, such a bottleneck could mean losing business as members frustrated by longer approval times look elsewhere. NAFCU, therefore, recommends that the Bureau develop a free tool for use by covered financial institutions that permits batch inputs and better enables covered financial institutions to more efficiently, cost effectively fulfil their Section 1071 responsibilities.

Protected Demographic Information and Visual Observation

Under the Proposed Rule, in certain circumstances, a covered financial institution's employee would be forced to determine the ethnicity and race of a small business applicant's principal owner via visual observation. NAFCU unequivocally opposes the Bureau's adoption of any regulation or examination practice that operates to require that any individual make any visual observation concerning any protected demographic information or similarly sensitive data of a small business applicant's owners. Humans have immense and persistent difficulties accurately and precisely identifying others' race and ethnicity. Routinely inaccurate visual observations of this sensitive data would not only threaten the integrity of other valuable Section 1071 data but would add unnecessary friction to small business relationships and give rise to avoidable, unreasonable fair lending risks.

The Proposed Rule's requiring, in certain instances, that a covered financial institution's employee make visual observations of protected demographic information may, too, expose covered financial institutions to compliance costs related to an evolving patchwork of state personal data privacy laws. While some states' personal data privacy laws provide financial

institutions an institution-level exemption, at least one state, California, provides financial institutions only an information-level exemption. To the extent protected demographic information is deemed not to be collected "subject to" or "pursuant to" the Gramm-Leach- Bliley Act, Californians may have certain robust personal data privacy rights with respect to their visually observed protected demographic information collected and maintained by covered financial institutions.

Discretionary Data Points

Section 1071(e)(2)(H) requires financial institutions to collect and report "any additional data that the Bureau determines would aid in fulfilling the purposes of [Section 1071]." The Proposed Rule would require covered financial institutions to collect and report the following eight discretionary small business lending data: pricing, time in business, North American Industry Classification System (NAICS) code, number of workers, application method, application recipient, denial reasons, and number of principal owners. In light of the significant one-time and ongoing Section 1071 compliance burdens already facing covered financial institutions with respect to their collection and reporting of mandatory data, NAFCU opposes the Bureau's adoption of any discretionary Section 1071 data points. The Proposed Rule's discretionary data points represent data that is neither materially useful in fulfilling the ultimate objectives of Section 1071 nor reliably obtainable by cost-effective means. NAFCU anticipates that any Section 1071 final rulemaking will tend to widen the competitive gulf between credit unions and big banks and fintechs that have the economies of scale and the technological sophistication to automate complex functions.

The Bureau's requiring covered financial institutions to collect and report even more discretionary Section 1071 data will only compound credit unions' competitive disadvantages. For example, NAFCU members who participated in the PPP noted that many small business applicants either did not know what a NAICS code was or how to determine which NAICS code most closely matched their business. Manually collecting just this data point will require a credit union to devote a significant amount of time and resources to ineffective education. One

statutory purpose of Section 1071 is to facilitate enforcement of fair lending—a goal that is not sector dependent. The identification of business and credit needs can be accomplished without explicit reference to NAICS codes, such as by leveraging already existing data sources and voluntary surveys of business owners. Furthermore, sector-specific analysis of business credit supply and demand is best left to the SBA, which already collects NAICS information through its lending programs. The risks of the Bureau's collecting the Proposed Rule's discretionary data is not limited to increased compliance costs that drive small business lending costs higher. The Bureau's collection and ultimate reporting of small businesses' time in business, NAICS code, and number of workers, coupled with census tract information, raises serious concerns about small businesses' privacy. Such discretionary data, when made public, could be used to re-identify small business borrowers and help competitors gain impermissible insight into financial information directly bearing on small businesses' long-term financial health and competitive goals.

Firewall

Section 1071 generally contemplates the existence of an information firewall between employees handling inquiries about a small business applicant's status as a women-owned, minority-owned, or small business and those employees engaged in underwriting. Under Section 1071(d)(2), if a financial institution discovers that an underwriter or others involved in making a determination regarding an application "should have access" to such information, it must provide an applicant a notice of "the access of the underwriter to such information, along with notice that the financial institution may not discriminate on the basis of such information."

Unfortunately, the Proposed Rule's low loan-volume threshold and expansive covered credit transaction definition will likely operate to require the distribution of the proposed Section 1071 information firewall disclosure far more often than Congress intended. Too frequent distribution will produce untenable, negative real-world effects that weigh most heavily on those the regulation is intended to protect. Many credit unions have small business lending departments comprised of three or fewer employees. Small business lending at such credit unions across the

country is more often than not an all-hands-on-deck effort. In operation, the Proposed Rule threatens to create the powerful illusion that these modestly-staffed credit unions are incapable of guaranteeing that protected demographic information will not affect an underwriting decision. The effect will likely be particularly pronounced with respect to women- and minority-owned small businesses, the entrepreneurs of which routinely come face-to-face with the realities of their relative economic disadvantages. A rational entrepreneur of a women- or minority-owned small business would be forced to consider accepting higher interest rates and other onerous credit terms in exchange for the relative peace of mind that a big bank's or fintech's seemingly limitless technology and personnel budgets ensure that protected demographic information remains shielded from underwriters.

The Bureau cannot eliminate the Section 1071 information firewall disclosure's giving the appearance that credit unions are incapable of adequately shielding protected demographic information from underwriters. But the Bureau should reduce the need for its distribution by adopting Section 1071 regulation with commonsense definitions and right-sized thresholds.

Reputational Risks Related to Statutory Limitations and Future Balancing Test

The publication of small business data from credit unions risks presenting a misleading portrait of overall credit availability due to variables such as field of membership and aggregate MBL limits. As a result of these unique statutory restrictions, credit union lending patterns may not translate easily when compared to other institutions. Accordingly, it is imperative that the Bureau supply a transparent description of the methods and analysis it will apply when evaluating Section 1071 data for supervisory purposes. The Bureau should also recognize that some credit unions may respond to perceived reputational risks associated with data publicization by eliminating certain product offerings or modifying underwriting practices in a way that reduces the overall diversity of small business products. In such a scenario, small businesses could ultimately find it more difficult to acquire credit on favorable terms if financial institutions seek to flatten pricing artificially because they are concerned by the outward appearance of such discrepancies, even when no discrimination, in fact, exists.

Credit unions may also need to allocate additional resources to respond to inquiries about Section 1071 data from NCUA examiners, who will be performing fair lending analysis of Section 1071 data for the first time. To help credit unions better assess possible reputational concerns, the Bureau must also provide a full and complete explanation of any balancing test it intends to use to limit public disclosure of Section 1071 data. Merely referencing a conceptual framework and then articulating the full policy later, as the Bureau does in the Proposed Rule and did with the HMDA, will not suffice. For credit unions to accurately assess the full range of privacy and reputational impacts that might be associated with any proposal, there must be a complete understanding of how the balancing test will be applied. For example, credit unions might approach their assessment of the costs of collecting certain data items by considering how it might be used to reidentify a borrower. The risk of reidentification cannot be fully known unless the Bureau provides a complete description of how a balancing test or other methodology for limiting public disclosure works.

One-Time and Ongoing Compliance Costs

NAFCU is significantly concerned that the Bureau has materially underestimated the one-time and ongoing costs credit unions are likely to face under the Proposed Rule. While, like others, NAFCU's members have had insufficient opportunity to explore all options, early indications are that third-party training, information technology, and auditing expenses are likely to be several multiples higher than the Bureau's estimates. The Bureau's estimates with respect to training, for example, tend to reflect a scenario in which the only staff trained on Section 1071 compliance are those staff for whom Section 1071 data collection and reporting are a primary, largely autonomous job function. Such a scenario may be realistic at the smallest credit unions that have only two or three staff engaged in business lending and at the very largest credit unions with dedicated fair lending compliance departments. However, for credit unions with modest but not minimal staff, such an expectation ignores the fact that it is often the case that all or most employees are trained on all compliance issues to promote cross-functional efficiencies.

Expenses may be driven higher still if the Bureau adopts an insufficient mandatory compliance schedule.

Mandatory Compliance Schedule

The Proposed Rule's 18-month mandatory compliance schedule would be aggressive even for the largest, most technologically savvy credit unions. As discussed above, the vast majority of credit unions likely to be covered financial institutions under the Proposed Rule will be forced to rely on multiple IT vendors to develop, redeploy, and cross-test Section 1071-compliant small business lending programs and tools. Furthermore, many credit unions, because they are exempt from the HMDA's reporting requirements, have no preexisting HMDA software solutions or IT vendor relationships to leverage. These credit unions will require even more time to come into compliance with robust, technology-intensive Section 1071 regulation.

Past experience with the Bureau's implementation of the HMDA suggests that the Bureau is likely underestimating the time required for IT vendors to adapt their products to comply with major rulemakings. Relatedly, many NAFCU members who entered the small business lending market for the first time through the PPP to help local businesses reported having done so by relying on existing resources, not new technologies or other efficiencies. That some credit unions may now provide a more diverse range of products does not necessarily equate to greater sophistication or reduced reliance on manual systems. Credit unions across the country have simply worked harder for longer to support their communities' small businesses during the COVID-19 pandemic. NAFCU strongly encourages the Bureau to adopt a phased mandatory compliance schedule based on covered financial institutions' loan volumes that begins no sooner than three years following the Bureau's adoption of a Section 1071 final rulemaking. The credit unions that have the least bargaining power with powerful third-party IT vendors are often the last to receive core system upgrades and must have the time necessary to become fully compliant with a Section 1071 final rulemaking.

We are supportive of efforts to address concerns about the compliance deadline such as the Small Lenders Exempt from the New Data and Excessive Reporting (LENDER) Act, offered by Representative French Hill.

Coordination of Examinations

Unlike mortgages, which are largely homogenous consumer products, small business loans can vary widely in design and purpose. Accordingly, prudential regulators' examiners applying the same analytical techniques and examination approaches applicable to the HMDA's enforcement to small business data may yield erroneous results. Absent a clear description of the methodologies that might be employed to perform fair lending analysis using Section 1071 data, there will likely be a period where prudential regulators' examiners' expectations are in flux and, perhaps, materially inconsistent. To the extent that credit unions are subject to Section 1071 reporting, the Bureau must coordinate with other FFIEC agencies, including the NCUA, to develop model examination procedures in advance of the Bureau adopting a Section 1071 final rulemaking.

Small Business Lending Data Collection and the SBA

If the SBA again engages in direct small business lending, small business borrowers would face two material, perhaps not obvious, risks – higher borrowing costs and a consolidated small dollar lending market. The Bureau cannot be held responsible for the actions of other agencies, but the Bureau must remain keenly aware that its Section 1071 rulemaking has significant impacts on a small business lending market shaped by powerful private and public competitive pressures.

First, the Proposed Rule's Official Commentary specifically includes "governmental lending entities" within the definition of a financial institution. While the SBA's balance sheet and reach may more closely resemble those of big banks and fintechs than those of a credit union, the SBA, as the PPP made clear, is significantly reliant on manual information processing and the smooth functioning of the individual offices within its vast network. If the SBA engages in direct lending, it will no doubt meet the Proposed Rule's definition of a covered financial institution. With the

lessons of the last few years firmly in mind, the SBA would likely find it necessary to train nearly all employees on Section 1071 compliance to ensure modestly staffed offices can meet their Section 1071 responsibilities in times of pronounced small business needs. To offset these and other costs related to the collection and reporting of Section 1071 data, the SBA would likely be forced to raise the costs of small business lending products that are, for some borrowers, the best available option.

Second, if the SBA again engages in direct small business lending, the SBA would threaten all credit unions' disintermediation in the increasingly important small dollar segment of the business lending market. Not only do recent SBA proposals lack the statutory guardrails to prevent the SBA from becoming credit unions' direct lending competitor, but they also create the risk of fintechs, which have never been permitted to originate 7(a) loans, driving credit unions entirely out of 7(a) lending. The direct lending proposal's net effect of increasing private-sector competition for ever fewer private sector SBA lending opportunities will chill credit unions' 7(a) lending and lead to a consolidation of small dollar lending to the detriment of small businesses. As the Bureau contemplates its Section 1071 final rulemaking, NAFCU encourages the Bureau to remain keenly cognizant that its decisions will bear mightily on a profoundly complicated and rapidly changing small business lending market. The Bureau cannot be expected to alleviate all the ill-effects of a potential SBA direct lending program, but the Bureau should ensure that its Section 1071 final rulemaking does not unnecessarily compound small dollar lending price increases or speed the small dollar lending market's consolidation. NAFCU does not support an SBA direct lending program and would urge expressly excluding loans extended by depository institutions and backed by a governmental entity from its Section 1071 final rulemaking's definition of a covered credit transaction.

Recommendations

With the final Section 1071 rule set to be released, NAFCU urges the CFPB to exercise its discretionary authority to exempt smaller institutions from this rule as the compliance costs outweigh any benefit. If such an exemption is not granted under the CFPB's Section 1022

authority, we would hope to see significant changes to the proposed rule as outlined above. Should the Bureau not address these, we urge Congress to step in with your oversight authority and to consider statutory changes to address our concerns such as enacting the Small LENDER Act. Failure to do so would threaten access to credit for many of our nation's main street small businesses who rely on community lenders like credit unions to meet their capital needs.

Furthermore, to help reduce barriers to credit unions providing credit to small businesses, we would urge Congress to take steps modernize the FCU Act's member business loan provisions such as updating the *de minimis* threshold for loans from $50,000 to $100,000 as proposed in the Member Business Loan Expansion Act.

Conclusion

While NAFCU supports the goal of ensuring access to capital for women-owned, minority-owned and small businesses, we believe the costs associated with instituting the proposed Section 1071 small business data collection rule will overshadow any hypothesized improvements in supervisory efficiency or market transparency. Congress also enacted Section 1022 of the Dodd-Frank Act, which requires an assessment of the effectiveness of each rulemaking at the CFPB, and even included a specific exemption provision with Section 1071 itself. The Bureau should exercise the authority granted by Congress to provide small lenders such as credit unions relief from a number of burdens stemming from the Section 1071 rulemaking. The alternative is to impose yet another data collection regime that is certain to exacerbate the cumulative toll of regulatory burden endured since the last financial crisis, particularly for smaller community financial institutions like credit unions that have experienced significant and ongoing consolidation. Section 1071, like many Bureau rulemakings, will likely drive further consolidation, reduced choice, and potentially result in small businesses losing access to trusted, responsible, and affordable community lenders. If the CFPB will not address these concerns in their rulemaking, we would urge Congress step in and make changes.

I thank you for the opportunity to testify today and look forward to answering your questions.

ACCION OPPORTUNITY FUND

TESTIMONY BEFORE THE UNITED STATES HOUSE COMMITTEE SUBCOMMITTEE ON Economic Growth, Tax, And Capital Access
BY
LUZ URRUTIA, CHIEF EXECUTIVE OFFICER ACCION OPPORTUNITY FUND, AND OPPORTUNITY FUND
ON
March 28, 2023

Good morning, Chairman Meuser, Ranking Member Landsman (OH-01), and Members of the Committee.

Luz's Background with Accion and Entire Career

Thank you for the opportunity to testify and discuss the CFPB's Small Business Lending Data Collection Rule, Section 1071.

My name is Luz Urrutia, and I am the CEO of Accion Opportunity Fund (AOF), one of the nation's leading non-profit Community Development Financial Institutions (CDFI) providing access to loans, business advising and networks to underinvested entrepreneurs.

I spent my entire career in for-profit financial services, which included nearly two decades at Wachovia Bank, then as the co-founder and CEO of a community bank in Atlanta, and as CEO of a payday lending company where I helped to ensure that they provide responsible financing to their customers.

I joined AOF as its CEO because of my experience as a lifelong for-profit banker and my passion for providing responsible financial services to underinvested communities. I know for a fact that business and lenders can generate profit and do the right thing investing in all communities.

AOF

As CEO, I am very proud of the impactful work (AOF) has done to provide capital to entrepreneurs that are often left behind by our financial system.

To date, we have deployed over $700 million to over 25,000 entrepreneurs and 80% of our borrowers are entrepreneurs of color, women and/or immigrants. In fact, women make up one out of every three clients we serve.

It is because of the entrepreneurs we serve that I have advocated for rules like Section 1071, which will allow our entire financial services system to fully see and better serve all of our entrepreneurs.

Entrepreneurs that need to be Seen by the Financial System

And this transparency is not just about fairness. It is also about strengthening our economy. A recent study shows that minority and women-owned small businesses employ nearly 20 million people and generate over $2 trillion in revenue.

I know this to be true, personally as the CEO of AOF, because I think about clients such as Reign Free from Oakland, who started and scaled her catering business after repeatedly being told that she did not qualify for a loan. We were her first lender to say yes.

I also think about Alicia Los Mayas from Hayward, who took the $5,000 loan we gave her, purchased a van and now she has a burgeoning tamales business nationwide.

I'm proud that we provide loans to everyone—Black, White, Latino, Asian and low-income. But I am especially proud of our investment in Black and Latina women who are starting up more businesses in this

U.S. than any other group. I am proud that AOF supports these entrepreneurs, and the businesses that they found, the local employees they train and hire, and the economic activity they generate.

1071

However, for decades, entrepreneurs like these women have not been seen by our financial system. While I am not here to defend or promote every letter of Section 1071, I recognize that this rule will accomplish three important things: it will help small business lenders, help entrepreneurs that desperately need access to capital and help policymakers that want to invest in our economy without creating new direct entitlement programs.

1. First, this rule could help the market to better address both the lack of access to affordable capital, and the rise of irresponsible lending. For the first time, everyone in financial services would be able to see which business models are successful at reaching minority-owned, women-owned and other small businesses. This transparency would attract investment capital and partnerships into models that work. We *can* have a market-based and pro-innovation approach to regulation, one that will actually *help* lenders expand customer acquisition — something that all community banks and lenders desperately want to do.

   But we need clarity on who the businesses are, who's serving them, and what capital they're getting. Because WE CANNOT MANAGE WHAT WE DO NOT MEASURE.

2. Second, as lenders the better we understand these businesses, it will help us tailor products and services to meet their needs. The more knowledge we gain about our markets, customers and their needs, the better equipped we are to building long-term

profitable relationships.

3. Finally, this rule helps spur additional investments in small businesses, which is the best way to reduce inequities without having to create new government programs. Instead, it will allow all of us to do what of our organizations have successfully done for years-- expand access to capital for underinvested entrepreneurs by leveraging existing public and private sector partnerships.

For these reasons, I am pleased to testify on how we can ensure that Section 1071 accomplishes its goals of spurring additional investment in all of our entrepreneurs.

I will conclude by saying that Access to capital for small businesses is a bipartisan priority. There are Mom and Pop stores in communities that are rural and urban; red and blue; Black and White, Hispanic, and Asian—and they are all powering our economy.

But we cannot do that without Section 1071 to shine light on these small businesses' credit applications.

Because as I said before--We cannot manage what we do not measure, and Sunlight is the best Disinfectant.

As we implement this well, we will finally be able to increase access to capital for small businesses and create a more transparent and successful financial services system.

Thank you and I look forward to your questions.







March 28, 2023

Hon. Daniel Meuser, Chairman
Subcommittee on Economic Growth, Tax, and Capital Access
House Committee on Small Business
2069 Rayburn House Office Building
Washington, DC 20515

Hon. Greg Landsman, Ranking Member
Subcommittee on Economic Growth, Tax, and Capital Access
House Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Meuser and Ranking Member Landsman,

On behalf of the Center for Responsible Lending (CRL),[1] the National Association for Latino Community Asset Builders (NALCAB),[2] and the National Coalition for Asian Pacific American Community Development (National CAPACD),[3] thank you for the opportunity to submit this letter for the record on the Subcommittee on Economic Growth's hearing entitled, "The End of Relationship Banking? Examining the CFPB's Small Business Lending Data Collection Rule." We firmly believe that the Consumer Financial Protection Bureau's (CFPB) final Section 1071 regulation will improve relationship banking by creating a robust and comprehensive data collection regime that helps ensure that small business lending is fair and accessible to entrepreneurs from all communities in the United States.

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[1] CRL is a non-profit, non-partisan research and policy organization that works to ensure a fair, inclusive financial marketplace. CRL's work focuses on those who may be marginalized or underserved by the existing financial marketplace -- people who often are targeted for unfair and abusive financial products that leave them worse off. Our affiliate, Self-Help Federal Credit Union ("Self-Help"), a Community Development Financial Institution and SBA lender, was an active Paycheck Protection Program ("PPP") lender throughout the entire program, with 65 percent of its PPP loans going to small businesses or nonprofits led by people of color. Through its Small Business Administration (SBA) lending programs and PPP advocacy, both Self-Help and CRL have had firsthand experience witnessing the barriers to entrepreneurship faced by people of color.

[2] NALCAB - The National Association for Latino Community Asset Builders is the hub of a national network of asset building community development organizations including more than 50 certified CDFIs. Members of the NALCAB Network invest in their communities by building affordable housing, addressing gentrification, supporting small business growth, and providing financial counseling on issues such as credit building and homeownership. Many of the people served by the NALCAB Network are low- to moderate-income individuals who are immigrants, or the children of immigrants.

[3] National CAPACD, The National Coalition for Asian Pacific American Community Development is a coalition of more than 100 member organizations with a mission to build a powerful coalition of Asian American, Native Hawaiian, and Pacific Islander (AANHPI) community-based organizations working with low-income populations. We utilize a comprehensive set of community development strategies from community organizing to development to advance equity and create vibrant, healthy communities. National CAPACD member organizations employ a diverse set of strategies tailored to meeting local community needs, including: the creation and acquisition of affordable housing & community institutions, assistance for renters and homeowners, services for financial capability and empowerment, community organizing, workforce development, and small business sustainability and entrepreneurship.

1. Our Nation has a Vested Interest in Ensuring that Small Business Capital is Both Fair and Accessible to Entrepreneurs from All Communities.

In addition to creating two-thirds of all net new jobs in the United States, small businesses account for 43.5 percent of the nation's gross domestic product.[4] And, next to owning a home, business equity is the second-largest source of personal wealth in the United States. Small business ownership is the backbone of America's economy and the key to maintaining a strong middle class. Ensuring that small businesses have the capital they need to grow is a matter of national importance that has previously garnered bipartisan support. However, accessing capital remains a problem for too many small business owners, with accessibility gaps driven by several factors—including the age of the business, the size of the loan, the business's location, and the race or gender of the business owner.[5]

The absence of reliable lending data has obscured the full scope of challenges small businesses face in securing the capital they need to sustain and scale their entrepreneurial efforts. Data on the availability of affordable credit based on the type and location of businesses can help policymakers and lenders develop targeted programs to address inequities in access and ensure that small businesses can obtain the capital they need to realize their full potential. The absence of data has been particularly challenging in addressing capital disparities for businesses operated by individuals from traditionally underserved communities.[6]

2. The Fastest-Growing Small Businesses in the United States, Minority-Owned Firms, are Experiencing Significant Challenges Accessing Capital from the Financial Marketplace.

The number of minority-owned small businesses continues to grow at a faster rate than their non-minority counterparts. Over a recent ten-year period, minority-owned small businesses grew by 79 percent—around 10 times faster than the average growth rate for all small businesses.[7]

Yet, research shows that entrepreneurs of color have difficulty securing the capital necessary to start and grow a business. Recent surveys by a consortium of Federal Reserve Banks consistently found significant disparities in the ability of white-owned businesses and businesses owned by people of color to obtain credit. The 2021 Federal Reserve Small Business Credit survey found that Latino-owned firms received capital at just 50 percent the rate of white-owned firms; black-owned firms obtained financing at one-third the rate of white-owned firms.[8] A 2019 report by National CAPACD, *Small Business, Big Dreams: A Survey of Economic Development Organizations and Their Small Business Clients in Low-Income Asian American and Pacific Islander Communities*, also found that many Asian American, Native Hawaiian, and Pacific Islander (AANHPI) micro-entrepreneurs experience significant challenges in securing capital from mainstream U.S. financial institutions for reasons including individual credit profiles (28% of survey respondents), difficulty in navigating the loan application process (20% of survey

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[4] What's New with Small Business – SBA's Office of Advocacy

[5] Bipartisan Policy Center, "*Small Agency, Big Mandate. A Bipartisan Road Map to Modernizing SBA*," available at https://bipartisanpolicy.org/report/modernizing-sba/.

[6] For more information on the extensive barriers to capital impeding entrepreneurship, see our organizations' 1071 comment letter, https://www.responsiblelending.org/research-publication/comment-cfpb-broad-coalition-urges-robust-data-reporting-requirements-small

[7] Emergent Research, "*Number of Minority Owned U.S. Small Businesses Growing Rapidly*," available at https://www.smallbizlabs.com/2017/10/number-of-minority-owned-us-small-businesses-growing-rapidly.html#:~:text=According%20to%20research%20from%20The,by%2079%25%20reaching%2011.1%20million

[8] Federal Reserve Banks, *Small Business Credit Survey. 2021 Report on Firms Owned by People of Color*, https://www.fedsmallbusiness.org/medialibrary/FedSmallBusiness/files/2021/sbcs-report-on-firms-owned-by-people-of-color

respondents), linguistic barriers (18%), and lack of knowledge regarding capital availability (17%).[9] AANHPI business owners have a great need for trusted resources that can provide culturally competent, one-on-one technical assistance and business counseling.

Improving capital access for minority-owned businesses will strengthen the nation's economy, create jobs, and build a robust middle class. Research by the Alliance for Entrepreneurial Equity Alliance estimates that if the number of Latino-owned businesses were proportionate to the population of the largest-growing ethnic group in the United States, there would be an additional 800,000 firms, creating 7.5 million more jobs and adding $1.2 trillion in economic activity.[10] Similarly, Citigroup estimates that fairer access to small business loans would enable African American entrepreneurs to add $13 trillion in revenue and create 6 million jobs over a twenty-year time period.[11]

We believe that a robust 1071 rule will spur entrepreneurship in communities that traditionally have lacked sufficient access to capital and lead to increased economic growth and an expanded pathway to economic prosperity for more Americans.

3. Increased Transparency in the Small Business Lending Market Will Produce Greater Institutional Accountability and Expand Access to Capital.

Section 1071 of the Dodd-Frank Act was designed to collect data "to facilitate enforcement of fair lending laws and enable communities, governmental entities, and creditors to identify business and community development needs and opportunities of women-owned, minority-owned, and small businesses."[12] In enacting the provision, the federal government correctly surmised that increased transparency would encourage lenders to demonstrate greater accountability in equitably providing capital to all communities while allowing regulators to focus their scrutiny on those market participants demonstrating bad behavior.

While some industry groups have sought to exempt a sizable share of small business lenders from 1071 data collection and reporting requirements or to weaken the rule's requirements, their argument is inconsistent with the nation's need to stimulate economic growth by improving capital access while simultaneously focusing the government's limited resources on developing narrowly tailored policy solutions that improve the market. History has shown that increased transparency in the financial markets improves lender self-accountability and leads to more accurate legislative and regulatory analysis of the problems and solutions to increasing access. A similar data collection requirement under the 1989 Home Mortgage Disclosure Act (HMDA) has confirmed that improved transparency results in expanded responsible loans for underserved communities. Shortly after implementing the HMDA requirement, conventional home mortgage lending to African Americans and Hispanics increased by 70 percent and 48 percent, respectively.[13]

4. The CFPB's Final 1071 Small Business Lending Data Collection Rule Reflects Extensive Analysis and Stakeholder Engagement.

The final small business lending data collection rule will be the result of years of research, engagement, supervisory work, and policy development by the CFPB. For example, in 2017, the CFPB convened a public field hearing on the topic, issued a Request for Information, and published a white paper on the key

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[9] National CAPACD Small Business, Big Dreams - National CAPACD
[10] Entrepreneurial-Inequity-in-America-20220426.pdf (imgix.net)
[11] minority-depository-institutions-brochure.pdf (citigroup.com)
[12] Office of the Federal Register, National Archives and Records Administration. 124 Stat. § 1071(a). https://www.govinfo.gov/content/pkg/PLAW-111publ203/pdf/PLAW-111publ203.pdf
[13] Fact Sheet on Section 1071 Small Business Loan Data » NCRC

dimensions of the small business lending landscape. The CFPB also continued to engage stakeholders on the issue in 2019 by holding a symposium on small business lending. In 2020, per the Small Business Regulatory Enforcement Fairness Act, the CFPB published an outline of proposals, convened a Small Business Review Panel to gather input on proposals under consideration, and released a report summarizing the panel's input and recommendations. The CFPB also solicited feedback from the general public on the outline of proposals and received nearly 60 comments before releasing its proposed rulemaking.

Because the CFPB consulted with small business advocates, business leaders, civil rights groups, and financial institutions—big and small– to create a final rule that maximizes transparency while also minimizing lenders' regulatory burden and costs, this Committee should have confidence that the final regulation fulfills Congress's intent in establishing Section 1071. The undersigned organizations urge committee members to recognize that, despite some initial investments and ongoing costs required of financial institutions, Section 1071's benefits to the small business lending marketplace and our nation's economy outweigh its costs.

Conclusion

Policymakers and lenders need comprehensive small business lending data to develop targeted programs to address inequities in access and ensure that small businesses can obtain the capital support they need to realize their full economic potential. Given the significant benefits of small business lending data collection, it is essential that the members of this committee and all stakeholders allow the CFPB's final 1071 rulemaking to proceed without any additional delay.

Sincerely,

The Center for Responsible Lending

National Association for Latino Community Asset Builders (NALCAB)

National Coalition for Asian Pacific American Community Development (National CAPACD)

Contacts: *Sunny Glottmann, Researcher, CRL, Sunny.Glottmann@responsiblelending.org*

David Ferreira, Government Relations, CRL, David.Ferreira@responsiblelending.org

Anju Chopra, Director of Policy, National CAPACD, Anju@nationalcapacd.org

Clarinda Landeros, Director of Public Policy, NALCAB, CLanderos@nalcab.org

March 25, 2023

House Subcommittee on Rural Development,
Energy, and Supply Chain
Chairman Wesley Hunt
1520 Longworth House Office Building
Washington, DC 20515

Dear Mr. Chairman,

My name is David Bleakley and I am the Executive Vice President at Colt Energy, Inc. an oil and gas exploration and production company operating in Eastern Kansas for over 70 years. I am writing this letter regarding the Quantification of Methane Emissions from Marginal (Low Production Rate) Oil and Natural Gas Wells study directed by the Department of Energy and performed by GSI Environmental out of Austin, Texas. This is the link to the final report from the DOE Quantification of Methane Emissions from Marginal (Low Production Rate) Oil and Natural Gas Wells (Technical Report) | OSTI.GOV . I personally witnessed GSI performing their Methane Emissions tests on our companies' marginal wells, at the wellhead (the actual point of production), separators (where oil, gas and water are separated), and tanks (where oil, natural gas liquids and water are stored) looking for methane leaks. Upon testing our wells GSI had to check to make sure their equipment was working properly because they tested so little or no methane leaking from our wells, separators and tanks. After checking their testing equipment, they did find that their testing equipment **was** working properly. Our wells were not the exception to this study, but more the norm for 90% of the marginal oil and gas wells GSI tested across the country in this study. I know several environmental groups have claimed these marginal (Low Production Rate) Oil and Natural Gas Wells are Super Emitters of methane gas, but this DOE independent study proves that is not the case. I hope that before the EPA issues these regulations on Methane Gas Emissions on Marginal (Low Production Rate) Oil and Gas Wells this DOE study is seriously reconsidered as the factual third-party study that it is. These marginal oil and gas wells because of the DOE study should be exempt from these EPA regulations. Thank you for your time.

Sincerely,

David P. Bleakley
Executive Vice President
Colt Energy, Inc.

Corporate Office
P.O. Box 388 - 1112 Rhode Island Rd.
Iola, Kansas 66749-0388
Phone (620) 365-3111 Fax (620) 365-3170

Kansas City Office
6299 Nall Ave., Suite 100
Mission, Kansas 66202-3547
Phone (913) 236-0016 Fax (913) 262-0058

CBA | CONSUMER BANKERS ASSOCIATION

March 24, 2023

The Honorable Dan Meuser
Chairman
Subcommittee on Economic Growth, Tax, and Capital Access
House Committee on Small Business
2361 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Greg Landsman
Ranking Member
Subcommittee on Economic Growth, Tax, and Capital Access
House Committee on Small Business
2069 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Meuser and Ranking Member Landsman:

The Consumer Bankers Association (CBA) is pleased to submit this letter for the hearing entitled "The End of Relationship Banking? Examining the CFPB's "Small Business Lending Data Collection" Rule" focused on the Consumer Financial Protection Bureau's ("CFPB" or "Bureau") notice of proposed rulemaking for Small Business Lending Data Collection under the Equal Credit Opportunity Act ("proposal"),[1] concerning the small business lending market pursuant to Section 1071 of the Dodd-Frank Act. CBA is the voice of the retail banking industry whose products and services provide access to credit to millions of consumers and small businesses. Our members operate in all 50 states, serve more than 150 million Americans, and collectively hold two-thirds of the country's total depository assets.

CBA and its member institutions understand that Section 1071 was mandated by Congress; however, this rule **is not as simple as data collection efforts undertaken on other lending products such as residential mortgages. Business loans are often complex and involve multiple owners who can be businesses themselves, not individual consumers which is an easier data point to capture**. Business lending materially differs from residential mortgage lending and the use of Home Mortgage Disclosure Act ("HMDA")-like reporting for business lending activity may not identify potential discrimination as Congress intended because of these important distinctions.[2]

[1] 86 FR 56356 (October 8, 2021).
[2] Examples include: (1) Residential lending shares the same type of collateral. Business lending may not be secured at all, and when secured, the type of collateral varies tremendously; (2) residential lending has (with rare exceptions) consumers as the applicants, whereas business lending involves loans to all sorts of applicants, ranging from sole proprietors to sophisticated corporate structures; (3) business loans are often renewals rather than new loans and are not akin to refinances in the residential world; (4) business loans have much shorter and varied durations; (5) the appropriate property address for a business loan to use for reporting and analysis can be debated with no easy or right answer; (6) capturing business loan applicants for reporting and analysis can be debated with no easy or right answer given the various ownership and structures; (7) residential mortgage transactions often do not result in ongoing relationships and are much more transactional; (8) residential lending generally involves creditor interactions with only the future homeowners, whereas in business lending, creditor interactions could be with a number of business representatives which may or may not include the principal owners; (9) residential mortgage applications seldom include more than two primary applicants whereas commercial credit applications may involve many equal part business owners; and (10) residential mortgage applicants customarily apply on their own behalf whereas commercial credit applicants may involve an authorized representative with no ownership interest in the business.

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We believe the dissimilar nature of business lending presents increased challenges and, therefore, increased risk of misleading data. Constructing fair lending analysis that will yield meaningful and appropriate conclusions for business lending is likely even more challenging.

CBA and its member institutions cannot stress enough the importance of well-balanced rules under Section 1071 to avoid overly burdensome data collection requirements that could stifle small business lending, greatly increase compliance costs for small business lenders, and open the door to costly litigation. Key to this rulemaking will be the Bureau's allowance for adequate compliance lead time for lenders to develop data collection platforms that will capture and report 1071 data accurately.

CBA values the Bureau's proposed adoption of many provisions that will make the 1071 data collection more efficient and meaningful. These positive steps include the CFPB's inclusion of a simplified small business definition, limiting data collection to women- and minority-owned small business, and the general ability for lenders to rely on borrowers' representations. We believe these changes will help lenders better collect small business data.

Compliance Lead Time

Under the proposal, a final rule implementing Section 1071 would be effective 90 days after publication in the Federal Register, with compliance mandated eighteen months after publication.

Given the complexities and the many other challenges presented by the Bureau in the proposal, it is difficult to say exactly how much lead time lenders will need to implement the regulations without knowing the specific requirements for implementation, which, of course, will only be known when the regulations are final. Due to the highly complex nature of the proposed amendments and the implications of not getting the collection of 1071 data right, the proposed eighteen-month compliance timeline will not allow lenders to properly implement any final 1071 rule. It is vitally important for lenders to have a reasonable amount of time to implement the new requirements. Providing adequate implementation time will allow financial institutions the opportunity to make the changes necessary to achieve the statutory purpose and Bureau's goals for 1071 data collection and reporting. Without the time to properly implement for Section 1071, lenders may be forced to pause small business lending, which could have significant negative impacts on the most vulnerable business the rule is intended to benefit. Accordingly, **we believe an implementation period of no less than thirty-six months would afford adequate time for lenders to properly stand up 1071 requirements.**

Covered Borrowers– Definition of Small Business

The proposal would require financial institutions to collect and report Section 1071 data regarding all "covered applications" from "small businesses." Small business would be defined by reference to the Fair Lending and Small Businesses September 10, 2021 definitions of "business concern" and "small business concern" in the Small Business Act[3] and the implementing regulations of the Small Business Administration ("SBA"),[4] which is consistent

[3] 15 U.S.C. 631 et seq.
[4] 86 FR 56356 at 789.

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with the approach specified in Section 1071.[5] The CFPB would not, however, employ the SBA's size standards for defining a small business concern, which vary based on a business's six-digit North American Industry Classification System ("NAICS") code. Instead, the CFPB would look to whether the business—regardless of NAICS code—had $5 million or less in gross annual revenue for its preceding fiscal year.[6] Any business that is at or under the $5 million threshold would be a "small business" for purposes of the proposed rule. CBA strongly agrees with the Bureau's application of a revenue-based approach to the definition of a small business. However, **we believe a $5 million gross annual revenue threshold is too high, would capture much larger businesses that should not be covered by the rule, and would obscure the intent of Section 1071 – the collection and analysis of data on the nation's truly small businesses.**

As acknowledged in the proposal, most of the small entity representatives convened for the 1071 SBREFA analysis commented that most of their small business customers were under $1 million in annual revenue.[7] We believe this is true and companies that fall above a $1 million threshold often offer different structures, are more sophisticated, and data collection would bleed into separate commercial banking operations with different systems, processes, and platforms, increasing the cost of collection, while offering little insight into actual small business lending.

Data analyses from some of our member banks also supports this notion. One such analysis found businesses with $1 million to $5 million in revenue much more closely resembled large businesses than those with $1 million or less. These institutions are much less likely to be a sole proprietorship, have five or more employees, and have multiple authorized officers who can act on the business' behalf. Additional member observations include:

- 39% of businesses with revenue under $1 million are reported as sole proprietorships as compared to 16% with revenue from $1 million to $5 million and 10% for those with revenue over $10 million.
- 54% of businesses with revenue under $1 million have employees counts less than or equal to 5 as compared to 34% for those with revenue from $1 million to $5 million and 21% for those with revenue over $10 million.
- 34% of businesses with revenue under $1 million have only one authorized officer on file as compared to 22% for those with revenue from $1 million-$5 million and 12% for those with revenue over $10 million.

Setting a revenue threshold at $5 million or less would also add complexity and unnecessary costs to institutions that currently lend to a broad range of business revenues. In moving from $1 million to $5 million, lenders start to get into commercial lending and often run into more complex ownership scenarios which becomes more cumbersome.

Data Collection and Reporting

[5] *See* 15 U.S.C. 1691c-2(h)(2).
[6] 86 FR 56356 at 789 - The Bureau is seeking SBA approval for this alternate small business size standard as required under the Small Business Act.
[7] 86 FR 56356 at 56429.

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Under the proposal, covered financial institutions would be required to collect and report three categories of data: (1) data generated primarily from specific requests by the institution; (2) data that may be provided by the applicant or discerned from information provided by the applicant or a third party; and (3) data that the institution itself generates. These three categories are made up of a total of twenty-one data points in the proposal.[8] Covered financial institutions would be permitted to rely on statements made by an applicant or information provided by an applicant when collecting and reporting data, but, where verification is permitted and the financial institution chooses to do so, a financial institution may be required to report verified information.[9] Covered financial institutions would be required to collect data on a calendar-year basis and report that data, along with certain identifying information about the institution, to the CFPB by June 1 of the following year.[10] Covered financial institutions would be permitted to reuse certain data points if the data were collected within the same calendar year as the current covered application and the institution has no reason to believe the data are inaccurate.[11]

CBA strongly supports the provisions in the proposal that limit the obligation of lenders to make any of their own determinations or observations concerning whether applicants are Covered Entities, the ability for lenders to rely on the accuracy of the response of applicants' representatives, and the affirmation that lenders do not need to continually ask if applicants are not responsive.[12] However, as proposed, in the case of race and ethnicity (but not gender) of an applicant's principal owners, the Bureau proposes for the information to be collected on the basis of observation. More specifically, if an applicant does not provide at least one principal owner's ethnicity, race, or sex information and the financial institution meets with any principal owners in person or by video, the financial institution would be required to collect such information via visual observation or surname.[13]

Data Points

Section 1071(e)(1) requires each financial institution to compile and maintain a record of certain information provided by any credit applicant pursuant to a request under Section 1071(b), and report that information to the Bureau. The Bureau refers to this information, along with the applicant's responses to the inquiries under 1071(b)(1), as "mandatory data points," which include: (1) whether the applicant is a women-owned, minority-owned, and/or small business, (2) application/ loan number, (3) application date, (4) loan/ credit type, (5) loan/ credit purpose, (6) credit amount/limit applied for, (7) credit amount/ limit approved, (8) type of action taken, (9) action taken date, (10) census tract (principal place of business), (11) gross annual revenue, and (12) race, sex, and ethnicity of the applicant's principal owners.

The Bureau has also proposed additional discretionary data points to be collect on top of the above-enumerated mandatory data fields. These include, among others, the collection of data points relating to pricing and NAICS code. CBA has always maintained that the 1071 data

[8] 86 FR 56356 at 56551.
[9] *Id*
[10] *Id.*
[11] *Id* at 56578.
[12] Id. At 56468- Under the proposal, minority-owned business status or women-owned business status could only be collected and reported on the basis of information provided by the applicant for purposes of Section 1071.[12] Financial institutions would not be permitted to collect or report such data based on any other basis (e.g., observation).
[13] *Id* at 56358.

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collection process will need to be as streamlined as possible in order to produce useful data. As noted above, the process for small business data collection will not be as simple as the process under HMDA for home mortgages and any unnecessary data points will only serve to add distortion to the data mandated under Section 1071. Accordingly, CBA believes the mandatory data points sufficiently capture the information sought under Section 1071 and urges the Bureau to reconsider any additional data points that would be unnecessary and would create more constraints on borrowers and lenders alike.

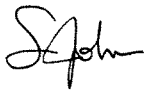
Publication of Data and Limitations on Access

Under the proposal, application-level data submitted by financial institutions would be made publicly available on an annual basis on the CFPB's website, subject to modifications by the CFPB to advance privacy interests.[14] In exercising its discretion to modify the data, the CFPB proposes to employ a "balancing test" that assesses the risks and benefits of public disclosure.[15] The CFPB also proposes to issue a policy statement regarding its intended data modifications after receiving at least one full year of Section 1071 data.[16]

The Bureau's intention to decide what data will be limited or private after the first year of raw data has been provided, and via "Balancing Test Policy Statement" rather than the rulemaking process, is misplaced. The risk of re-identification is higher for small businesses and the Bureau should not make privacy decisions via a policy statement, as it initially did for the 2015 HMDA data. It is critical that the Bureau undertake a notice-and-comment rulemaking to decide the privacy protections for Section 1071. Furthermore, we urge the Bureau to provide the initial privacy standards within the final rule, then adjust (via notice-and-comment rulemaking) after the initial year of data has been received.

Our members are concerned the impact this rule will have on the availability of small business loans, especially for our small member institutions and the threat the release of data could present for litigation. We appreciate Congress taking a closer look at the 1071 rule and the impact this could have on main street businesses that have a close working relationship and rely on access to credit options provided by our member institutions. CBA greatly appreciates the opportunity to share our suggestions and to work with policymakers on considerations regarding Section 1071.

Sincerely,



Lindsey D. Johnson
President and CEO
Consumer Bankers Association

[14] 86 FR 56356 at 56512.
[15] *Id.* at 56358.
[16] *Id*

1225 New York Avenue, NW, Suite 1100, Washington, DC 20005
consumerbankers.com

January 6, 2022

Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Via Electronic Submission

Re: Docket No. CFPB–2021–0015 or RIN 3170–AA09, Small Business Lending Data Collection Under the Equal Credit Opportunity Act (Regulation B)

Dear Director Chopra:

The American Bankers Association[1] and 51 state bankers associations, (the Associations) appreciate the opportunity to comment on the Consumer Financial Protection Bureau's notice of proposed rulemaking to implement section 1071 of the Dodd Frank Wall Street Reform and Consumer Protection Act (the proposal).[2] Section 1071 amends the Equal Credit Opportunity Act (ECOA) to require financial institutions to collect and report to the Bureau certain data regarding applications for credit made by small businesses, including women-owned businesses and minority-owned businesses.

Summary of the Comment

The Associations support the goals of section 1071, which are to facilitate enforcement of fair lending laws and to help regulators and the public identify opportunities for community development. Our members oppose discrimination in any form, and support enforcement of fair lending laws. Likewise, banks support community development by investing in the neighborhoods they serve, for the improvement of those communities, the businesses that operate there, and the families who live and work there.

However, unless the Bureau revises the proposed rule, it will impose significant costs on banks – costs that will be felt most acutely by community banks – that will negatively affect their small business customers. The proposed rule's scope is unnecessarily far reaching; it would exempt very few community banks, define small businesses so broadly as to include tens of thousands of large businesses, and require institutions to collect and report data on numerous data points in addition to the Congressionally required data points. All of these actions combine to negatively impact community banks and their customers, in stark contrast to Director Chopra's assertions of support for community banks and relationship banking.[3]

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[1] The American Bankers Association is the voice of the nation's $23.3 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $19.2 trillion in deposits and extend $11 trillion in loans.
[2] 86 Fed. Reg. 56,356 (Oct. 8, 2021).
[3] Press Release, Consumer Fin. Prot. Bureau, Opening Statement of Director Rohit Chopra Before the House Committee on Financial Services, https://www.consumerfinance.gov/about-us/newsroom/opening-statement-director-rohit-chopra-before-house-committee-financial-services/ (Oct. 2021).

The proposal includes a lengthy, yet largely conjectural, analysis of the costs and benefits of the proposed data collection regime. The Bureau estimates that the one-time costs of implementing the regulation would be between $312 million and $323 million for depository and non-depository institutions, and it estimates ongoing *annual* costs of between $372 million and $392 million, respectively. The Bureau contrasts these costs with the net income per origination and per application, for small business loans, without explaining how it calculated net income. Unsurprisingly, the Bureau concludes that these cost estimates, which experience demonstrates likely understate actual costs, do not outweigh the benefits to fair lending enforcement.

The Associations and others have repeatedly expressed concern about the costs of the rule, to little or no avail. Small Entity Representatives (SERs) and other stakeholders told the Bureau its cost estimates for the outline of proposals considered during the Small Business Regulatory Enforcement Fairness Act (SBREFA) review were too low, and yet it has made no changes in response. Instead, the proposal recites feedback received during the SBREFA process indicating that its estimations of certain costs are too low. Similarly, the proposal recites comments on the Bureau's 2017 Request for Information that raised concerns about the cost of implementing 1071. Disappointingly, the proposal simply seeks additional comment without explaining why the comments on costs have been ignored.

The proposal fails to consider the cost of duplicative and burdensome data collection and reporting. For example, covered banks that meet data reporting thresholds for HMDA and CRA will be collecting and reporting data on a single application or loan for all three data reporting obligations, but not in the same way. In addition, the Bureau's cost estimates do not factor in the additional annual costs for fair lending compliance. The 1071 data will offer increased opportunities for examiners to rely on statistical analysis to assert discrimination in small business lending. To be prepared to respond to anticipated disparate impact claims, banks will need to devote considerable additional resources to expanded fair lending compliance programs.

The increased costs associated with the 1071 rule will reduce competition in the small business credit market, despite the Director's statements about the importance of competition in financial services.[4] Over time, the 1071 rule will drive further consolidation, and the gradual loss of community banks. Reduced competition will lead to fewer choices and higher prices for small businesses. Non-banks will absorb some of the small business lending done today by banks, but they will not be able to offer their customers the benefits of a banking relationship and the technical assistance banks provide to their small business customers.

While understating the costs of the rule, the proposal also overstates the rule's benefits for fair lending. Experience with PPP shows that most small business applicants will decline to provide demographic information or leave questionnaires blank· therefore, the data on race and ethnicity of business owners will be flawed. Records with missing demographic data will either be excluded from fair lending analyses, or data users will have to use proxies for race and ethnicity

[4] Press Release, Consumer Fin. Prot. Bureau, Statement of CFPB Director Rohit Chopra Member, FDIC Board of Directors December Open Meeting of the Board, https://www.consumerfinance.gov/about-us/newsroom/statement-of-cfpb-director-rohit-chopra-member-fdic-board-of-directors-december-open-meeting-of-the-board/ (Dec. 2021).

to try to identify fair lending issues. These problems call into question the benefit of the data collection, and whether the costs are justified by the benefits.

The Bureau seeks to address the prospect of missing demographic information by requiring lenders to identify business owners' race and ethnicity by visual observation or surname when the applicant declines to provide the information. This practice is antithetical to section 1071, which clearly expresses Congress' intent for an applicant to have the right to choose whether to provide any of the information requested.[5] It will also yield wildly inaccurate data on race and ethnicity. Nevertheless, regulators, advocates, and investigative reporters will rely on it to target lenders for fair lending concerns.

Small businesses will also see their privacy significantly eroded once the Bureau releases the 1071 data to the public. Under the proposed rule, application-level data submitted by financial institutions will be publicly available on the Bureau's website, subject to modification by the Bureau to protect privacy. There is little question that data users will be able re-identify small businesses with just *two* of the proposed data points—census tract and NAICS code. Publication of other data points may disclose sensitive personal financial information or confidential business information about an applicant. This will undermine small business owners' privacy, increase fraud, and encourage the aggregation, sale, and use of information without small businesses having any ability to control the use of their information.

Although the Bureau proposes to study re-identification risk and to employ a "balancing test" to assess the risks and benefits of public disclosure, it does not plan to allow the public to comment on the study or the decisions the Bureau makes on redaction or modification. The Associations strongly recommend that the Bureau reconsider this plan, and urge the agency to initiate an Administrative Procedure Act (APA) compliant rulemaking to determine which data can be publically released without sacrificing small business owners' privacy.

We summarize here our comments on specific provisions of the proposed rule:

- **The Associations support an activity-based exemption from the 1071 rule for community banks; however, the rule should exempt financial institutions with 500 or fewer small business loan originations in each of the two preceding calendar years.** The proposed 25-loan threshold for coverage is much too low and would force many community banks to raise prices, set minimum loan amounts, or even exit banking entirely to avoid the costs of the 1071 rule.

- **The Associations support a simple and clear definition of a small business as one that has $1 million or less in gross annual revenue.** The proposed revenue cap of $5 million will cover larger businesses; the final rule should define a small business as one with $1 million or less in gross annual revenue in the preceding fiscal year.

[5] 15 U.S.C. § 1691c-2(c) (2018) ("Any applicant for credit may refuse to provide any information requested pursuant to subsection (b) in connection with any application for credit.").

- **The proposed definition of an application, which triggers data collection and reporting for covered institutions, should be retained in the final rule.** It provides the flexibility needed for a rule that will cover different products, from term loans, lines of credit, and real estate secured transactions.

- **The proposed definition of a covered credit transaction is generally appropriate and we support the inclusion of merchant cash advances**. However, we urge the Bureau to cover trade credit, as excluding it adds to the unlevel playing field between providers of trade credit and banks.

- **The Bureau must address the duplication between 1071 and HMDA by removing all business purpose transactions from HMDA.**

- **The Bureau must work proactively with the banking agencies to eliminate duplicative and inconsistent requirements in 1071 and the CRA data.**

- **The Associations support the proposal to define a "minority individual," for purposes of determining minority-owned status, using only aggregate ethnicity and race categories.** Doing so will help avoid burdening applicants with lengthy lists of subcategories, which would likely be overwhelming and confusing.

- **The final rule should retain the proposed definition of a "principal owner" based on the Customer Due Diligence rules.** Financial institutions are already familiar with this concept in the CDD rules.

- **The Associations oppose the requirement to collect and report the discretionary data points.** The statutorily mandated data points will fulfill the statutory purposes without the need for the discretionary data points. The eight discretionary data points unduly increase the burden on reporting financial institutions and create more opportunities for errors, even with reasonably adapted procedures to avoid errors.

- **The Bureau lacks evidence to add pricing information to the data points.** In addition to compliance burden, the pricing data will be used to draw erroneous conclusions about fair lending, causing needless reputational risk. Over time, banks are likely to employ less flexibility to qualify small businesses, resulting in less credit availability.

- **The final rule should not require collection and reporting of NAICS Codes.** Most small businesses do not know their NAICS Codes; thus, the data are likely to be very inaccurate. Moreover, NAICS Codes, combined with census tract, will make it easy to re-identify a small business.

- **The Associations support the proposal to rely on an applicant's statement that the business is minority- and/or women-owned.** ABA also supports the proposal's definition of a minority individual using only aggregate race and ethnicity categories.

- **The Associations oppose collecting race and ethnicity by visual observation or surname.** This requirement is contrary to voluntary data provision, and will lead to inaccurate data, which will lead to erroneous claims of discrimination.

- **The Associations support the proposal not to require collection of the sex of the principal owners by visual observation or surname.**

- **While the Associations support the proposal to allow institutions to rely on applicants' statements for many data points, we oppose the requirement to report verified information if the institution verifies the applicant's statement.**

- **The firewall requirement is unworkable and will impose needless burden on institutions.** The Bureau should provide more flexibility in the use of the exception, where a firewall is infeasible. However, even the exception will cause disruption and put some banks at a competitive disadvantage.

- **The Bureau should exempt financial institutions from the requirement to maintain demographic data separately from other application materials**. The requirement will only frustrate the purposes of 1071 by making it harder to do fair lending analyses and audits for compliance with 1071.

- **The Associations support the proposed bona fide errors provision and the safe harbors; however, the proposed error tolerances are too low and must be revised.**

- **Institutions need three years to implement a rule of the magnitude of section 1071.** The propsed18-month period is inadequate and will result in inaccurate data in the early years of collection.

Comments

I. Definitions

A. Definition of a covered financial institution – §§ 1002.102(h) and 1002.105(b)

The proposed rule defines a covered financial institution as one that originated at least 25 covered transactions in each of the two preceding calendar years. The Bureau is proposing an exemption because although it believes it must collect data from all types and sizes of financial institutions, it is concerned that institutions with the lowest volumes of small business lending

might reduce or cease their activity because of "fixed costs of coming in to compliance" with the rule. This would "be contrary to the community development purpose" of 1071.[6]

1. The Associations support an activity-based exemption.

The Bureau believes that an activity-based exemption would provide a simple basis for institutions to know whether 1071 applies to them. Comments on the Bureau's SBREFA outline supported using only originations, and not dollar volume or other metrics in combination with originations.[7]

The Associations agree that an activity-based exemption (without an alternative asset-based exemption) is relatively simple for low-volume lenders to apply. However, the exemption will impose some burden, as most institutions do not track the gross annual revenue of their small business customers.

The Associations also support the Bureau's decision not to base the exemption on applications, and we support a two-year look back period.

2. The proposal lacks empirical support for a 25-loan threshold for coverage.

The Associations appreciate the challenge of establishing an appropriate and defensible threshold for coverage. However, the Bureau has had more than five years to develop data to support its proposed 25-loan threshold, and has not done so. Instead, the Bureau relied on FFIEC Call Reports and the Credit Union reports, which provide data on outstanding loan balances, not originations, to "impute the missing data" on loan originations. The Bureau presents its method for deriving these estimates in its Supplemental Estimation Methodologies published with the proposal.[8] Despite statements by Director Chopra expressing interest in feedback from community banks on the proposal, understanding the "missing data" methodology requires sophisticated understanding of statistical analysis that is accessible only to PhD statisticians and economists.[9]

The Bureau further obfuscates the data it relies on to evaluate the activity-based thresholds under consideration. Rather than publishing the "imputed" data on the number of originations, the preamble presents only a table showing the percentage of loans and depositories covered by triggers of 25, 50 and 100 loans. As for non-depositories, the Bureau states "it has no information for non-depository institutions such that the Bureau could provide similar estimates for comment."[10] Yet, in the Regulatory Flexibility Analysis (RFA), the Bureau is somehow able to

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[6] 86 Fed. Reg at 56418-19.
[7] Consumer Fin. Prot. Bureau, *Final Report of the Small Business Review Panel on the CFPB's Proposals Under Consideration for the Small Business Lending Data Collection Rulemaking*, at 5642 (Dec. 2020), https://files.consumerfinance.gov/f/documents/cfpb_1071-sbrefa-report.pdf.
[8] Consumer Fin. Prot. Bureau, Supplemental Estimation Methodology for Institutional Coverage and Market-Level Cost Estimates in the Small Business Lending Data Collection Notice of Proposed Rulemaking (Sept. 2021), https://files.consumerfinance.gov/f/documents/cfpb_section-1071-nprm-supplemental-estimation-methodologies_report_2021-09.pdf.
[9] *CFPB Director Concerned About Reg Burden for Small Banks,* ABA BANKING J. (Oct. 28, 2021), https://bankingjournal.aba.com/2021/10/cfpb-director-concerned-about-reg-burden-for-small-banks/.
[10] 86 Fed. Reg at 56,422.

estimate the number of non-depository lenders that would be covered by the proposal, separately showing the number of small non-depository lenders that would be covered.[11]

The proposal's mix of percentages, numbers, and complex formulae for imputing originations from Call Report data make it impossible to comment on the Bureau's assessment that a 25-loan trigger is necessary to achieve the statutory goals. We understand that the FFIEC does not have data on non-depository activity; however, the Bureau has had several years to gather such data from other sources and has, apparently, made no effort to do so beyond asking the public for data.

3. The proposal lacks a compelling rationale for a 25-loan threshold.

Not only has the Bureau failed to provide data supporting the proposed threshold for coverage, the proposal lacks a compelling rationale for a 25-loan trigger. The preamble does not explain why a 25-loan trigger is necessary and appropriate to fulfill 1071's purposes, which are to facilitate fair lending enforcement and community development. We do not endorse the 100-loan trigger; however, that trigger would cover 90% of small business lending by depositories, which is surely more than adequate for 1071's purposes.

The Bureau asserts that to fulfill 1071's purposes, it must collect data "from all sizes and types of financial institutions" other than those with low lending volume, "particularly given the variety of entities identified in ECOA section 704B(h)(1)."[12] In addition, the Bureau states that "several SERs" and "many comments" on the SBREFA outline supported a 25-loan threshold. The Bureau indicates that it has rejected, "to this point," the views of many other SERs and stakeholders who supported triggers of 100 loans or more, because it is not convinced that higher triggers are "more necessary or appropriate to carry out the purposes of section 1071."[13]

The Bureau appears to believe that institutions making fewer than 25 loans might reduce access to credit if covered by the rule, frustrating the community development purpose. We agree that a lender making so few small business loans would cease making loans available, given the costs of 1071. But we strongly believe that an institution making 50 or 100 loans would also exit the business or raise prices, given the costs and burdens of 1071 compliance.

As for the Bureau's reliance on ECOA section 704B(h)(1) in stating that the rule must cover institutions of all types and sizes, the Bureau has not explained why it supports a 25-loan trigger. On its face, section 704B(h)(1) merely defines a "financial institution" as any type of organization – partnership, corporation, association, trust or other entity – engaged in financial activity. The most that can be said about section 704B(h)(1) is that the rule should cover all types of *organizations*; it does not address the organizations' activity levels, size or even the charter type of organizations covered.

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[11] *Id.* at 56,569; tbl. 17.
[12] *Id.* at 56,420.
[13] *Id*

4. The estimates of "institutions subject to reporting" lack critical information on non-depository small business lenders.

Even if ECOA section 704B(h)(1) requires coverage of different sizes and types of institutions, the section-by-section discussion of covered financial institution does not explain how the 25-loan threshold covers all sizes and types of institutions. Instead, the section-by-section discussion shows that a 25-loan trigger covers 40% of one type of institution—depositories—and 98% of their small business originations.

If the Bureau believes the rule must cover institutions of all sizes and types, it has an obligation to estimate coverage across different types and then clearly share that information with commenters in the section-by-section discussion of the definition of a "covered institution," so that they have a meaningful opportunity to comment. However, there is no such information in the section-by-section discussion of the definition of a covered institution. Instead, the Bureau presents some information in the Regulatory Flexibility (RFA) analysis, where it shows the numbers of different institutions that the proposal would cover, including how many of those institutions are "small" under SBA's size standards. However, it is not clear how the Bureau estimated coverage of non-depositories for purposes of the RFA, given that it stated that it does not have data on non-depositories' activity level.

The lack of information on non-depositories in the section-by-section discussion skews the Bureau's estimates of "institutions subject to reporting" at each of the thresholds. This omission makes it *appear* that less than 50% of small business lenders will be covered at even the proposed 25-loan threshold. In reality, 51% of small business owners have applied for credit from a non-depository institution, according to a Federal Reserve survey.[14] If the non-depository data is included, the table would show that even at the highest threshold for reporting considered by the Bureau, the percent of lenders subject to reporting will be more than sufficient to meet the statutory purposes of section 1071.

5. The final rule should exempt banks making fewer than 500 covered loans in each of the two preceding calendar years.

Based on ABA's survey of its members and analysis of Call Report data, the final rule should exempt institutions with fewer than 500 covered originations in each of the two preceding calendar years.[15] Such a threshold would achieve the Bureau's stated objective, to collect data from institutions of different sizes and types, without conflicting with section 1071's community development purpose.

We estimate that a 500-loan threshold would result in coverage of 70%, by dollars, of banks' small business lending. That coverage would be in addition to the covered lending of credit

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[14] *See* The Federal Reserve Banks of Atlanta, et al., The Federal Reserve's Small Business Credit Survey 2021 Report on Employer Firms (2021), https://www.fedsmallbusiness.org/medialibrary/FedSmallBusiness/files/2021/2021-sbcs-employer-firms-report.

[15] ABA conducted a survey of members November 11, 2021, to December 2, 2021, which resulted in responses by 479 banks and savings associations across 40 states. The respondents ranged from banks with assets of less than $500 million to more than $75 billion.

unions, fintechs, commercial finance companies and other non-bank lenders. Covering 70% of bank lending to small businesses would yield a large and robust data set for regulators and the public to use to fulfill section 1071's purposes.

At the same time, a 500-loan threshold would not subject small community banks to the costs and burdens of the section 1071 rule. These banks have fewer loan originations over which to costs of compliance than larger institutions.

6. The Bureau has underestimated the costs of compliance for community banks.

Although Small Entity Representatives (SERs) and others told the Bureau its cost estimates are too low, it has made no changes in response. Instead, the proposal simply recites feedback received during the SBREFA review process indicating that its estimations of certain costs are too low—for example, estimated costs for training, salary estimates for employees too junior for the tasks involved, and costs of transcribing data.[16] However, the Bureau has made no changes to its analysis in response to these concerns and does not explain why it has not done so.

In addition, commenters on the Bureau's 2017 Request for Information stated that lenders would bear costs associated with litigation and reputational harm from "false positive" analyses asserting that lenders have engaged in discrimination.[17] Again, the Bureau simply recites these concerns and "seeks comment on the extent of the possible costs of litigation or reputational harm."[18] ABA also predicted that banks will need to devote additional resources to fair lending compliance programs. However, the Bureau's cost estimates do not appear to factor in this cost.

The Bureau asserts that community banks will not exit the market based on its one-time cost survey. But the Bureau has not made the survey data available to the public for comment, making it hard to evaluate the Bureau's assertions about the impact of the data reporting regime on the cost and availability of small business credit.

In our conversations with members, we found that many are reluctant to say that they will exit the market altogether. We attribute this to the existential threat such an exit poses to the vast majority of community banks. Our survey found that for community banks, on average small business lending makes up 45% of their total lending portfolio. Given the importance of small business lending to these banks, a bank that stops originating small business loans is likely to have to close or merge with another institution.

Most bankers are unwilling to predict they will cease to exist, at least at this time. We also believe that the compliance and fair lending officers who typically fill out surveys would not consider a complete exit from small business lending possible out of concern about the impact on their fair lending and CRA programs.

The Bureau contends that the costs for small institutions are not large comparatively. The Bureau's analysis suffers from several flaws. First, the Bureau's activity estimates for types A

[16] 86 Fed. Reg at 56,560-61.
[17] *Id.* at 56,561.
[18] *Id.* at 56,560.

and B institutions are significantly lower than the activity reported by community banks in our survey. The Bureau states that type A institutions originate 100 covered loans per year, and that type B institutions originate 200 covered loans per year. In contrast, bank survey respondents with assets under $500 million reported an average of 276 small business loan originations in 2019 by bank, which is more than double the CFPB's estimate. Similarly, bank survey respondents with assets of $500 million to $999.9 billion reported an average of 359 small business loan originations in 2019.[19]

The Bureau's underestimation of community bank activity calls into question its cost estimates, particularly the ongoing costs. The cost of ensuring that each record is accurate rises with the number of records that an institution must scrub for data integrity.

Second, the proposal's estimation of costs appears to have significant gaps. For example, although the Bureau estimates that the one-time costs for Type A and B institutions are $58,400 and $44,500, respectively, it is not clear that those totals included costs associated with hiring new FTEs.[20] In ABA's survey, 88% of respondents stated that they would have to hire more FTEs, with community banks, on average estimating they would hire 2-3 additional FTEs. Some community banks estimated they would need to hire 10 FTEs.

It is also unclear whether and how the Bureau accounted for the salary costs of *existing* FTEs in its estimate of one-time costs. The Bureau only presents the number of staff hours – presumably of existing staff – that will be required to collect and report the data, without any dollar estimates.[21] In our survey, 96% of respondents said they would have to assign new duties to existing staff. Community banks estimated that, on average, 8 to 13 employees would have to take on additional duties. These reassignments impose significant opportunity costs that the Bureau's cost estimates fail to consider.

The Bureau states that even if variable costs are passed on to small businesses in the form of higher rates or fees, "The Bureau expects this would comprise a small portion of the total cost of the average loan to the average small business applicant."[22]

We asked our survey respondents what they would do in response to the one-time and ongoing costs of the rule. They indicated that they would raise rates and fees, both in the near term and over the longer term. This contrasts with the Bureau's assertion that institutions will only pass on variable costs and only in relation to the one-time cost of compliance.

Regarding estimates of ongoing costs, the Bureau did not conduct a survey but instead relied on its estimates for the 2015 HMDA rule, with some adaptations. The proposal estimates that type A institutions would incur $ $7,386 in total annual ongoing costs, or about $74 in total cost per application processed (assuming a representative 100 applications per year). For Type B institutions, the Bureau estimates $35,476 in additional ongoing costs per year, or around $89 per application (assuming a representative 400 applications per year). For

[19] ABA's survey focused on 2019 originations, to avoid anomalous results stemming from PPP lending.
[20] 86 Fed. Reg at 56,556, tbl. 9.
[21] *Id.* at 56,556, tbls. 10, 11, and 12.
[22] *Id.* at 56,562.

Type C institutions, the estimate is $243,266 of annual ongoing costs, or $41 per application (assuming a representative 6,000 applications per year).[23]

The Bureau's estimates of ongoing costs are not even close to being accurate, based on ABA's survey. Among other things, the ongoing cost estimates suffer from the Bureau's underestimation of activity levels for community banks, as discussed above. In addition, we asked respondents to estimate their ongoing costs, using the Bureau's list of tasks in table 14.[24] 62% of the respondents to ABA's survey are HMDA reporters; therefore, they have experience with data collection and reporting. The estimates of these bankers are considerably higher than the Bureau's, as seen in the table below. For example, looking at banks with assets below $500 million, they estimate ongoing costs of $40,162 and banks with assets of $500 million to $999.9 million estimate ongoing costs of $67,089.

Estimated Average Annual Ongoing Costs Per Compliance Task (Actual Dollars)

	Less than $500M	$500M to $999.9M	$1B to $9.9B	$10B to $74.9B	$75B or more	All
Transcribing data:	6,202 (n=47)	10,395 (n=32)	16,162 (n=51)	50,469 (n=11)	28,843 (n=2)	14,414 (n=143)
Resolving reportability questions:	2,928 (n=45)	4,436 (n=32)	11,169 (n=52)	28,284 (n=13)	801 (n=2)	8,498 (n=144)
Transferring to 1071 data management software:	4,240 (n=39)	6,974 (n=38)	6,701 (n=36)	20,499 (n=10)	-	7,140 (n=113)
Geocoding data:	2,059 (n=38)	3,607 (n=27)	3,729 (n=48)	6,732 (n=14)	1,650 (n=2)	3,505 (n=129)
Standard annual edit and internal checks:	4,465 (n=44)	9,113 (n=32)	18,256 (n=49)	46,606 (n=13)	26,591 (n=2)	14,584 (n=140)
Researching questions:	2,297 (n=43)	5,011 (n=34)	3,486 (n=50)	12,532 (n=13)	1,132 (n=2)	4,286 (n=142)
Resolving question responses:	2,054 (n=43)	3,199 (n=23)	4,607 (n=34)	11,420 (n=13)	-	4,451 (n=96)
Checking post-submission edits:	1,904 (n=41)	4,760 (n=32)	3,945 (n=48)	9,897 (n=13)	298 (n=2)	4,038 (n=136)
Filing post-submission documents:	1,385 (n=40)	4,256 (n=31)	3,824 (n=47)	4,937 (n=13)	257 (n=2)	3,248 (n=133)
Small business data reporting/geocoding software:	6,396 (n=36)	7,152 (n=29)	13,908 (n=48)	62,029 (n=13)	13,885 (n=2)	15,017 (n=130)
Training:	4,812 (n=48)	7,390 (n=33)	13,687 (n=53)	30,474 (n=13)	21,631 (n=2)	11,005 (n=149)
Internal audit:	3,180 (n=37)	4,003 (n=30)	19,858 (n=46)	45,001 (n=13)	123,375 (n=2)	15,492 (n=128)
External audit:	5,134 (n=46)	3,931 (n=27)	9,156 (n=46)	14,548 (n=10)	-	7,046 (n=129)
Exam preparation:	2,585 (n=45)	3,552 (n=31)	8,788 (n=50)	26,322 (n=12)	25,183 (n=2)	7,372 (n=140)
Exam assistance:	1,056 (n=33)	1,500 (n=27)	3,115 (n=42)	18,473 (n=11)	7,239 (n=2)	3,686 (n=115)
All:	40,152 (n=53)	67,089 (n=34)	121,807 (n=54)	301,815 (n=15)	250,883 (n=2)	102,549 (n=158)

Source: ABA Survey 2021

In addition to underestimating the rule's ongoing costs, the Bureau attempts to make the costs appear even smaller by juxtaposing them with its estimates of the net income from small business lending using Call Report data.[25] We understand that the Bureau does not have net income data for covered financial institutions, but we cannot determine how the Bureau arrived

[23] *Id.* at 56,559-60.
[24] *Id.* at 56,559.
[25] *Id.* at 56,560.

at its estimates of net income; the proposal provides no explanation other than a reference to Call Reports. Moreover, the Bureau had years to seek more concrete information on net income, through surveys or other means, which it could have shared with the public. However, the Bureau did not do so, falling short of its obligation to base its cost analysis on quantitative information.

ABA did not have sufficient time within the comment period allowed, to gather comprehensive data from members on net income. However, information from one community bank with assets under $500 million indicates that the Bureau's estimates are significantly higher than actual net income earned on small business loans. For this bank, the average *gross* income on small business loans it originated in 2021 is $13,500, before subtracting any costs.[26] In contrast, the Bureau states that the average net income for small business originations is $105,000 to $119,000 for Type A banks, and $50,000 to $57,000 for Type B banks.[27]In addition, our community bank's data shows that it makes loans that generate as little gross income as $115 – these are loans that are unlikely be made after the 1071 rule takes effect, limiting credit availability to the small businesses and farms that need it most.

Based on our survey and our discussions with members, we believe the costs of the rule as proposed will be much larger than the Bureau's estimates and that they will be passed on, to the detriment of small businesses seeking credit. Even if banks decide to absorb all or some of the compliance costs, their capacity to lend to small businesses will then be constrained. Small businesses will have fewer choices, resulting in a reduction in competition. Some small businesses will turn to larger financial institutions, including those operating online. In addition, non-banks will absorb some of the small business lending done today by banks, but they will not be able to offer their customers the benefits of a banking relationship and the technical assistance banks provide to their small business customers. Both outcomes are in contrast to the Director's recent statements about the importance of competition and relationship banking.

Moreover, the fair lending benefits the Bureau cites in the proposal are likely overstated.[28] As shown in the table below, experience with PPP shows that most small businesses will not provide demographic information. Any data on race and ethnicity based on visual observation or surname will be inaccurate. And records with missing demographic data will either be excluded from fair lending analyses, or data users will have to use proxies for race and ethnicity to try to identify

[26] The data do not include PPP loans originated in 2021.
[27] 86 Fed. Reg at 56,560.
[28] *See, e.g.,* 86 Fed. Reg. 56,555: ("Data reported under the proposed rule would allow regulators to prioritize fair lending reviews of financial institutions.."). The lack of reliable demographic data will also undermine the benefits of disclosure, in the CFPB's application of the "balancing test" in determining whether to modify or withhold certain data from the public.

fair lending issues. These problems call into question the benefit of the data collection, which is troubling in light of the costs the rule would impose.

PPP Demographic Data Reported[29]			
Demographic	**2020**	**2021**	**Total**
Race	17.4%	29.5%	24.2%
Ethnicity	22.5%	33.0%	28.5%
Gender	31.8%	44.0%	38.7%

To minimize these negative impacts from the costs of the rule, we urge the Bureau to raise the activity-based exemption threshold from 25 to 500 loans. Doing so will help preserve the relationship lending Director Chopra recognizes is so important to small businesses and small farms and the communities they serve.

B. Definition of small business – § 1002.102(p)

The proposal defines a small business as one that meets the Small Business Administration's (SBA) definition, with one clarification. Such a business would only be small for purposes of the 1071 rule if, and only if, it has gross annual revenues of $5 million or less in its most recent fiscal year. The preamble states that the proposal would not apply the SBA's size standards, which rely on the NAICS codes, to define a small business.

1. The Associations support a revenue-based determination.

The Associations support a definition of a small business that is simple, objective and relatively easy to apply. Applying the SBA's size standards rules and NAICS codes would be unworkable fin the context of small business lending. We agree with the Bureau that, for the 1071 data collection, an institution must be able to determine quickly and easily whether an applicant is a small business under the rule because they must collect demographic information on covered applications that Regulation B otherwise prohibits.

We also agree with the Bureau that institutions are more likely to obtain demographic information from applicants if they request it earlier in the application process rather than later. Using the NAICS codes to identify small businesses would take much longer, delaying the collection of demographic information. Using the NAICS codes would also impose large training costs on financial institutions.

A definition based on gross annual revenue, as determined by the applicant's statement, will facilitate compliance by allowing institutions to ask for demographic information early in the process and better achieve the purposes of Section 1071.[30]

[29] Source: ABA Analysis, SBA data as of June 8, 2021.
[30] *Id.* at 56,433.

2. The Bureau should define a small business as an entity with $1 million or less in gross annual revenue.

The Associations urge the Bureau to revise the proposed definition so that the data collection covers only credit applications from small businesses. We recommend that the final rule use $1 million as the limit on the applicant's gross annual revenue, not $5 million in gross annual revenue. The Bureau justifies its proposal of $5 million, stating that it would exclude 270,000 businesses deemed small under SBA size standards (out of 7.2 million small employer firms), and cover 77,000 businesses that are not small under those standards. It appears that the 77,000 businesses are also employer firms, though the preamble is not clear on this point.

Although the Bureau considered a $1 million limit in its SBREFA outline, the proposal states that a $1 million gross annual revenue limit would exclude too many institutions deemed small under SBA's size standards—without indicating how many businesses would be excluded. However, in the SBREFA outline, the Bureau estimated that a $1 million limit would not cover 1.2 million *employer* firms deemed small by SBA, or 23 percent of all employer firms. Significantly, the outline also states that a $1 million limit would exclude *all* employer firms that are not small under SBA's size standards.

The Bureau's reliance on data on employer firms makes it seem that a $1 million limit would result in 23% of all small businesses being excluded from the definition. However, the Federal Reserve Study of Small Businesses indicates that 81% of small businesses are non-employer firms.[31] Moreover, the same study indicates that these firms are more likely to be owned by minorities and women. Yet the Bureau presents no analysis of data on non-employer firms.

The Bureau's 2017 report on small business lending noted, "[A]pproximately 95 percent of all businesses had less than $1 million in annual revenues. Roughly 97.7 percent of all minority-owned businesses and 98.3 percent of all women-owned businesses were similarly under this $1 million in annual receipts threshold."[32] A definition of "small business" that covers 97.7%, and 98.3% of all minority and women owned businesses, and 95% of all businesses, would provide an extremely robust data set for 1071 purposes.

In addition, Regulation B has long recognized that businesses with $1 million or less in gross annual revenue are more vulnerable and need more protection in the form of adverse action notices than larger businesses.[33] Creditors are permitted to provide notices to larger businesses within a reasonable time (as opposed to 30 days for smaller businesses), and need not provide reasons for denial unless the applicant requests such information in writing.

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[31] The Federal Reserve Banks of Atlanta, et al., Small Business Credit Survey: 2021 Report on Nonemployer Firms (2021), https://www.fedsmallbusiness.org/medialibrary/FedSmallBusiness/files/2021/2021-sbcs-nonemployer-firms-report.

[32] Consumer Fin. Prot. Bureau, Key Dimensions of the Small Business Lending Landscape (May 2017), https://files.consumerfinance.gov/f/documents/201705_cfpb_Key-Dimensions-Small-Business-Lending-Landscape.pdf.

[33] 12 C.F.R. § 1002.9(a)(c)(3)(i) (2021).

Collecting and reporting data from businesses with gross annual revenues of $1 million or less is also consistent with the Community Reinvestment Act (CRA). Under the current CRA rule, the large bank lending tests focuses, in part, on the bank's record of lending to businesses with gross annual revenues of $1 million or less.[34] In addition, loans to businesses may be eligible for consideration as community development loans, if, among other things, the loan finances businesses that either meet the size eligibility standards of the SBDC or SBIC programs or *have gross annual revenues of $1 million or less.*[35]

The proposed rule covering small businesses that have $1 million or less in gross annual revenue would better fulfill the purposes of 1071 and align with existing regulatory regimes.

C. Definition of a covered application – §§ 1002.102(f) and 103(a)

Proposed § 1002.102(f) defines a covered application as an oral or written request for a covered credit transaction that is made in accordance with procedures used by a financial institution for the type of credit requested. The Associations support the proposed definition, as it is consistent with the definition of an application in subpart A of Regulation B in § 1002.2(c). Covered financial institutions are familiar with subpart A's definition of an application, which triggers responsibilities for creditors, including the notice requirements in § 1002.9.

1. The Associations support giving lenders latitude to set their own application process.

We urge the Bureau to retain comment 103(a)-1, which gives an institution the latitude to establish its own application process and procedures, including designating the type and amount of information it will require. The comment is consistent with longstanding interpretation of Regulation B subpart A, and its flexibility is critical. The proposal covers a variety of small business lending products that require different information from applicants depending on the product. Institutions needs this flexibility to continue to offer their customers the products that best suit their needs.

Although the comment clearly permits an institution to determine its own procedures for applications, the section-by-section discussion may be read to suggest otherwise:

> Pursuant to ECOA section 704B(b)(1), an 'application' triggering data collection and reporting obligations occurs without regard to whether such application is received in person, by mail, by telephone, by electronic mail, or other form of electronic transmission, or any other means.[36]

We urge the Bureau to clarify that an institution is not compelled to accept applications by any means the applicant chooses. Instead, the Bureau should clarify that if an institution has procedures for application by one or more means, it must collect and report data on applications

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[34] *See, e.g., id.* § 228.22(b)(3)(ii).

[35] *See, e g , id.* § 228.12(g)(3); *see also* Interagency Questions and Answers, Q&A __.12(g)(3) – 1, 81 Fed. Reg. 48,506 (July 25, 2016).

[36] 86 Fed. Reg. at 56,398.

made through any one of those methods. This clarification is critical because some banks cannot accept applications online or by mail, and most fintechs cannot accept applications in person.

2. The Associations support the exclusion of prequalifications and inquiries from the definition of an application.

We also support proposed comment 110(a)-3, which excludes inquiries and prequalifications from the definition of an application, even if they would otherwise be deemed applications under subpart A. However, the Bureau should amend this comment to clarify that preapprovals are also not considered applications for purposes of 1071. It would also be helpful if the Bureau could provide examples of scenarios that are inquiries, prequalifications, and preapprovals in the commentary. While the section-by-section discussion contains some examples, these examples do not carry the authority of the commentary and are not included in the Code of Federal Regulations.[37]

We also support the Bureau's proposal to exclude renewals and extensions from the definition of an application. We question the value of including credit line increases, given the burden that will be placed on lenders and borrowers who expect a streamlined process. Although we appreciate the Bureau's attempt to address our concerns about line increases by permitting financial institutions to re-use certain data points, a 24-month period would be more reasonable than the 12 months the Bureau has proposed.

3. The Associations oppose coverage of overdraft lines of credit.

According to the preamble, the Bureau intends to cover overdraft lines of credit. The Associations oppose coverage of these lines, as creating even more operational and compliance burden. We believe banks will stop offering these lines of credit, disadvantaging small businesses that need short term credit to cover unexpected expenses.

4. We oppose reporting on transactions when an applicant initially seeks a covered credit product but ultimately is offered and accepts a product that is not covered.

The Associations believe data on transactions that are not covered should not be reported. It defies logic to require reporting on transactions that the Bureau has decided should not be covered. Moreover, the partial information would likely be of low utility.

[37] It is paramount that any examples or interpretations be included in the commentary, rather than left in the section-by-section discussion. The 1071 rules will be subject to interpretation by courts, and courts generally consider only material in the regulation and commentary. More importantly, ECOA section 706(e) provides a safe harbor from civil liability for any act or omission made in "good faith conformity with any official rule, regulation, or interpretation thereof by the Bureau or in conformity with any interpretation or approval by an official or employee of the Bureau . . . duly authorized by the Bureau to issue such interpretations or approvals . . . ." It is not clear that Bureau statements in a section-by-section analysis would meet the standard for safe harbor.

D. Definition of a covered credit transaction – §§ 1002.102(g) and 1002.104(a)

The Bureau proposes to require covered financial institutions report data for all applications for transactions that meet the definition of business credit unless otherwise excluded. Proposed § 1002.104(a) would define the term "covered credit transaction" as an extension of business credit that is not an excluded transaction under § 1002.104(b). Loans, lines of credit, and credit cards, and merchant cash advances (MCAs) would fall within the scope of the proposed rule.

1. There is no need to define loans, lines of credit, and credit cards.

Covered credit transactions would include loans, lines of credit, and credit cards, and the Bureau is not proposing to define such terms. We agree with the Bureau that the Rule does not need to define loans, lines of credit, and credit cards, as these products are already covered by proposed definition of "credit" in § 1002.102(i). Defining these terms would add unnecessary complexities, and these terms are already generally understood in the business lending community.

2. The Associations support inclusion of Merchant Cash Advances.

The SBREFA outline indicated that the Bureau was considering excluding MCAs. The Bureau is now proposing to cover MCAs. We support the Bureau's inclusion of MCAs as covered credit transactions under the proposed rule. We appreciate the Bureau responding to comments made in the SBREFA process, including ABA's, urging the Bureau reconsider exclusion of MCAs. The Bureau appropriately recognizes the increased use of MCAs by small businesses, as well as some problematic aspects of MCAs and the potential for abusive tactics.

The inclusion of MCAs means that the 1071 rule would cover the majority of products that small businesses use to obtain financing, in furtherance of the fair lending and the business and community development purposes of section 1071. Their inclusion would create a more level playing field across financial institutions that provide financing to small businesses as well as create a data set that better reflects demand for such financing.

In addition, we do not believe the Bureau needs to define MCAs or other sales-based financing transactions, as the proposed definition of "credit" covers these terms.

3. The Bureau must address the overlap between 1071 and HMDA, and it must commit to working closely with the banking regulators to address duplication and inconsistency between 1071 and the CRA data collection.

The Bureau proposes that business-purpose loans involving dwellings would be covered credit transactions under 1071 by adopting Regulation C's definition of dwelling and its commentary regarding investment property. The Bureau anticipates a relatively small but not insignificant overlap of HMDA and 1071 that will require duplicative reporting on real estate investment loans.. The Bureau considered excluding all HMDA-reportable transactions from the 1071 rule but believes such an exclusion would add complexity to data analysis and may be at odds with the statutory purposes of section 1071. The Bureau is considering whether it should require

financial institutions to flag applications reported under both regimes for data integrity and analysis purposes.

The proposed overlap between HMDA and 1071 would create significant and unnecessary complexities for covered financial institutions. While the Bureau has made efforts to limit the inconsistencies between HMDA and 1071, differences do exist, and requiring two sets of data to be collected and reported introduces needless complexity and burden. A borrower for a product subject to both reporting regimes will be given Form 1003 and the 1071 data collection form, which is likely to be confusing and frustrating for borrowers. Additionally, reporting and ensuring consistency between both collection regimes will impose substantial burden on covered financial institutions.

The Bureau should address this issue by removing business purpose loans from HMDA's scope. Creating a clear distinction between the two regimes would greatly reduce complexity and burden on financial institutions, as well as minimize confusion for credit applicants. We recognize this would require a new rulemaking, and we ask the Bureau to initiate the HMDA rulemaking on a parallel track so that both rules are finalized and implemented concurrently.

In addition, the 1071 rule will require reporting on transactions that are also reported under CRA rules by banks with assets above $1 billion. The overlap will result in costly duplication and confusion, as the 1071 proposal requires different reporting than CRA. For example, the 1071 proposal differs from CRA with respect to the treatment of renewals and extensions. The Bureau must work closely with the banking agencies working to modernize the CRA rules in order to reduce duplication and the friction caused by the different rules.

4. The final rule should list all excluded transactions in the regulatory text.

The Bureau proposes to exclude certain types of transactions from the definition of "covered credit transaction." While we agree with the Bureau's list of exclusions – except trade credit, for the reasons discussed below – we recommend that all of the excluded transactions are listed under § 1002.104(b). As proposed, some of the excluded transactions are listed in the rule text, while others are mentioned only in the official commentary to § 1002.104(b) (e.g., factoring). For clarity, the Bureau should list all exclusions in the rule text, including an exclusion for credit covered by Regulation Z, which covers only consumer-purpose lending.

The rule or commentary also should clearly state that loan purchases are not covered. Although we understand that a purchase does not involve an application for credit, in our experience compliance burden will be reduced if the rule or commentary contains a declaration that purchased loans are not covered.

5. The Associations recommend that trade credit be a covered credit transaction.

The Bureau should reconsider its decision to exclude trade credit from the rule's coverage. The Bureau states that providers of trade credit are not financial institutions, but that logic is circular. Merchants providing trade credit are providing a financial service to purchasers. Moreover, they are providing it at a steep discount that banks cannot match given their regulatory obligations. The preamble states that these merchants are unlikely to report accurately; however, the Bureau

has tools to address inaccurate reporting. Exempting providers of trade credit because the data collection would be challenging for them only exacerbates the unlevel playing field that currently exists between banks and trade credit providers.

E. Definition of minority-owned and women-owned small business – §§ 1002.102(m) and (s) and "minority individual" – § 1002.102(l)

The proposal defines a minority-owned business as one for which (i) more than 50 percent of its net "ownership or control" is held by one or more "minority individuals" and (ii) more than 50 percent of its "net profits or losses accrue" to one or more "minority individual." A minority individual would be defined as a natural person who is one or more of the following: Hispanic/Latino; Black or African-American; Native Hawaiian or Other Pacific Islander; Native American or Alaska Native; and Asian.

The Associations support the proposal to define a "minority individual," for purposes of determining minority-owned status, using only aggregate ethnicity and race categories. Doing so will help avoid burdening applicants with lengthy lists of subcategories, which would likely be overwhelming and confusing.

F. Definition of principal owner – § 1002.102(o)

The proposal defines a principal owner as a natural person who directly owns 25 percent or more of the equity interests of the business.[38] The Bureau notes that this definition is used for the Customer Due Diligence (CDD) rules, and should be familiar to financial institutions. The Bureau states that for 1071, entities would not be considered principal owners, and indirect ownership by individuals would not be considered in determining principal ownership.

The Associations support using the CDD rules to define a principal owner in the 1071 final rule. As the Bureau notes, banks are already familiar with this concept in the CDD rules. The Associations also agree that the 1071 rule should not include entities, and indirect ownership by natural persons. Including entities and indirect ownership would add unnecessary complexity to the 1071 rule.

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[38] If the Bureau intends to require the institution to provide applicants with the definition of a principal owner, in writing, as comment 102(a)(o)-2 suggests, that requirement should be placed in the regulation at § 1002.107(a)(20), or in the commentary to the data collection portion of the rule. Moreover, the same requirement is repeated in Appendix G, adding length and complexity to the rule. In general, the commentary for principal owner is almost entirely repeated in the Appendix. The Bureau could reduce length and burden by eliminating the repetition.

In addition, Appendix G contains certain statements that appear to be interpretations of the rule and that are not instructions, including a statement that institutions should not collect demographic information for guarantors unless they are also principal owners. If the intent is for Appendix G to provide simple instructions, then interpretations should be moved to the commentary or regulation.

II. Data Points - § 1002.107(a)

A. The final rule should not require covered financial institutions to collect and report the discretionary data points.

Congress mandated the collection and reporting of thirteen data points. Section 1071 gives the Bureau the authority to require any additional data that the Bureau determines would aid in fulfilling the purposes of that section, which as noted previously, is to facilitate enforcement of the fair lending laws and to help identify business and community development needs. The Bureau is proposing to use its discretionary authority to require financial institutions to collect and report eight additional data points. Notably, one of these data points – pricing – includes several additional pieces of information.

The statutorily mandated data points will fulfill the statutory purposes without the need for the discretionary data. The eight discretionary data points unduly increase burden and create more opportunities for errors, even with reasonably adapted procedures to avoid errors.

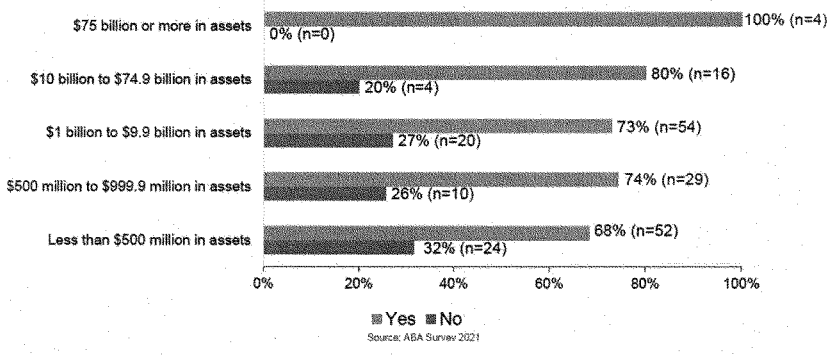
Many of the discretionary data points mirror data that Congress added to HMDA in the Dodd Frank Act—for example, expanded loan pricing data. However, if loan pricing data were needed to fulfill section 1071's purposes, Congress would have included the data point in section 1071 at the same time that it included expanded pricing data in HMDA.

The Bureau fails to consider the cumulative impact of these discretionary data points on financial institutions in comparison to the minimal benefits they will provide. The rule will require significant changes and additions to loan origination systems and processes, policies and procedures, training, and oversight. While the 2015 HMDA rule expanded an existing data collection and reporting regime, this rule will introduce a completely *new* reporting regime and one that impacts far more lines of business, credit products, and employees than HMDA's reporting obligation.

To comply with section 1071, banks will need to establish new procedures and processes for collecting and maintaining the data for all affected business units, update core systems and loan origination systems (many – almost a third of respondents to our survey – will require new systems), train all employees involved with commercial lending, and finally, test the new process and systems and make necessary adjustments. Banks also will need to hire and train employees to conduct data integrity scrubs and to report the data.

According to our survey, approximately a third of community banks will have to purchase commercial loan origination software to comply with the 1071 rules. In addition, the majority of community banks stated that they would have to update their current LOS, as the table below shows:

To comply with the proposed 1071 data collection and reporting requirements, our bank will need to update commercial loan origination software (LOS)



More importantly, the table below from our survey indicates that the Bureau's estimates are much lower than the real cost to update LOS. The Bureau estimated that a type A institution would spend $16,900 for this purpose, and a type B institution would spend $17,200 to update LOS. In our survey, banks with assets of $500 million or less reported costs for updating that average $39,500. Banks with assets over $500 million to $999.9 million reported costs that average $ 61,000.

Cost estimate to - Update commercial loan origination software (LOS)

	Mean	Maximum	Median	Minimum	Standard Deviation	Valid N
Less than $500 million in assets	39,500	200,000	25,000	3,500	52,933	17
$500 million to $999.9 million in assets	61,000	225,000	25,000	10,000	92,019	5
$1 billion to $9.9 billion in assets	59,583	150,000	50,000	0	57,018	6
$10 billion to $74.9 billion in assets	1,300,000	2,500,000	1,300,000	100,000	1,697,056	2
$75 billion or more in assets	-	-	-	-	-	0
All	131,133	2,500,000	25,000	0	461,263	30

Source: ABA Survey 2021

The Associations believe that other costs will be incurred to resolve interpretive issues surrounding the data points. While some data points are straightforward (e.g., loan number), others are open to interpretation. Experience with HMDA demonstrates that even a seemingly straightforward data point such as action taken or action taken date can be difficult to get right without clear guidance from the Bureau. HMDA also has shown the need for clarifications and reinterpretations issued later, which add significantly to implementation costs, burden, and the time frame.

Many of the 1071 discretionary data points will generate interpretive issues and be difficult to report correctly. Indeed, respondents to ABA's survey estimate that they will spend annually an average of $8,498 resolving reportability questions, $4,286 researching questions, and $4,451 resolving question responses. Further, most businesses do not know what their NAICS code is, which makes that data point vulnerable to inaccuracies, despite financial institutions' efforts to correctly report applicant provided data. The Bureau should take an incremental approach and begin with requiring the collection and reporting of only the statutorily-mandated data elements, and then reassess and reevaluate as necessary.

B. Comments on Certain Data Points

1. Application Method -- §§ 1002.107(a)(3)

Proposed § 1002.107(a)(3) would require financial institutions to collect and report "application method," defined as the means by which the applicant submitted the covered application directly or indirectly to the financial institution. A financial institution would comply with this by reporting one of the following options: in-person, telephone, online, or mail. If the financial institution has contact with an applicant in multiple ways, it would report the method based on a "waterfall approach." If a financial institution interacts with an applicant both online and by mail, a financial institution would report application method based on the method by which it, or another party acting on its behalf, requested the ethnicity, race, and sex of the applicant's principal owners pursuant to proposed § 1002.107(a)(20).

The application method data point, which is discretionary, will increase the compliance burden for covered financial institutions. In particular, the "waterfall approach" unnecessarily complicates reporting, as often there are several interactions with a small business, and it may be difficult to discern exactly how an application was received. For example, an applicant may provide much of the information for the application in person but then may provide additional information on the telephone or online. Based on the proposed commentary, it is not clear how the financial institution should report the application method in that scenario. Further, while the data point is "the means by which the applicant submitted the covered application" the related commentary discusses when a financial institution "meets with the applicant" or "communicated with the applicant by telephone." This commentary is confusing and does not provide clear guidance on how financial institutions can comply.

Rather than proposing an unnecessary, overly complex waterfall approach for application method, the Bureau should adopt the approach it proposes to use for applications involving both mail and online. Under that approach, a financial institution would report the application method based on the method by which it, or another party acting on its behalf, requested the ethnicity, race, and sex of the applicant's principal owners pursuant to § 1002.107(a)(20). The Bureau's stated purposes of gathering and collecting this data point are not furthered by the complex waterfall approach. Instead, a clear standard on how financial institutions should report this method that can be applied for all situations would better meet the Bureau's intent and would reduce the burden on financial institutions.

2. Action Taken -- § 1002.107(a)(9)

The Bureau proposes in § 1002.107(a)(9) to require reporting of the "action taken" by the financial institution on the covered application. The actions reported include: originated; approved but not accepted; denied; withdrawn by the applicant; or incomplete. The Bureau proposes to categorize all incomplete applications as a single category of "incomplete."

a. The Bureau should ensure that 1071 and HMDA are consistent.

Our chief concern with the action taken data point is its inconsistency with HMDA, particularly for transactions that may need to be reported under both regimes. We understand the Bureau's reasoning for proposing a single category of incomplete, as opposed to the approach under Regulation C, which provides separate categories for denials (including on the basis of incompleteness) and files closed for incompleteness (if the financial institution sent a written notice of incompleteness). We agree with reserving the "denial" action taken category solely for credit-related denials, rather than also including denials that are based on incompleteness. However, the misalignment of action taken categories between these two reporting regimes will cause substantial difficulty for financial institutions. This further supports our recommendation that an application reportable under 1071 should not also be a reportable transaction under HMDA.

b. The final rule should not require a flag for counteroffers.

We agree that the rule should not require an action taken category or flag for counteroffers. Regulation C does not include such a flag, and the two rules should be as consistent as possible. In the small business lending context, determining whether an action is a counteroffer is extraordinarily complex, and it is infeasible to capture all the proposed 1071 data fields for every counteroffer negotiated with an applicant. Such a category or flag would overly complicate this data point and likely lead to confusion and data errors.

3. Pricing Information -- § 1002.107(a)(12)

The Bureau proposes to use its discretionary authority to require collection and reporting of the following pricing data points: (i) the interest rate, and if adjustable, the margin, index value, and index name; (ii) the total origination charges; (iii) broker fees; (iv) non-interest charges scheduled to be imposed in the first year of the loan or line; (v) costs for MCAs; and (vi) whether the lender could have imposed a prepayment penalty, and whether it did so.

a. The final rule should not include loan pricing information.

The Associations strongly oppose requiring institutions to collect and report pricing data. Including pricing data in the initial 1071 data set, without understanding how small business loan pricing works, will restrict the availability of small business credit and negatively impact the economy. The Bureau should use supervision to determine if issues in pricing merit inclusion in the 1071 rule and to evaluate whether reporting the proposed pricing data *can* achieve the statutory objective of facilitating enforcement of the fair lending laws and fostering community development. While the banking industry supports both goals, we have strong concerns that reporting pricing data will achieve neither objective. Small business lending at banks is highly individualized and underwriting and loan pricing depend on many heterogeneous variables that are inherently unsuitable for aggregate analysis to determine whether discrimination occurred.

Small business loan pricing reflects the unique, non-commoditized nature of small business lending. Lenders typically consider certain factors, including but not limited to, cash flow, collateral, loan purpose and type, industry risk, time in business, and timing of receivables and payables, but there is no generally recognized industry standard applied to each of these. This is in stark contrast to residential mortgage lending, where industry and regulators have generally coalesced around certain standards, for example, loans with loan-to-value ratios over 80% are usually deemed riskier, and priced accordingly, than those with ratios below 80%.

Instead, banks assess each underwriting factor on a case-by-case basis to determine risk and price each small business loan. This flexible process allows banks to make more credit available than if there were strict guidelines, benefitting small businesses. However, regulators and the public are bound to view differences in pricing for businesses that appear to be similarly situated as evidence of illegal discrimination, when a closer review of all of the information available to the underwriter would dispel that conclusion. Providing and explaining each credit decision in supervision or enforcement is costly, and to be prepared to respond to anticipated increased claims of discriminatory pricing, banks will need to devote considerable additional resources to expanded fair lending compliance programs.

Advocates will also view the public data set as showing discrimination in pricing. As with HMDA, the data will drive media reports alleging discrimination in pricing, based only on the data, causing unwarranted damage to banks' reputations. Even if banks are given an advance copy of a story and the opportunity to respond, it is impracticable for each bank to defend each of its pricing decisions in media stories.

Over time, pressure from supervision, enforcement, and media reports will incentivize lenders to reduce the flexibility inherent in small business lending decisions. This will make credit harder to get for small businesses that may pose more risk.

We include a comparison of decisions on three small business applicants, to illustrate our concerns:

Factor	Business A	Business B	Business C
Loan amount	$65,000	$62,500	$67,500
Interest rate	5.00%	4.25%	4.50%
Origination fee	1.00%	1.00%	1.00%
Term	84 months	84 months	84 months
Purpose	Purchase equipment	Purchase equipment	Purchase equipment
Type	Standard	Standard	Specialty
Reason	End of life replacement	Expand capacity	Enter new (untested) product line
Personal guarantee	Yes	Yes	Yes
Guarantee strength	Weak	Strong	Good
Industry	Food/beverage	Food/beverage	Food/beverage
Time in business	20 years	15 years	20 years
2020 revenue	$2,000,000	$2,000,000	$2,000,000
Revenue trend	Declining	Increasing	Stable
Management stability	Significant turnover	Stable	Stable

As the table shows, these three applicants might appear similarly situated in the 1071 data. Each is in the same type of business, they are all seeking to purchase equipment, with 84-month terms, and the businesses all have the same amount of revenue in 2020. However, the highlighting shows that there are nuanced differences in risk that fairly and prudently result in different pricing for these businesses.

If the Bureau includes pricing information in the final rule, over time banks will not be willing to make some of these judgments about risk. The result will mean that some small businesses are shut out of the capital market. Section 1071 is intended to foster community development, and the Bureau should use its discretionary authority to fulfill, not frustrate, that purpose.

b. The Associations oppose collection and reporting of APR.

The Associations oppose requiring collection and reporting of the APR. The Truth in Lending Act (TILA) requires disclosure of an APR for consumer credit, and since TILA's enactment in 1968, business credit has been exempt from TILA. Moreover, Congress has not amended TILA to include business credit. In 2010, when Congress enacted the Dodd Frank Act, it made numerous amendments to TILA and could have expanded it to cover small business lending. Congress did not change TILA's scope, and the Bureau should not abuse its discretionary authority in 1071 to do so now. While some commenters cite state laws requiring disclosure of an APR for business credit, only 2 out of 50 have enacted such laws.

c. Collecting and reporting the interest rate will not yield useful data.

The proposal's attempt to capture interest rates shows the complexity of collecting and reporting pricing data, which the Bureau would add to the already costly process of collecting and reporting the statutory data points. For adjustable rate transactions, the institution must report not

only the interest rate, but also the margin, index value, and index name "at origination." [39] However, the commentary directs institutions to report the index value at the time the application "was approved" by the financial institution.[40] Often the index value is not at all related to either of these events, and will only add burden without helping data users understand the loan's pricing.

d. The final rule should not include origination fees.

The proposal defines origination charges as the total amount of all charges "payable directly or indirectly by the applicant and imposed directly or indirectly by the financial institution at or before origination as an incident to or a condition of the extension of credit, expressed in dollars."[41] The Bureau notes that the definition mirrors TILA's finance charge definition. As discussed above, Congress has had many opportunities, including in the Dodd Frank Act, to require lenders to calculate a finance charge for small business lending, and has not done so.

The Bureau should not use its discretionary authority to add this requirement to the mandatory data points. Compliance with TILA is challenging, and requires more training, testing, and systems updates than the Bureau has accounted for in its cost estimates. For example, while some third party charges could be excluded from the origination charge, for others it is not clear whether they are excluded. At the same time, the proposal requires institutions to include a broker fee, even though the proposal requires institutions to report broker fees separately. This data point will be inflated, fraught with errors, and will require lenders to constantly check, correct, and retrain staff.

e. The Associations oppose collection of initial annual charges.

For the same reasons as discussed above, the Associations oppose reporting of initial annual charges, including those imposed by third parties. Likewise, we do not support including fees the borrower could avoid – e.g., late fees – even if the applicant states their intention to incur avoidable fees. If an institution must report higher initial annual charges because the applicant states that it intends to incur those charges, data users will assume the institution decided to charge that applicant more than others. Recognizing and documenting such statements is operationally unworkable, and the inclusion of these fees would distort the data.

f. There is no support for including broker fees in the final rule.

The Associations oppose requiring institutions to collect and report data on broker fees. The Bureau states that the presence of brokers "creates opportunities for potential practices that inflate the cost of small business credit."[42] However, the Bureau provides no evidence that brokers are inflating the cost of credit.

The Bureau also states that fair lending risks may be "heightened in the small business lending market because applicants lack the substantive protections afforded to consumer credit

[39] Proposed § 1002.107(a)(12)(i)(B).
[40] Proposed cmt. 107(a)(12)(i)-4.
[41] Proposed § 1002.107(a)(12)(ii).
[42] 86 Fed. Reg. at 56,459.

applicants, such as the prohibition on basing loan originator compensation on the terms of a transaction."[43] Congress added that prohibition to TILA in the Dodd Frank Act. Had Congress been concerned about broker fees in small business credit, it could easily have extended TILA's prohibition to small business credit. Alternatively, Congress could have added broker fees as a data point in section 1071. The Bureau should not add to the already significant burden of 1071 by requiring a data point without any evidence that broker fees are a problem in the small business lending market.

g. Prepayment penalties should not be included in the final rule.

The Associations oppose requiring institutions to collect and report data on prepayment penalties. Typically, a financial institution's credit policies do not address prepayment penalties, or any rates or fees; credit policies are written generally and not for specific products. The context in which prepayment penalties may be imposed in commercial lending is complex and is specific to a particular transaction.

The burden of collecting this information is high, and the Bureau cites no evidence that institutions are applying prepayment penalties in a discriminatory manner or that they are used to impede community development. The Bureau states that penalties may be large, based on a percentage of the outstanding balance, and "understands there *may* be concern among stakeholders" that certain small businesses "*may* be steered to loans" with penalties.[44] However, the Bureau offers no evidence of steering to support this burdensome discretionary data point. The simple assertion that penalties might be large and a percentage of the outstanding balance does not justify requiring institutions to collect and report the data.

Moreover, the proposal would put most institutions at a disadvantage to MCA providers. The proposal does not require MCA providers to collect and report charges that are, effectively, prepayment penalties for MCAs. Nearly all MCA providers collect a finance charge at prepayment that represents the finance charge for the full term of the loan.[45] The proposal would not cover MCA charges for prepaying, creating an unlevel playing field for small business finance.

4. Census Tract -- § 1002.107(a)(13)

The proposal would require financial institutions to collect and report the census tract using a "waterfall" approach, as follows: (i) the address where the proceeds of the credit will be applied; or (ii) if the information in (i) is not available, the applicant's main office or headquarters; or (iii) if the information in both (i) and (ii) is not available, another address or location associated with

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[43] *Id.*

[44] *Id.* at 56,461.

[45] This practice is described as a "hidden prepayment charge" in the Small Business Borrowers' Bill of Rights. Disclosure of this form of prepayment charge, alongside any traditional prepayment penalty, is required under New York law using the following language:

"(i) whether the recipient would be required to pay any finance charges other than interest accrued since their last payment. if so, disclosure of the percentage of any unpaid portion of the finance charge and maximum dollar amount the recipient could be required to pay; and

(ii) whether the recipient would be required to pay any additional fees not already included in the finance charge."

the applicant. The proposed rule would also require that the financial institution report which one of the three types of addresses it used to determine the census tract reported. An institution would not be required to ask for the address related to (i) through (iii) above; the Bureau states that institutions can use the address that they are currently using for CRA reporting if they are required to report CRA data.

a. The proposed waterfall approach is needlessly complex.

The Associations support the proposal's flexible approach to reporting census tract, including permitting CRA reporters to use the same address for both data collections. However, the waterfall is unnecessarily complex and requires the institution to determine that information is not available before going to the next step in the waterfall. Instead, we recommend that the final rule give institutions the option to use one of the three addresses to determine the census tract location.

b. The Associations support a safe harbor for census tract reporting.

The proposal provides a safe harbor in § 1002.112(c)(1), which would state than an incorrect entry for census tract is not a violation of ECOA/subpart B if the institution obtained the census tract by correctly using a geocoding tool provided by the FFIEC or the Bureau. However, the safe harbor would not apply if the FFIEC or Bureau geocoding tool did not return a census tract for the address the institution provided.

We generally support the safe harbor. Despite reasonable efforts to avoid them, geocoding errors are common, particularly in rural areas, and even correct use of the geocoding tool can result in no census tract being identified. We urge the Bureau to adjust the safe harbor to provide protection for reasonable processes to identify and report the census tract when the FFIEC/Bureau tools do not return a census tract.

5. NAICS Code -- § 1002.107(a)(15)

Using its discretionary authority, the Bureau proposes to require financial institutions to collect and report a 6-digit NAICS code appropriate for the applicant's business. A financial institution would comply with this requirement if it uses the NAICS codes in effect on January 1 of the calendar year covered by the small business lending application register that it is reporting. When a financial institution is unable to collect or determine the applicant's NAICS code, it reports that the NAICS code is "not provided by applicant and otherwise undetermined."

The Bureau also proposes to permit a financial institution to rely on applicable applicant information or statements when determining and reporting the NAICS code. A financial institution may rely on a NAICS code obtained through the financial institution's use of business information products, such as company profiles or business credit reports, which provide the applicant's NAICS code. And, the proposal would provide a safe harbor for incorrect NAICS codes if the first two digits of the code are correct, the applicant does not provide the code reported, and the institution maintains procedures reasonably adapted to correctly identify the subsequent four digits.

Our members are extremely concerned about the challenges of reporting the NAICS code and the accuracy of the NAICS code data. They report that most small businesses do not know their NAICS code, increasing the opportunity for the data to be inaccurate. We also understand that not every business clearly falls within a NAICS code category, and therefore it becomes an interpretive issue for either the small business applicant or the financial institution, furthering the likelihood of inaccuracies. Moreover, the NAICS codes are scheduled to change in 2022, which will increase the chances for inaccuracies, as small businesses may not know their new code or that the SBA made changes to NAICS codes.

The Associations appreciate the attempt to reduce burden by offering a safe harbor; however, the safe harbor does not apply when the institution relies on the applicant's statement for the NAICS code. Thus, financial institutions that want the safe harbor would be required to try to determine the NAICS code themselves, a process that is burdensome and still fraught with risk of inaccuracies. For these reasons, we oppose collection and reporting of NAICS codes.

6. Minority- and/or women-owned businesses - §§ 1002.107((a)(18) and (19)

The proposed rule requires institutions to ask each covered applicant whether it is minority-owned and/or women-owned. The proposal clearly states that the determination of whether a business is minority or women-owned rests with the applicant, "A financial institution provides the applicant with the definition of a minority owned business [and woman owned business] when asking the applicant to provide its" status . . . but the financial institution is neither permitted nor required to make its own determination regarding the applicant's minority-owned [and women owned] business status."[46]

a. Applicants should determine whether the business is minority and/or women owned.

We support the proposal for the applicant, rather than the institution, to determine whether a business is minority and/or women-owned. We appreciate the proposal's clarity that institutions are not required or permitted to determine the business's status. Requiring institutions to determine the business's status would be extremely burdensome and impracticable. We also support the proposed language that can be offered to the applicant to assist them with their determination about minority and/or women-owned status.

We understand comments 102(l)-1 and 102(m)-2, and 102(s)-2 to require the institution to give the applicant the definition of a minority individual, a minority-owned business, and a women-owned business. The Bureau should clarify this by using "shall" or "must" in these comments.

b. The Associations support the proposal which would not require institutions to identify minority and women owned status by visual observation or surname.

We strongly support the decision not to require any visual observation or surname requirements in connection with minority or women-owned status. Such a requirement would be unworkable in determining whether a business is minority or women-owned.

[46] Proposed comments 102(m)-2 and 102(s)-2.

c. The Associations support combined information requests.

We also support permitting the institution to combine questions about ownership status with questions about the race, ethnicity and sex of the principal owners (in App. F, Paragraph 2.)

7. Race, ethnicity and sex of the principal owners - § 1002.107(a)(20)

The proposed rule requires an institution to ask the applicant for the race, ethnicity and sex of its principal owners, and the institution must provide the applicant with the definition of a principal owner in §1002.102(o). The institution cannot require the applicant to provide the information. The proposal would also require the institution to inform the applicant that it need not provide the information, and that the institution is prohibited from discriminating against the applicant. When an application is taken in person and the applicant declines to provide the information, the institution must identify the principal owners' ethnicity and race – but not their sex – by visual observation or surname.

The proposed rule would require the institution to use both aggregate and disaggregated subcategories (subcategories) when collecting the principal owners' ethnicity and race. The Bureau states that it "acknowledges" that this might "make data collection more difficult" on the phone and at point-of-sale.[47]

The proposal includes the subcategories used in Regulation C, but would diverge from Regulation C by adding subcategories for Black or African-American. In addition, the Bureau states that it is seeking comment on whether it should require use of subcategories for White and if so, what those subcategories should be. The Bureau also seeks comment on whether the final rule should include an aggregate category for Middle Eastern or Northern African.

In addition, the Bureau asks for comment on whether the collection of race and ethnicity should be combined into a single question, based on the 2015 National Content Test: Race and Ethnicity Report Analysis.

a. The Associations oppose use of disaggregated subcategories for ethnicity and race.

The Associations oppose the requirement to use the disaggregated subcategories for ethnicity and race. In its outline of proposals for the SBREFA review, the Bureau acknowledged increased burden as the reason for not considering the subcategories.[48]

Experience with HMDA shows that using the subcategories will be burdensome and frustrating for applicants and lenders. Using the subcategories in 1071 will impose more burden than in mortgage applications, which typically involve no more than two applicants. The 1071 proposal appears to require the institution to use the subcategories for up to *four* principal owners.

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[47] 86 Fed. Reg. at 56,480.

[48] "The Bureau stated in the SBREFA outline that it anticipated that requiring reporting based on visual observation and/or surname could create unwarranted compliance burdens in the context of small business lending, although the Bureau sought feedback on the potential challenges, costs, and benefits of implementing such a requirement." *Id.* at 56,476.

The subcategories will add length and friction to the application without providing meaningful benefits to data users. The Bureau states that the subcategories "could be beneficial when attempting to identify potential discrimination or business and community development needs in particular communities."[49] However, the Bureau notes that the data will not be useful if institutions do not have a sufficient number of applicants or borrowers within particular subgroups to permit reliable assessments of whether unlawful discrimination may have occurred . . . ."[50] The Bureau's own HMDA analyses show that mortgage applicants rarely select these subcategories:

> The vast majority of applicants selected one race, with the exception of applicants who selected American Indian or Alaska Native (in which case only a modest majority selected one race)." For ethnicity, "for most applicants, only one field of ethnicity was used (95.1 percent). Only about five percent used two ethnicity fields."[51]

The Bureau cites no evidence that small business applicants are likely to behave differently than mortgage applicants when confronted with all of the subcategories. Applicants for small business financing are certain to be as frustrated with this process, if not more, than mortgage customers have been. Note that in a telephone application for a mortgage, the institution is required to read aloud all of the subcategories to the applicant. If the Bureau requires the same approach in 1071, for up to four principal owners for each applicant, applicants are likely to react negatively.

The Bureau states that using the subcategories will promote "consistency with existing HMDA requirements."[52] However, the subcategories proposed in the 1071 rule are not consistent with current HMDA collection requirements, as the proposal includes subcategories for Black or African American. If the Bureau's goal is consistency with Regulation C, then it should not add new subcategories.

b. The Associations oppose adding aggregate categories at this time.

The Associations believe that to promote consistency with Regulation C and federal data standards, the Bureau should not add an aggregate category for Middle Eastern or North African at this time. Although the Office of Management and Budget in 2017 proposed to include that category in its Federal Data Standards on Race and Ethnicity, it never finalized that proposal. To avoid greater confusion and burden, the 1071 rule should only require use of the aggregate categories currently used in Regulation C and in OMB's data standards.

c. The final rule should not combine the questions about ethnicity and race at this time.

The Associations urge the Bureau not to combine the questions about ethnicity and race at this time. The Census Bureau's 2015 study discussed in the preamble indicates that many people who

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[49] *Id.* at 56,480.
[50] *Id.*
[51] Consumer Fin. Prot. Bureau, Introducing New and Revised Data Points in HMDA: Initial Observations from New and Revised Data Points in 2018 HMDA 22 (Aug. 2019), https://files.consumerfinance.gov/f/documents/cfpb_new-revised-data-points-in-hmda_report.pdf.
[52] 86 Fed. Reg. at 56,480.

select Hispanic or Latino ethnicity do not select a race because they do not identify with any of the aggregate race categories. However, the Bureau acknowledges that the 2020 Decennial Census did not combine the two questions, and they remain separate questions in Regulation C. At this time, the Associations believe the Bureau should maintain consistency across data collection rules and with the Census. Doing so will ease the burden on institutions collecting the data, and will also make analysis of the data easier for industry, regulators, and fair housing and community development groups.

d. The Associations oppose collecting race and ethnicity of principal owners by visual observation or surname.

The proposal would require financial institutions to identify the ethnicity and race of the applicant's principal owners by visual observation or surname, if the applicant declines to provide the information. However, the proposal prohibits an institution from identifying the sex of principal owners by visual observation or surname.

The Associations oppose a requirement to identify a principal owner's ethnicity and race by visual observation or surname. We support the proposal's requirement that the institution not identify the sex of the principal owners. Although the Bureau does not explain the different rule for sex, we believe a rule that does not require bank staff to guess the sex of a principal owner reflects the correct approach. Employees find this uncomfortable, and we believe most individuals who decline to provide the information would be offended if they knew that an employee was going to select an ethnicity, race and sex for them. Most importantly, the data generated by guessing race and ethnicity are bound to be inaccurate, providing no real benefit in exchange for the drawbacks of the requirement.

As experience with PPP lending shows, some applicants will decline to provide information on the race, ethnicity and sex of principal owners, and this will undermine the data's usefulness for fair lending analyses. However, the proposed solution - requiring lenders to identify race and ethnicity by visual observation – will not solve the problem. To encourage applicants to self-identify their race, ethnicity and sex, we recommend that the Bureau engage in a significant and sustained consumer education campaign about the data collection and its purposes.

We note that the extent of the visual observation or surname requirement is unclear. The section-by-section discussion and commentary state that an institution would have to identify *at least one* principal owner by visual observation or surname if the applicant does not provide the race and ethnicity of at least one principal owner.[53] However, the rule states that institutions must collect the "ethnicity, race, and sex of the applicant's principal owners . . . ."[54] The Bureau also asks for comment on whether, for point-of-sale situations, the race, ethnicity and sex of only one principal owner should be required.[55]

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[53] *Id* at 56,483.
[54] Proposed § 1002.107(a)(20).
[55] 86 Fed. Reg. at 56,480.

e. The Bureau should consider exemptions for point-of-sale collection.

Based on feedback from SERs and other stakeholders, the Bureau "acknowledges" that compliance with some aspects of the proposed rule may be particularly challenging in certain situations. The Bureau asks whether it should exempt credit applications offered by retailers at point-of-sale from some or all of the proposed rules for collecting the principal owners' race, ethnicity and sex, including the requirement to identify race and ethnicity by visual observation or surname; using the disaggregated subcategories; and collecting information on up to four principal owners.[56]

We support an exemption in the final rule from the collection of demographic information on the small business owners in private label and co-branded credit applications. Requiring collection of sensitive data in a retail environment will discourage small businesses from applying at point of sale, restricting access to credit. Asking an individual to identify the race, ethnicity and sex of a business's principal owners at check out or a customer service desk with other customers and store employees nearby introduces privacy risk that the proposal does not address. We note that recently enacted privacy laws, including California's Consumer Privacy Act, deem race and ethnicity as sensitive personal information (PI) entitled to greater protections than other PI.[57]

Similarly, the proposal to collect demographic information in retail stores is likely to discourage retailers from entering into private label and co-branded arrangements. Merchants need speed and simplicity to offer credit in the store, and private label and co-branded lenders have created processes to meet these needs. Similarly, small businesses also prefer a quick and seamless check out application experience. As a result, applications generally request only that information necessary to make a credit decision.

Moreover, given the sensitivity of the information requested, many applicants will decline to provide the information, and we do not believe retail employees should identify a principal owner's race and ethnicity based on visual observation or surname. As a result, we anticipate the vast majority of small business point of sale credit applications will lack demographic information, even if not exempted in the final rule from collection and reporting this information.

The proposed rule would likely decrease access to private label and co-branded credit, without advancing sections 1071's far lending and community development objectives. The quality of data collected in a retail environment is likely to be poor. Retail employees, who do not work for the lender, will have little incentive to collect accurate and complete information, and training would be extremely expensive given frequent turnover in these positions. As the Bureau notes, FinCEN's CDD rule exempts point-of-sale transactions for retail purchases up to $50,000.

We urge the Bureau to exempt private label and co-branded commercial credit applications from the requirement to collect demographic information.

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[56] *Id* at 56,480.
[57] Cal. Civ. Code §§ 1798.121 (2021).

f. Collection of sex of principal owners should be revised to refer to gender.

The Associations generally support the Bureau's proposed rule for collecting the sex of the principal owners. As noted, the proposal would not require the institution to collect the principal owners' sex by visual observation or surname, and we believe this is the right approach.

However, we recommend that the Bureau consider substituting "gender" for "sex," as gender is more consistent with modern usage. In addition, the Bureau could provide some additional check boxes for trans and nonbinary in addition to the self-description and free form text line.

g. The sample data collection form is helpful.

The proposal includes a sample data collection form that explains the purpose of the data collection, defines and collects information on principal owners, and defines and collects information on minority and women-owned status. The Associations support inclusion of the sample form in the final rule. We urge the Bureau to provide sample forms in Spanish and other non-English languages at the time the final rule is issued.

h. The Bureau should reduce repetition in the rule, commentary, and Appendices F and G and consolidate all mandatory statements in one place.

We appreciate the Bureau's efforts to explain the data collection rules in Appendices F and G. However, there is a lot of repetition between the appendix, commentary and regulation; in addition, the appendices appear to contain mandatory statements that should be in the rule itself. It would be simpler for financial institutions if all of the binding requirements and prohibitions were in one place – preferably in the rule – rather than spread across the rule, commentary and Appendix.

III. General rules for data reporting

A. Verification of applicant provided information -- § 1002.107(b)

The proposal does not require institutions to verify applicant-provided information. An institution may rely on an applicant's statements in compiling certain data points. However, under the proposal, if the institution verifies the data, the institution must report the verified information. The Bureau states that applicant provided data is sufficiently accurate to carry out the purposes of section 1071.[58]

1. The Associations support permitting institutions to rely on applicants' statements, but oppose the proposed requirements regarding reporting verified information.

As the preamble notes, ECOA section 704B(e)(1) does not require institutions to verify applicant provided information.[59] No SERs or other stakeholders asked the Bureau to require verification of applicant information, according to the Bureau.[60] A requirement to do so would greatly

[58] 86 Fed. Reg. at 56,485.
[59] *Id* at 56,484.
[60] *Id*

increase the already significant burden that the 1071 rule will impose on institutions. Contrary to the Bureau's assertion that the requirement to report verified data would not add operational difficulty, having to update the LAR to reflect data points that are verified will increase operational burden, as institutions will have to build processes and train personnel to capture the information and determine whether the LAR should be updated.[61]

2. The proposed rule regarding verification is unclear and should be removed.

We also note that the meaning of "verification" is unclear. If an institution asks the applicant for its NAICS code in connection with an application for small business credit, and the institution also asks for the applicant's tax return to verify some other information and notices the NAICS code on the tax return is different, must it report the NAICS code on the tax return? If so, then the proposal imposes more burden than the Bureau has accounted for, as every piece of information on other documents might have to be compared to the information on the application. It is also unclear that this burdensome process would improve data accuracy.

In addition, it is not clear whether verification includes other information about an applicant that an institution might have elsewhere in its files. What if an institution asks the applicant for the NAICS code and does not request a tax return, but happens to have a copy of the applicant's tax return in its system, in connection with another transaction two years ago? Is the institution required to verify the NAICS code based on the old tax return? Such a requirement would be burdensome, requiring institutions to search their systems to determine if they have other information on the applicant, and would not add measurable value to data accuracy.

The Bureau asks for comment on whether the rule should require institutions to indicate whether data points were verified. The Associations do not support requiring institutions to report whether given data points have been verified. The Bureau did not provide a rationale for such a requirement, and we do not see any benefit from adding another data field to indicate whether the institution reported data provided by the applicant or has reported verified data. Moreover, the concept and application of the verification requirement are murky and unworkable, and it should not be included in the final rule.

B. Time and manner of collection -- § 1002.107(c)

The proposal requires an institution to maintain procedures to collect applicant-provided data points at a time and in a manner that is reasonably designed to obtain a response. Comment 107(c)(1)-2 provides that an institution has the latitude to design procedures "that work best for its particular lending model and product offerings" so long as the procedures are reasonably designed to collect the applicant-provided information.

The Associations appreciate the flexibility provided to financial institutions. However, the commentary is confusing and should be clarified or eliminated. Comment 107(c)(1)-7 suggests that an institution must report "updated" information, however, it is not clear what "updating" means. For example, if an applicant supplies information without the institution requesting it, must the institution "update" its reporting based on that information? In addition, it is not clear

[61] *Id* at 56,485.

how this requirement to report updated information relates to the proposal to report verified information. The Associations believe these references to updating information should be removed from the final rule.

IV. Firewall -- § 1002.108

ECOA section 704B(d) states that "[w]here feasible, no loan underwriter or other officer or employee of a financial institution, or any affiliate of a financial institution, involved in making any determination concerning an application for credit shall have access to any information provided by the applicant pursuant to a request under subsection (b) in connection with such application." If the financial institution determines that an underwriter, employee or officer involved in making a determination "should have access" to any information provided by the applicant pursuant to a request under 704B(b), the financial institution must provide a notice to the applicant of the underwriter's access to such information, along with notice that the financial institution may not discriminate on the basis of such information.

A. The firewall will impose needless burden on institutions.

As ABA stated in comments during the SBREFA review process, banks are concerned with implementing a firewall. The firewall, especially in connection with the requirement for recording and maintaining an applicant's demographic information separate from the application and accompanying information, creates unnecessary burdens on covered financial institutions. The requirement to keep the protected demographic information separate is likely unworkable for many institutions, given the roles of individuals involved in accepting and processing applications. By comparison, HMDA and Regulation C have no such requirement to record and maintain Form 1003 information separate from the consumer's application. Functionally, these requirements will be difficult for many institutions, particularly smaller institutions, to implement.

For many institutions, the individual accepting a small business's application is a loan officer that will be involved in making a decision on that application. This is true at larger institutions as well as smaller ones, as many institutions provide loan officers with decision authority up to a certain dollar amount, meaning these loan officers are involved in making a determination concerning the application.

We appreciate that the Bureau has developed a notice to be used when establishing a firewall is not feasible. However, the rule text should refer to the model language in the notice.

B. Providing the notice will put some institutions at a competitive disadvantage.

In addition, we are concerned that using the exception, and therefore, providing the notice, may put a financial institution at a competitive disadvantage with an institution that does not need to use the exception. A small business may be troubled by the notice's reference to discrimination and access to demographic information, and as a result, may be encouraged to seek credit from a bank that does not have to provide the notice because it can create a firewall. Therefore, we ask that the Bureau consider exempting smaller financial institutions from the firewall to avoid

putting these institutions at an unfair disadvantage compared to others that can establish the firewall.

C. The firewall should not be applied to demographic information based on visual observation or surname.

We urge the Bureau not to expand the firewall provision to information about principal owners' ethnicity and race that is obtained via visual observation and/or surname. The firewall as proposed creates significant practical burdens and expanding it to visual observation and surnames would make it nearly impossible for many to comply.

D. The Bureau should give institutions more flexibility in determining that the firewall is infeasible.

We appreciate that the proposal would permit a financial institution to determine that several employees or officers should have access to the protected demographic information (e.g., all loan officers). However, we do not understand why an institution could not make that determination for all employees and officers, so long as the exception notice is provided to all applicants. At small institutions, a class of employees (e.g., loan officers or others involved in making a determination on an application), comprise a larger percent of total employees. We do not believe the distinction on how a financial institution can use the exception furthers the purpose of Section 1071. Therefore, we urge the Bureau to give financial institutions latitude to determine how to apply the exception, whether it be a group of employees or officers or all employees or officers.

V. Reporting Data to the Bureau

A. Reporting to the Bureau -- § 1002.109(a)

The Associations support the proposed requirement for institutions to report their data to the Bureau by June 1, however, the Bureau should permit institutions that want to file their data on March 1 to do so.

B. Reporting when multiple financial institutions are involved in a covered credit transaction – § 1002.109(a)(3)

The proposed rule provides guidance for reporting responsibilities when more than one financial institution is involved in a covered credit transaction. The Bureau appears to intend for the rule to mirror Regulation C's requirements in § 1003.4(a) and commentary.

1. The Associations generally support the proposal but request clarity when applications do not result in originations.

The Associations support this proposal. However, for applications that do not result in an origination, the rule text states that "any financial covered financial institution that made a credit decision shall report the application." For clarity, we suggest that the rule text match comment 109(a)(3)-1.ii., which appears to require that each covered financial institution that reviewed the application reports the credit decision it made (if it made one), or reports that the application was

withdrawn or closed for incompleteness, as appropriate. As currently proposed, the text could be read to mean that as long as one institution reports its decision, then others need not do so.

2. Financial institutions should not be required to determine whether a withdrawn applicant has received credit elsewhere.

In the preamble, the Bureau states:

> Proposed § 1002.109(a)(3) would further provide that if there was no origination, then any covered financial institution that made a credit decision shall report the application. The Bureau is aware that under certain lending models as they operate today, financial institutions may not always be aware of whether another financial institution originated a credit transaction. The Bureau believes that information on whether there was an origination should generally be available, or that lending models can be adjusted to provide this information at low cost. For example, if an applicant applies to Financial Institutions A and B, and then withdraws an application with Financial Institution A, then Financial Institution A should be able to ascertain whether the applicant obtained credit from Financial Institution B.
>
> *****
>
> The Bureau seeks comment on this aspect of its proposal. In particular, the Bureau seeks comment with respect to proposed § 1002.109(a)(3) on whether, particularly in the case of applications that a financial institution is treating as withdrawn or denied, the financial institution can ascertain if a covered credit transaction was originated by another financial institution without logistical difficulty or significant compliance cost.[62]

It is completely impractical for institutions to determine whether an applicant has received credit at another institution. The Associations reject any notion that the rule should require that institutions make such determinations. The burden would be considerable, adding to the already significant burden involved with the data collection in general.

C. Publication of data - § 1002.110

The Associations support the proposal to have the Bureau provide LARs to the public, rather than each institution doing so.

VI. Recordkeeping - § 1002.111

Under the proposal, institutions would be required to retain records of compliance, including the LAR, for three years. In addition, the proposal requires institutions to "maintain, separately from the rest of the application and accompanying information," the applicant's statements whether it is minority- and women-owned, and the race, ethnicity and sex of the principal owners. The proposal also requires institutions to ensure that personally identifiable information about an individual is not combined with the 1071 data.

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[62] *Id.* at 56,495.

A. The Bureau should exempt institutions from the requirement to maintain demographic information separately from other applicant information.

For separate maintenance of demographic information, ECOA section 704B(b)(2) states that the institution must "maintain a record of the responses . . . separate from the application and accompanying information." The Bureau should use its exemption authority in ECOA section 704B(g)(1) to exempt institutions from the separate maintenance of demographic information in § 1002.111(b) and its commentary. That authority allows the Bureau to make exceptions and exemptions that are necessary and appropriate to carry out the purposes of section 1071. The proposed requirement will only make examinations and audits for fair lending, 1071 data integrity, and community development needs more cumbersome and costly. If the demographic information must be stored separately, it would have to be retrieved from a separate file and associated with a particular application to perform any analysis and for any test for accuracy.

B. The final rule should give institutions flexibility in how they collect demographic information.

In addition, the Bureau's reading of ECOA section 704B(b)(2) is problematic and thus proposed § 1002.111(b) is unclear. Proposed § 1002.111(b) states that institutions must "maintain" the information separately. In the section-by-section discussion, the Bureau states that a commenter asked it to clarify in the 1071 rules that demographic information can be collected on an application form, as is the case in Regulation C. [63] The Bureau does not squarely address the commenter's request, other than to note that HMDA does not contain a provision that mirrors ECOA section 704B(b)(2). The Bureau further acknowledges that prohibiting collection of demographic information on the application itself will interfere with the proposed requirement in § 1002.107(c)(1) that institutions have procedures reasonably designed to obtain applicant-provided data. Yet, comment 111(b)-1 states that an institution "could" collect the information separately from the application, which suggests that institutions could also choose to collect the information on the application form itself.

However, the Bureau also states that an institution must *not* collect the demographic information on the same form as the rest of the application in the section-by-section discussion of proposed §1002.107(c)(1) (procedures reasonably designed to obtain applicant-provided data points). The Bureau states that asking for applicant-provided information at the time of a covered application "in connection with a written application form" would be more likely to obtain a response, as required by proposed § 1002.107(c)(1), "provided *any collection form* requesting applicants' protected demographic information . . . . *is separate from* the application form and other documents . . . as would be *required* by proposed § 1002.111(b)."[64]

The final rule should not prohibit collecting the demographic information on the same form as the rest of the application. Notably, that prohibition would disrupt SBA's 7(a) loan process, as the Borrower Information Form 1919 for the 7(a) program includes questions on the applicant's

[63] *Id* at 56,501.
[64] *Id* at 56,487, emphasis added.

race, ethnicity, and other demographic information, along with other application material.[65] More importantly, the Dodd Frank Act does not prohibit including demographic questions on an application form; it requires "recording" the information separately, which is a requirement we believe the Bureau should waive, as explained above.

Mandating separate collection of demographic information would only complicate the small business application process for no benefit—in fact, it would frustrate the purpose of the 1071 data collection. Our members report that collecting information on a separate page, screen, or email makes it more likely that applicants will skip the questions because they are uncomfortable with these questions, and they want to move through the application quickly.[66] Applicants will be even more likely to skip the questions if the final rule includes the disaggregated subcategories for ethnicity and race.

D. The Bureau should waive the separate maintenance requirement when the firewall is infeasible.

The Bureau requests comment on whether the separate maintenance requirement should be "waived" when an institution determines that the "firewall" required in § 1002.108(b) is infeasible, because underwriters or other staff need access to the demographic information.[67] The Bureau should waive the separate maintenance requirement when the firewall is infeasible. It will be operationally burdensome, without any benefit, to maintain demographic information separately, and if it is infeasible to maintain a firewall, it is just as infeasible to maintain the information separately from the rest of the application that an underwriter to which the underwriter needs access.

VII. Bona fide errors

A. Bona fide errors and safe harbors - § 1002.112 and Appendix H

The Bureau proposes to define a bona fide error in compiling, maintaining, or reporting data with respect to a covered application as an error that was unintentional and occurred despite the maintenance of procedures reasonably adapted to avoid such an error. Further, such an error is presumed not to be a violation of ECOA or proposed subpart B if the number of such errors does not exceed the thresholds set forth in proposed Appendix H (the so-called "tolerance thresholds"). However, an error is not a bona fide error if either there is a reasonable basis to believe the error was intentional or there is other evidence that the financial institution did not maintain procedures reasonably adapted to avoid such errors. A financial institution is presumed to maintain procedures reasonably adapted to avoid errors with respect to a given data field if the number of errors found in a random sample of the financial institution's submission for the data field does not equal or exceed a threshold specified by the Bureau for this purpose. An error that

[65] U.S. Small Bus. Admin., Borrower Information Form, https://www.sba.gov/document/sba-form-1919-borrower-information-form (last visited Jan. 5, 2022).
[66] It may be that separate collection and maintenance of the demographic information is intended to facilitate the "firewall" between the information and decision makers, but it is needlessly overbroad.
[67] 86 Fed. Reg. at 56,502.

meets the criteria for one of the four safe harbor provisions would not be counted as an error for these purposes.

B. The proposed tolerance thresholds are too low for a data collection as challenging as 1071.

We appreciate the Bureau's acknowledgment that bona fide errors may occur despite the maintenance of procedures reasonably adapted to avoid errors. However, we are concerned that the tolerance thresholds are very low. We do not believe that the tolerance thresholds for HMDA reporting provide a fair and appropriate measure for the tolerance thresholds for this rule. First, implementation of 1071 introduces an entirely new data collection and reporting regime. Implementation and oversight of the 1071 rule will be a monumental task for financial institutions, especially smaller institutions, and will require the creation of entirely new policies and processes, along with the necessary staff training and oversight. Second, for most institutions, small business lending involves many different credit products, lines of business, and employees than residential mortgage lending. Banks will strive to adopt and maintain procedures reasonably adapted to avoid errors in compiling, maintaining and reporting data. Yet, even with these procedures, we believe bona fide errors are likely to occur, especially given the substantial number of data points the Bureau is mandating. We ask that the Bureau increase these tolerance thresholds in recognition of the substantial implementation efforts that financial institutions will undertake.

C. The Bureau should provide a one-year grace period for errors in the 1071 data.

Additionally, we ask the Bureau to provide a one-year grace period for errors in the compiling, maintaining and reporting of 1071 data. The Bureau provided such a grace period for the 2015 HMDA rule, and it is necessary for the 1071 rule, as well, due to the substantial implementation burden that financial institutions will face.

D. Errors in data collection during crises such as COVID-19 should not be counted towards error tolerances.

Finally, our recent experience with the COVID-19 emergency has shown that there may be circumstances when financial institutions need to provide credit quickly to their communities. The Paycheck Protection Program (PPP) presented an opportunity for financial institutions to provide relief to small businesses in their communities. However, the short timeframe for implementation, along with the constant flow of new and revised guidance from the SBA created significant challenges to financial institutions. If there is a need for a program similar to PPP in the future, 1071 data collection and reporting may complicate its rollout. Therefore, we ask that application data for special programs such as PPP not be counted for purposes of determining tolerance thresholds.

VIII. Implementation

A. Compliance date - § 1002.114

The proposal would require financial institutions to begin collecting data 18 months after publication of the final rule. Although the SBREFA outline indicated that the Bureau was considering a two-year implementation period, the preamble states that the Bureau "agrees with the stakeholders that asserted that a shorter implementation period is preferable given the length of time that has elapsed since the passage of section 1071 of the Dodd-Frank Act."[68]

1. The Bureau should give covered institutions three years to implement the final rule.

The 18 months the Bureau proposes for implementation is completely inadequate for a rule that is both complex and broad in coverage. Not only does the rule require collection of 21 data points, some of which require additional itemization, but also the separate maintenance of demographic information and consideration of whether a firewall is feasible. If a firewall is not always feasible, institutions must build processes to ensure it gives applicants the disclosure..

To ensure compliance with these requirements, financial institutions will need time to draft and/or revise policies and procedures. They will have to hire new employees in production, operations, risk, compliance, and IT, in a tight labor market. They must also buy or upgrade software for loan origination and integrate that software with other systems. Our members state that the work to get all systems in place and integrated is not a one-time task; instead, it is an iterative process of testing, finding problems, and fixing them, and then re-testing. This process will need to be carried out across multiple lines of business that are covered by the 1071 rule.

Community banks that rely on core system providers must wait for these providers to update their systems, then the bank must test the updates and work with the core to resolve problems, and only after all problems are resolved can their HMDA/CRA vendors begin to adapt their systems to integrate with the core system.

Some community banks use a platform and not their core system provider to originate small business loans. These banks must ensure that, once their core provider has built the fields for all of the data points, that each is mapped individually to the small business lending platform. This requires the creation of multiple APIs, which imposes additional costs and delays.

In addition to banks' reliance on the core providers and platforms, many banks rely on HMDA/CRA vendors to scrub and report their data. These vendors cannot begin their work on 1071 until the cores and platforms are finished changing their systems, and the financial institution has tested those systems. Those banks that do not report HMDA or CRA data will be entering relationships with these vendors for the first time and will not have the experience with the testing process that other banks have.

Training for 1071 compliance will be an extensive undertaking, covering loan officers and other customer-facing staff as well as risk, operations, fair lending, legal and IT employees. Most bank

[68] *Id* at 56,507.

staff working in the small business area are not used to collecting data to the accuracy standards the Bureau envisions. Some staff may be familiar with HMDA and CRA; however, the overlap with 1071 will generate confusion, requiring additional training for these staff.

The proposed 18-month implementation period stands in stark contrast to the implementation period for the Bureau's 2015 HMDA rule changes. The Bureau published the final changes to the HMDA rule in October 2015, with the revisions taking effect for data collected on or after January 1, 2018. The 1071 rule is much larger undertaking for financial institutions than the 2015 HMDA rule changes; for 1071, institutions must build an entire data collection regime, whereas for HMDA they were required to make changes to an existing data collection scheme.

Shortchanging the 1071 implementation period will result in inaccurate data for the first few years, limiting its usefulness for fair lending enforcement and community development. The activities described above cannot be bypassed, nor can they be rushed to meet an artificial deadline. While we understand that 1071 was enacted over 10 years ago, that has no bearing on the time it takes to implement a rule as complex and far reaching as 1071. We urge the Bureau to allow three years for the industry to implement the rule, which will facilitate the collection and reporting of better quality data.

2. The final rule should require data collection beginning on January 1.

The preamble indicates that collection of 1071 data might begin on the date that is 18 months after the final rule is published, even if that date is not a January 1. The Associations oppose starting data collection on a date other than January 1. Having less than a full year's worth of data will not provide regulators and others with a representative and complete data set. In addition, data users will want to make year over year comparisons, and a partial year must be ignored in these efforts. The rule should require that data collection begin on a January 1 just as the Bureau did for changes to HMDA in 2015.

IX. Privacy

The Bureau proposes to adopt a balancing test as the method by which it would implement its discretion to delete or modify data before making the data available to the public. Specifically, the Bureau proposes to modify or, as appropriate, delete data fields from the public 1071 data if it concludes that the release of the unmodified data would create risks to the privacy interests of applicants, related natural persons, or financial institutions that would not be justified by the benefits of such release to the public in light of the statutory purposes of section 1071.

The proposal presents only a partial application of the balancing test for public comment. The Bureau states that after it receives at least one full year of 1071 data, the Bureau intends to analyze the data for re-identification risk and then issue a policy statement setting forth its intended modifications and deletions. At this time, the Bureau does not intend to re-propose its balancing test analysis for public comment prior to issuing the policy statement.

A. The Bureau's procedure for applying the balancing test is flawed and must be revised.

The Bureau must reconsider its approach to protecting privacy. While the Bureau cannot conduct a full analysis of the potential harms of disclosing 1071 data at this time, without that analysis, the public does not have a meaningful opportunity to comment on this aspect of the rule.

Presumably, the Bureau believes that the data should be published without delay, at the expense of important privacy interests. We disagree. It is in all parties' best interest for the Bureau to fully analyze the re-identification and other privacy risks of 1071 data and then publish that analysis for public comment in order to determine those modifications and deletions that are necessary to protect the privacy and proprietary interests of small business owners and the financial institutions that serve them.

The Bureau's disregard for administrative process and public input in the determination of privacy issues was also on display in 2015 when it issued amendments to Regulation C followed by a policy statement rather than notice and comment rulemaking required by HMDA. However, even then the Bureau published the policy statement for public comment. At a minimum, we urge the Bureau to follow that process in this rulemaking.

However, we disagree with the Bureau's determination that an Administrative Procedure Act (APA) notice-and-comment rulemaking process is not required for decisions about modifying or deleting data prior to making the data public. The statute does not state or otherwise indicate that the Bureau may use this discretion without following an APA rulemaking process. There are two provisions in 1071 that provide the Bureau "discretion:" (1) the authority to "delete or modify data collected under this section which is or will be available to the public"[69] and (2) the authority to "compile and aggregate data collected under this section for its own use; and make public such compilations of aggregate data."[70] The Bureau proposes § 1002.110(b) in this rulemaking to implement the latter provision, but offers no explanation as to why believes it can exercise discretion, without rulemaking, to resolve the significant privacy issues presented by the former. The provisions should be treated the same; both should be implemented through an APA rulemaking process. The future policy statement applying the proposed balancing test is a "rule" under the APA, as it will implement and interpret law and policy. It is not simply a general statement of policy.

B. Comments on the preliminary application of the balancing test to data points.

The Associations have substantial concerns with the Bureau's preliminary application of the balancing test to the proposed data points. For benefits, the analysis provides vague statements that are not clearly linked to the statutory purposes of fair lending enforcement and community development. For example, the Bureau makes the vague statement that the application method "would allow the public to better understand the role of the financial institution as a creditor and would facilitate pricing analyses by helping the public identify potential factors in pricing

[69] 15 U.S.C. § 1691c-2(e)(4) (2018) (ECOA Section 704B(e)(4)).
[70] *Id.* § 1691c-2(f)(3)(A), (B)) (ECOA Section 704(f)(3)(A), (B)).

outcomes."[71] And as discussed above, the demographic information is likely to be missing or inaccurately identified through visual observation or surname, undermining the data's usefulness for fair lending analyses.

We are also concerned about the re-identification risks of certain data points, but without the Bureau's re-identification study, our ability to comment is limited. However, even without such a study, the release of a business' census tract location and NAICS code presents substantial re-identification risk. Notably, the banking agencies do not publish CRA small business data on a loan-by-loan basis, in part because of the ease of re-identifying small business owners based on geography. Our members, SERs, and other stakeholders have consistently expressed concern about the very real potential for any data user to identify a business owner.

While some data may not appear sensitive or harmful, our members note that fraudsters can use any data, no matter how innocuous, to perpetuate fraud. After the SBA released the PPP data, banks experienced fraudulent attempts to access small business customers' accounts through phishing and other techniques. Phishing scams are getting more sophisticated by the day, and if a small business can be re-identified through the 1071 data, the Bureau's decision to release that data will make them even more vulnerable.

Fraud aside, other companies will mine the 1071 data, aggregate it, and sell it to interested parties, which will compromise the privacy of small businesses and their owners. The trend in privacy laws, including the California Consumer Privacy Act (CCPA) and the General Data Protection Regulation (GDPR), is to reduce or restrict companies' ability to gather and sell information about unsuspecting persons. The Bureau must delete or modify many of the data fields to protect small businesses and financial institutions, and it can do so without compromising the objectives of 1071.

C. Sensitive data points must be modified or redacted.

Certain data points are extremely sensitive for a small business, and if re-identification were to occur, there is a significant potential for a negative impact on that business. For example, the loan purpose may reveal information the small business would consider confidential commercial information, such as plans for a business acquisition or expansion. If that information is made public, it may put the small business at a competitive disadvantage.

The same is true regarding credit amount applied for and the amount approved or originated. Reasonable inferences can be made about a small business's financial status based on this information, if the small business is re-identified. Similarly, the information on action taken and denial would reveal a business's financial status, which would be harmful competitively. Also, if a business is re-identified and the 1071 records show it applied for credit through multiple channels or multiple lenders, and/or was declined, this information may harm a business's prospects for credit.

The most sensitive data is in the pricing information, as that has direct connections to a small business's financial health. Revealing this information about a small business would

[71] 86 Fed. Reg. at 56,526.

unquestionably reveal confidential and sensitive competitive information, placing the business at a substantial competitive disadvantage. Because many small businesses are sole proprietorships, pricing information also reveals the proprietor's personal financial standing and their competitive position.

D. The Associations oppose inconsistencies with HMDA disclosure.

We are concerned that, in certain instances, the Bureau is considering making a data point public when the same data point is deleted or modified under HMDA. For example, the Bureau indicates it may modify the application date, which has never been made public under HMDA. The Bureau offers no explanation for this inconsistent treatment. The Bureau should ensure that any data deleted in the HMDA dataset is deleted in the 1071 dataset, including: the unique identifier; the application date; and the action taken date. All of these data points are deleted from the HMDA data before it is made public.

The unique identifier is particularly problematic and must be deleted from the public dataset. The unique identifier often includes the loan number or account number, and therefore, that data point, combined with the financial institution's name, provides a substantial opportunity for fraud. For a line of credit, these two data points (the unique identifier and the financial institution name) can easily provide an opportunity for fraudsters. By comparison, since 1990, the application or loan number has been deleted from the HMDA dataset; and in 2018, the Bureau deleted the universal identifier from the public data set. It must take the same approach with respect to the 1071 data.

E. The Associations support redaction of free form text fields.

We agree with the Bureau's proposal to delete all free form text fields from the public dataset. Similar to HMDA, it would not be feasible for the Bureau to review the contents of each free-form text field submitted before disclosing the loan-level data to the public. Deleting these data fields appropriately balances the risks to privacy of involved parties and the benefits of disclosure in light of 1071's purpose.

Conclusion

We appreciate this opportunity to comment on the Bureau's 1071 proposed rule. If you have any questions about our comments, please contact Kitty Ryan at kryan@aba.com, (202) 663-5478.

Sincerely,

American Bankers Association
Alabama Bankers Association
Alaska Bankers Association
Arizona Bankers Association
Arkansas Bankers Association
California Bankers Association
Colorado Bankers Association

Connecticut Bankers Association
Delaware Bankers Association
Florida Bankers Association
Georgia Bankers Association
Hawaii Bankers Association
Idaho Bankers Association
Illinois Bankers Association
Indiana Bankers Association
Iowa Bankers Association
Kansas Bankers Association
Kentucky Bankers Association
Louisiana Bankers Association
Maine Bankers Association
Maryland Bankers Association
Massachusetts Bankers Association
Michigan Bankers Association
Minnesota Bankers Association
Mississippi Bankers Association
Missouri Bankers Association
Montana Bankers Association
Nebraska Bankers Association
Nevada Bankers Association
New Hampshire Bankers Association
New Jersey Bankers Association
New Mexico Bankers Association
New York Bankers Association
North Carolina Bankers Association
North Dakota Bankers Association
Ohio Bankers League
Oklahoma Bankers Association
Oregon Bankers Association
Pennsylvania Bankers Association
Puerto Rico Bankers Association
Rhode Island Bankers Association
South Carolina Bankers Association
South Dakota Bankers Association
Tennessee Bankers Association
Texas Bankers Association
Utah Bankers Association
Vermont Bankers Association
Virginia Bankers Association
Washington Bankers Association
West Virginia Bankers Association

Wisconsin Bankers Association
Wyoming Bankers Association

Addressing the Gap in Consumer Protection for Small Business Consumers Through a Multiple Method Research Program

CFPB Symposium Report

Glenn L. Christensen
Garrett Research Fellow, Associate Professor of Marketing
Brigham Young University
(g@byu.edu; 801-422-1773)

Sterling A. Bone
Associate Professor of Marketing
Utah State University
(sterling.bone@usu.edu; 435-797-9631)

Jerome D. Williams
Distinguished Professor and Prudential Chair in Business
Rutgers University-Newark
(jeromew@newark.rutgers.edu; 973-353-5541)

Report Overview

For more than a decade we, as academic researchers, have investigated the experience of small business customers seeking financial products for their businesses. We have employed a variety of research methodologies to explore the "lived" experiences of small business owners seeking financing, including matched-paired mystery shopping, video ethnography, depth-interviews, controlled experiments, and surveys. From this research, we show that with limited financial sophistication, entrepreneurial small-business consumers approach the financial marketplace much more like retail financial consumers than sophisticated, corporate customers. Furthermore, we find that the customer service received by these small business customers seeking small business bank loan products is consistently poor and that the actual treatment of racial minority and women-owned small business banking customers is significantly inferior in critical ways. These findings suggest that the playing field for women and minority-owned small businesses is not level and the business and personal outcomes for these individuals and for the economy as a whole is suboptimal.

Small Business Entrepreneurs Need Consumer Protection

Small business loan customers often approach the credit marketplace with similar financial acumen as when they pursue retail, consumer banking products. However, unlike consumers seeking mortgages and consumer credit, the current state of consumer financial protection does not extend a protecting hand to small business banking consumers. The current state of public policy continues to make the assumption that small business-borrowers are more

financially savvy than consumer-borrowers, and thus do not require as broad-reaching protections (Bone, 2006). To illustrate this erroneous assumption, in 2005 we conducted interviews with state and federal banking regulators and discovered a regulatory and consumer protection gap in the policies protecting small business consumers. For example, a State Supervisor of Consumer Credit and Compliance and a FDIC Senior Compliance Officer revealed how consumer protection regulations were note designed for small business consumers.

> "Like I said, they're called consumer protection regulations for a reason— because they protect consumers.... I have this discussion every day with somebody who has a business account and wants me to go after the bank because they do not like how their business account is being handled and I just tell them, "You know what? You are not a consumer; consumer protection laws do not apply. If you don't like what you got from the bank and if you have a contractual agreement, see if they are violating it. And if they are then sue'em! If they're not and you have agreed to it, you've got a contract. You don't like it, go somewhere else." I am very... I don't mean to sound too harsh or hard-nosed, but consumer protection regulations do not apply." (Female – State Supervisor of Consumer Credit and Compliance)

> "To be honest with you, commercial loans, for our purposes, are not... there's not that many issues with them as far as consumer compliance because they're not consumer loans, so it really mitigates our analysis on commercial products.... In essence, the world has decided that the commercial borrower should be savvy by and large.... They ought to know more of the financial aspects. It's [compliance regulations] really protecting the smaller guys. Now that's not to say fair lending is, when you think about fair lending and what that really means, that's the only real criteria that overrides everything. So if they are being treated fairly then they don't need... let's say for a commercial property they don't need a RESPA and all the other consumer-related documents.... The lowest common denominator is a first-time homebuyer; that is why you have all these documents... whereas in commercial, these people know the market, they don't need disclosures, they [the government] are not as worried about the individual being dooped in what they are doing." (Male – FDIC Senior Compliance Officer)

This gap between marketplace policy protections and the lived reality of the vast majority of small business operators sets the stage for small business banking consumers to fall through the regulatory cracks which allows a greater possibility for exploitation and abuse. We have dedicated years of research to understanding the reality and lived experiences of racial minority and women-minority owned business, and how membership in a protected class makes these minority-owned business customers more vulnerable to differential treatment in the marketplace including the entrepreneurial financial products marketplace (Bone, Christensen, and Williams, 2014; Bone et al. 2019).

Goal-Directed Journey and Pre-Application Testing

Think of an entrepreneur deciding to seek funding for her small business. This decision for her is not a discrete or isolated choice but rather an important step necessary to reach other, higher steps within a larger goal-journey. For example, financial goal for her might be to cover

production expansion costs in order to serve more customers thus increasing revenues and profitability. These goals in turn are not isolated choices for our exemplar entrepreneur, but are similarly important steps toward building a successful business, providing for her employees and family, giving back to her community, leaving a legacy for her family, living a life of independence, and experiencing a deep sense of accomplishment and contribution. Thus, the choice to seek financing is an important, even crucial step in a longer life-journey—a means to a much larger and self-defining end.

Zooming in on the life of a consumer who has made the decision to seek financing for her business reveals an involved consumer choice journey which requires a series of behaviors and subchoices that must happen before she can chose to even apply—investigating loan options, finding potential providers and choosing those to include in her final consideration set, evaluating different attributes of loan products and choosing the attributes on which to rely when finalizing choice, identifying loan requirements, collecting relevant information and documentation, and so on.

Thus, experiencing obstacles, roadblocks, or dead ends—even during the early stages of information search for small-business lending—can discourage or derail an entrepreneur's choice-goal to seek funding for business expansion. This in turn may require a painful reworking of her superordinate and self-defining life goals. Given the criticality of early stage preapplication information search, our research has focused on understanding the experiences of entrepreneurs during this important stage of the journey for small business financing.

Matched-Paired Mystery Shopping Studies

Data is a required component in combatting institutional and systematic discrimination, but it is not effective in a vacuum. Matched-pair mystery shopper testing is a valuable investigative tool for uncovering systematic and institutional barriers that raw data and surveys alone cannot detect. The U.S. Department of Justice, the CFPB, and HUD have all used mystery shopping testers to uncover institutional discrimination that exists in consumer lending (CFPB, 2016; U.S. Department of Justice, 2016). However, to date, none of these agencies have attempted to use mystery shopping testing to uncover potential discrimination possibly faced by minority small business entrepreneurial consumers.

In Bone, Christensen, and Williams (2014), we report the results of the first independent study published using a matched-paired method with small business consumers. We compare the experience of mystery shopping Hispanic and Black consumers to white consumers as they visit banks for entrepreneurial, small-business loans. The results unfortunately show that even when white and minority consumers are identical "on paper" (for example, all the consumers in the study wore the same clothes, asked for identical loans for identical businesses and had identical backgrounds—other than their race/ethnicity), they were treated differently by bank loan officers and minorities were treated more poorly than their white counterparts. Unfortunately, minorities were given different information, were asked for more financial and other information, were given significantly less encouragement, and were less likely to get offers to help in the loan application process by loan officers.

In Bone et al. (2019), we conduced additional mystery shopping tests of 17 bank locations in two large metropolitan statistical areas (MSAs) in the eastern United States. These markets were selected by first analyzing the regional demographic composition of each bank's location according to the United States' 2010 Census Data tracts categorized as low, moderate, middle, and upper income as classified under Consumer Reinvestment Act (CRA) guidelines using median family income. We then used CRA data collected by the Federal Financial Institutions Examinations Council (FFIEC) to determine the lending patterns of these banks. This data revealed the number and dollar amount of loans originated to each census tract. This study analyzes interactions amongst branches that have high, moderate, and low levels of spending to those of low-moderate income tracts. We conducted a total of 52 tests (or 26 matched-pairs with one Black tester and one white tester).

Six Black and five white male testers came to the banks with nearly identical business profiles and strong credit histories to inquire about a small business loan product ($60,000 – $70,000 loan to expand their business and to possibly hire a part-time employee). The profiles of the test and control groups were sufficiently strong such that on paper, either profile would be very likely to be approved for a loan. We designed the profiles for both the protected and control testers to be well above the threshold of what is acceptable loan requests, however, we purposefully designed the qualifications of Black testers to be superior to the qualifications of the white testers. In other words, on paper the protected, Black, tester was financially better off than the control, white, tester. Thus, one would hope for the experience of Black testers to be more positive, or at the very least, equal to the experience of the white testers. This makes this study a conservative test for the presence, if any, of disparate and discriminatory treatment in the test condition.

The results show that Black testers were asked to provide more information about their businesses and personal financials than white testers ($\chi^2 = 17.25$; $p = .01$). Specifically, compared with the white testers, Black testers were more frequently requested to provide the information of their business financial statements (73.1% vs. 50.0), the amount of their accounts receivable (11.5% vs. 0.0), and their personal W-2 forms (30.8% vs. 0.0%). In addition, we identified a troublesome pattern of loan officers inquiring about marital status. Asking about marital status as a determination of credit worthiness is a direct violation of fair lending law (15 USCS § 1691). We found that Black testers were asked if they were married (marital status) (M = 23.1%) significantly more frequently than compared to white testers (M = 3.8%; $\chi^2 = 4.13$; $p = .04$). In addition, Black testers were asked about spousal employment status (M = 11.5%) significantly more frequently than compared to white testers (M = 0.0%; $\chi^2 = 3.18$; $p = .07$). The similar test and control profiles are created in a manner that should result in a loan approval based solely on the income of the tester alone. There would be no reason or need to incorporate a spouse's income into the credit worthiness decision-making process. Furthermore, only the Black testers where asked if their spouse is employed. The results also reveal differences in the level of assistance and encouragement offered to the Black testers ($\chi^2 = 9.43$; $p = .05$). Compared with their white counterparts, Black testers were less frequently offered a future appointment (11.5% vs. 23.1%), offered help to complete an application (11.5% vs. 26.9%), thanked for coming in (80.8% vs. 96.2%), and asked how they can help (92.3% vs. 100%).

Racial Homophily Test

A critique and limitation of these results is whether the race and gender of the bank employee influence the treatment that testers experienced, and if so, how? To address this limitation, we recently conducted (in 2018) a matched-paired mystery shopping test in the Los Angeles metropolitan statistical area where we tested whether the racial homophily—or similarity of bank employee race and the tester race—further investigates the differences we encountered in our earlier work. Consistent with the earlier tests we again found differences across the testers, including in the information that was required to make application for a small business product (see Figure 1). Minority customers were statistically more likely to be asked for personal financial information than their white counterparts.

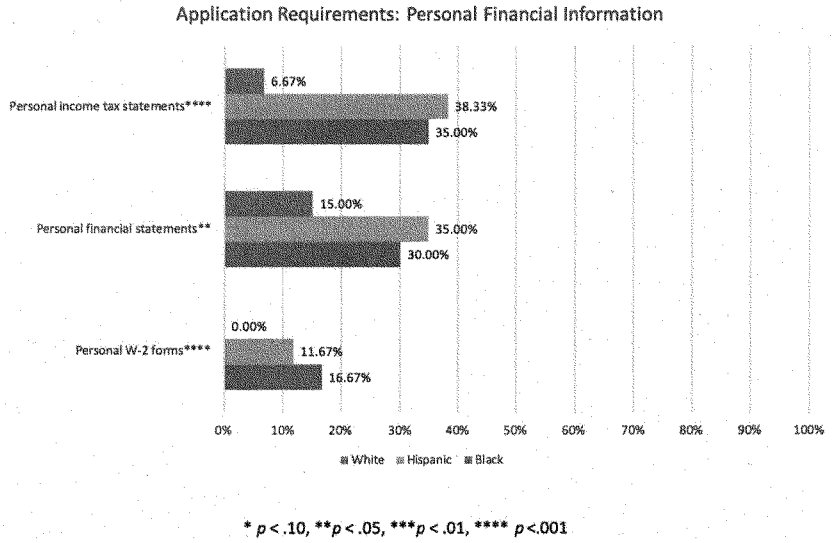
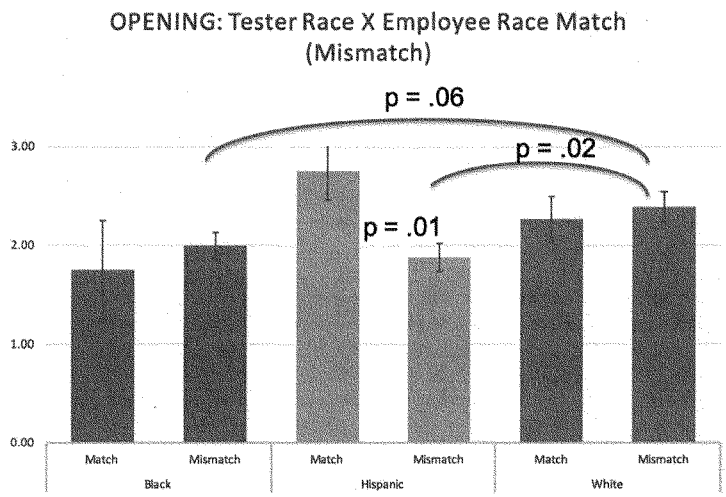


Figure 1: Application Requirements - Personal Financial Information (LA 2018)

To expand understanding regarding the impact of racial homophily, we compared interactions where tester and employee race matched or was unmatched and found significant differences in two experiences, the opening of the encounter (e.g. asking and using the name of the tester) and the closing of the encounter (e.g., offering the tester an application). Consistent with racial homophily, Hispanic testers received a better opening experience when they were served by a Hispanic bank employee (see Figure 2). When Hispanic and Black testers were served by someone that was of a different racial background from them, each received a poorer opening experience than when White testers were served by someone that was non-White.

Turning to the closing experience and comparing within race, Hispanic testers received a better closing experience when served by a Hispanic bank employee (homophily) than when they experienced a race mismatch. Finally, during the closing experience, Hispanic testers served by Hispanic bank officers received a better closing compared to Black testers *and* White testers served by a bank employee that was of their same race.

Figure 2: Opening - Racial Homophily (LA 2018)



Narrative Analysis

In addition to analyzing the data using empirical quantitative methods, we collected detailed narratives from each test. In these narratives the tester was asked to describe each of the actors (e.g. bank employees) involved, the detailed events of their interaction and the conversation and discourse they experienced during their time in the bank. Comparing the narratives of the Black testers to the white narratives revealed that Black testers experienced micro-aggressions along with the disparate treatment they received. Victims of consumer discrimination bear a psychological burden as a result of overt and subconscious discrimination. Because consumer discrimination occurs in everyday situations, it constitutes the kind of micro-aggressions that can have cumulative debilitating effects over the course of a person's lifetime. For example, we found that on multiple occasions the loan officer during their visit with Black

testers went to a government website listing all registered businesses to verify if the minority tester's business was registered and in good standing. This did not occur for any white tester.

Analyzing the narratives of matched-paired tests to the same bank location revealed other types of micro-aggressions experienced and reported by Black testers. For example, while both testers lived about an hour from the bank branch, it was suggested to the Black tester to visit a bank branch closer to his home, while the white tester was told that the business specialist is not in and offered to set up a meeting for the next time the business specialist is available. Another example that occurred is of a matched-pair where the tester met with the same loan officer on the same day. Both testers were asked about the location of their business which—according to the scenario they were trained on—about an hour away from the bank. In this incident, the Black tester was then asked why he was in area and he responded, as directed, by saying that he was in the area to meet with a potential client. On the other hand, the white tester was not asked this question.

Conclusion and Recommendations

Access to capital for a small business is critical for growing and accumulating wealth for all consumer groups, regardless of race. However, access can be hindered or frustrated in the early steps of a consumer's journey seeking small business banking products. The availability of data and information along the consumer's journey to access capital is of paramount importance if markets are to improve for all consumers. Based on this research, we conclude and give our support for Section 1071 of the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) (Pub. L. 111-203, H.R. 4173) which requires financial intuitions that engage in small business lending to report their lending activities with the same transparency already required of home mortgage lending sector.

We are convinced of the power of data to enlighten and illuminate. The data we have personally gathered and published demonstrates the power of data to highlight inequities and disparate customer treatment in the small business lending marketplace. Our findings have shown that for all entrepreneurs, it is difficult journey to obtain financing for their ventures. For minority entrepreneurs especially, this journey is not across a level playing field. Rather it is an uphill journey where they encounter obstacles in their path that their white counterparts simply do not experience as often—if they experience them at all. Even when in our data collection, we "tilted the scale" in favor of minority testers, the data showed that better financially qualified, minority small-business applicants encountered difficulties not experienced by majority testers. These data show that in the small-business lending marketplace, we are simply not there yet.

For these reasons, we support greater data gathering among policy-makers to create increased transparency in the marketplace. Transparent markets allow light to highlight and expose inequities and areas of disparate treatment among marketplace participants. In our view, the potential costs of reporting the data called for in Section 1071 are far outweighed by the illumination and marketplace transparency those data have the power to provide. At the same time, there is a cost to not collecting and reporting these data. That cost, currently incurred, is an unclear and uninformed understanding of the full width and breadth of the small-business lending landscape. In our view, greater access to data will allow citizens and policy-makers

increased insight to make informed, data-driven decisions as to policy in this economically vital marketplace.

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Via Electronic Submission

January 6, 2022

Comment Intake—Section 1071 Small Business Lending Data Collection
Bureau of Consumer Financial Protection
1700 G Street NW
Washington, DC 20552

RE: [Docket No. CFPB-2021-0015] — Small Business Lending Data Collection Under the Equal Credit Opportunity Act (Regulation B)

Dear Sir or Madam:

The Independent Community Bankers of America ("ICBA")[1] welcomes the opportunity to comment on the Consumer Financial Protection Bureau's ("CFPB" or "Bureau") Proposed Rule on Small Business Lending Data Collection ("Proposal"). Among other requirements, Section 1071 of the Dodd Frank Act requires financial institutions ("FIs") to collect certain data regarding applications for credit from women-owned, minority-owned, and small businesses, and to report that data to the Bureau on an annual basis. While ICBA firmly supports the intention behind the Proposal and the desire to expand access to credit for minority-owned, women-owned, and small businesses, we remain deeply concerned that the proposal's overly broad coverage will uniquely disadvantage the business customers of community banks.

Specifically, we believe that the Proposal will threaten the privacy of small business customers, increase the cost of credit, discourage "loan shopping" for the best product, increase

[1] *The Independent Community Bankers of America® creates and promotes an environment where community banks flourish. ICBA is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education, and high-quality products and services.*

With nearly 50,000 locations nationwide, community banks constitute roughly 99 percent of all banks, employ nearly 700,000 Americans and are the only physical banking presence in one in three U.S. counties. Holding nearly $5.9 trillion in assets, over $4.9 trillion in deposits, and more than $3.5 trillion in loans to consumers, small businesses and the agricultural community, community banks channel local deposits into the Main Streets and neighborhoods they serve, spurring job creation, fostering innovation and fueling their customers' dreams in communities throughout America. For more information, visit ICBA's website at www.icba.org.

compliance costs, and most unfortunately – erode the customized, relationship-banking model in which community banks take pride.

GENERAL COMMENTS

Small business lending is complex and cannot be "commoditized" in the same way as consumer lending. Each small business loan has customized terms based on an analysis of numerous factors. Complex lending should not be subject to simplified, rigid analysis, which might give rise to unfounded fair lending complaints. For this reason, the proposed rules under Section 1071 will have a chilling effect on community banks' ability to price for risk, unless the Bureau can properly tailor a rule that excludes community banks from coverage.

The application of this consumer protection law is grossly incongruous with the underlying nature of small business lending. Unlike consumer loan products, such as mortgages and credit cards, small business loans are non-homogenous and do not lend themselves to standardized recordkeeping or comparative analysis.

EXECUTIVE SUMMARY

As explained more fully below, ICBA has the following main concerns and recommendations.

1. The smallest community banks will inappropriately be covered by the scope of the rule.
   The CFPB should exclude community banks with assets of $1.3 billion or less from coverage. By providing partial or full exemption from this rulemaking, the Bureau will still overwhelmingly meet the objectives of the law while mitigating the associated costs.

2. The Proposal's coverage of nearly every existing business will disproportionally increase the cost of, and decrease access to, credit for truly small businesses.
   The CFPB should define a "small business" as a business with gross annual revenue of $1 million or less.

3. Nearly doubling the number of data points will greatly increase the burden of complying with the congressional intent of the law while also increasing the threat to small business applicants' privacy.

The final rule should only require the collection and reporting of statutorily mandated data points.

4. The Proposal will unnecessarily risk the privacy of small business applicants.
The CFPB should publish a full privacy balancing test after one year's collection of data and provide an opportunity for notice and comment before determining which data to make public.

5. Community banks will not have ample time to comply in good faith with this rule.
The final rule should provide at least three years for FIs to comply, or in the alternative, stagger the implementation dates based on asset size.

6. The firewall requirement cannot feasibly be met by community banks, and the proposed solution will create a chilling effect for community banks, granting larger FIs and fintech companies a competitive advantage.
The inability to firewall information is additional justification to exclude smaller, federally supervised FIs from this rulemaking. Alternatively, the CFPB should establish a platform where applicants can anonymously input their demographic information for all FIs.

7. Compliance with this rulemaking will be an entirely new environment for many community banks.
While ICBA supports the proposed safe harbors and allowance that bona fide errors are not Equal Credit Opportunity Act ("ECOA") violations, ICBA recommends that the Bureau additionally provide for a 12-month grace period after the compliance date.

8. Though recordkeeping is a necessary part of any data collection rulemaking, it will nonetheless prove difficult for many community banks.
ICBA recommends that the Bureau provide banks with options to report annually or as loan applications are received.

9. Verifying small business applicant information presents additional burdens beyond the mere collection of information.
Though ICBA welcomes the Bureau's proposal not to require FIs to verify applicant-provided information, ICBA urges the Bureau not to require FIs to provide separately verified information.

SECTION-BY-SECTION COMMENTS

1) A coverage threshold of $1.3 billion for federally supervised FIs would collect information for more than 90 percent of all business loans made.

The Proposal defines a "Financial Institution" as "any partnership, company, corporation, association (incorporated or unincorporated), trust, estate, cooperative organization, or other entity that engages in any financial activity."[2] This is a broad definition which covers any bank, credit union, financial technology company, or non-bank lender that is engaged in small business lending. We believe the breadth of this definition is appropriate because it tends towards regulatory parity for larger participants in the small business lending market, regardless of what type of business form they take. **We recommend the adoption of this proposed definition without revision**.

By contrast, we strenuously object to the proposed §1002.105(b), which defines what constitutes a *covered* financial institution, and therefore determines the scope of the rule. **The rule proposes to cover any FI that "originated at least 25 covered credit transactions for small businesses in each of the two preceding calendar years."**[3] In other words, any FI that originated fewer than 25 covered small business loans in the two preceding calendar years is exempt from the rule. **This exemption threshold is inappropriately low; and if §1002.105(b) is implemented as proposed, it will almost certainly raise the cost of credit for the small business borrowers that Section 1071 is designed to protect, as thousands of small lenders would be forced to shoulder the significant compliance costs associated with a major new data collection requirement.**

We have heard from the smallest community banks in the country, and there is significant consternation about the collection and reporting requirements of this rule. Our analysis of publicly available Call Report data substantiates this concern. **If the proposed 25 loan threshold is finalized, we conclude that at least 780 banks with less than $100 million in assets will be subject to the rule,**[4] **yet would only provide an incremental increase in the number of business loans reported. For context:**

- **the average bank of less than $100 million in assets has 13.1 employees working at 1.6 branches.**

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[2] 86 Fed. Reg. 56577.

[3] *Id.*

[4] Based on analysis of the number of "loans to small business" reported on Schedule RC-C, part II of the Call Report in the four quarters ending with Q3 2021, this category includes "loans secured by nonfarm nonresidential properties" and "commercial and industrial loans" in amounts less than $1 million. While this is not a perfect match for the requirements of Section 1071 because borrower revenue is not reported (no such data is currently reported), we believe it is a sufficiently close proxy to demonstrate the broad scope of the proposed rule.

- Banks below $200 million in assets have an average 20.8 employees at 2.2 branches.
- Banks below $750 million in assets have an average of 36.4 employees at 3.4 branches.

To reiterate, the final rule should capture the supermajority of the number of small business loans – more than 90 percent of the market – that burdens the fewest number of community banks.

a) Asset-Based Thresholds

We urge the Bureau to exempt all community banks with less than $1.322 billion in assets, which is the current threshold used by the FDIC, the Federal Reserve Board, and the Office of the Comptroller of the Currency to define a "small bank" in the agencies' Community Reinvestment Act ("CRA") regulations.[5] This threshold is currently recognized by federal banking regulators and within the banking industry as a delineating line between small banks and larger banks with increased compliance capacity and regulatory obligation. Using the CRA threshold would also focus the rule on those banks that already have more advanced compliance systems, particularly for data collection, as the result of their coverage under CRA.

Alternatively, we propose that the Bureau exempt all community banks defined as small businesses under the Small Business Administration's North American Industry Classification System ("NAICS") size standards. Currently, that threshold is set at $600 million in assets.[6] According to the regulations, "SBA's size standards define whether a business entity is small and, thus, eligible for Government programs and preferences reserved for 'small business' concerns."[7] Because Section 1071 is a law designed to protect small businesses, the CFPB should not implement regulations which substantially burden banks below $600 million in assets and are themselves legally defined as small business concerns.

Either of these thresholds would burden many fewer banks than the proposed rule – without substantially altering the data on small business lending reported to the government. **Based on the Call Report data, if the $1.322 billion exemption threshold is used, the CFPB will collect data on 91.27% of all small business loans made by banks.** The actual percentage of small business lending data collected will likely be even greater because the Bureau is also proposing to collect data from non-bank lenders. **If the $600 million threshold is used instead, the CFPB will capture 95.78% of small business lending data.**

[5] 12 CFR 345.12; 12 CFR 228.12; 12 CFR 25.12.
[6] 13 CFR 121.201.
[7] 13 CFR 121.101.

To subject thousands of additional small depository institutions to a complex and costly rule to collect data on 4.22% of the small business lending market is unreasonable. If the exemption threshold is not raised, this rule will harm small lenders and their borrowers. It will lead to additional compliance costs which the smallest lenders will disproportionately bear and be forced to pass on to customers. It will drive consolidation in underserved and rural areas as lenders clamor for economies of scale. It will lead some banks to scale back or discontinue small business lending. The proposed rule, with its capriciously low exemption threshold, favors large institutions with large compliance teams and has a disproportionate negative impact on small lenders that genuinely understand their communities and local small businesses. **The exemption threshold must be raised to prevent these highly foreseeable negative effects.**

b) Volume-Based Threshold

We do not favor the use of a volume-based threshold for depository institutions and instead favor an asset-based threshold. In general, an asset-based threshold is a better solution because lending volume can vary from year to year, leading to potential uncertainty about whether the bank must comply, or to situations where a bank vacillates between being a covered FI or an exempt one from year to year.

While bank assets can also vary, once a bank crosses an asset threshold, it is less likely to cross below it in subsequent years. Additionally, because banks can forecast when they are likely to surpass an asset threshold well in advance, they are better able to plan and budget for the necessary investments in software, training, and personnel in advance of required compliance.

Community banks are not the "Too Big To Fail" Wall Street banks with compliance staff numbering in the thousands. They are small, locally owned, and locally managed institutions, with a of employees. Many of these employees perform multiple roles within the bank and are already responsible for complying with a myriad of complicated regulations.

The CFPB's proposal is in excess of 200,000 words and fills 251 pages in the Federal Register. Given the complexity of the issue and of the federal rulemaking process, this may be an appropriate length, and we appreciate the depth of the Bureau's analysis. Nevertheless, the reality is that the proposed rule is a massive document that will create significant and ongoing compliance burdens for covered FIs. For community banks, this burden will be particularly onerous and costly, and it may force some institutions to recoup those onerous costs by assessing additional fees to small business borrowers or scale back or eliminate their presence in the small business lending market.

Therefore, in the strongest possible terms, we urge the CFPB to exercise its statutory authority to exempt small community banks from compliance with this proposed regulation.[8] The CFPB is proposing to utilize this authority to exempt FIs which make less than 25 loans. We oppose this threshold and instead, urge the CFPB to implement an asset-based exemption threshold for small banks. An asset-based exemption is less prone to annual fluctuation than an activity threshold and would allow the Bureau to align its regulations with existing regulatory requirements.

If the Bureau opts to use a volume-based threshold for FIs, we must renew our objection that the proposed threshold of 25 is too low. It would require compliance by many of the smallest banks in America. We recommend a 1,500-loan exemption threshold. This threshold would exempt an average community bank with less than $750 million in assets, while still collecting more than 90% of small business lending data.

c) FI Characteristics

Apart from using asset size or loan volume to determine the rule's coverage, ICBA recommends that the Bureau also consider the underlying characteristics and activities of the FI. Specifically, ICBA recommends that the Bureau provide partial or total exemption for FIs that are (1) community development financial institutions ("CDFI"), (2) Minority Depository Institutions ("MDI"), or (3) located in rural areas or underserved areas.

i) CDFI

CDFIs, accredited by the U.S. Department of the Treasury, are FIs that are committed to community-focused lending but have difficulty raising the capital needed to provide affordable financial services. Among other requirements, a FI with a CDFI designation must demonstrate and prove that it: (1) has a primary mission of promoting community development, (2) primarily serves a target market, such as a predominantly low-and-moderate income ("LMI") community, and (3) maintains accountability to that target market.

The Bureau decided to exempt CDFIs when implementing the Qualified Mortgage ("QM") rule, finding that CDFIs that provide mortgage loans generally employ underwriting guidelines tailored to the needs of LMI consumers.[9] In providing this exemption, the Bureau explained

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[8] *See* 12 USC 5512(b)(3), which gives the CFPB authority to "unconditionally exempt any class of covered persons ... from any provision of this title, or from any rule issued under this title, as the Bureau determines necessary or appropriate to carry out the purposes and objectives of this title." This provision unambiguously gives the CFPB the authority to exempt community banks below a designated asset threshold if the Bureau conducts a cost-benefit analysis and concludes that the cost to community banks and their customers outweigh the benefits of requiring community banks to comply.

[9] 78 Fed. Reg. 35464

that because CDFIs are more likely to consider non-standard factors and do not typically underwrite to industry-wide standards, that they can better account for the unique credit characteristics of LMI consumers.

At the time, the CFPB exempted CDFIs because LMI consumers "have difficulty obtaining responsible and affordable credit, and that the burdens imposed by the ability-to-repay requirements would significantly impair the ability of these creditors to continue serving this market."[10] The same logic would hold here if the Bureau were to exempt CDFIs from coverage under a 1071 rule. CDFIs should not be additionally burdened by complying with this rule when they are already serving LMI populations. They already document many of the data points being proposed, and if the Bureau does not provide whole exemption, then partial exemption from redundant data points would be prudent.

ii) MDI

MDIs were designated under the Financial Institutions Reform, Recovery, and Enforcement Act ("FIRREA"), when Congress recognized that minority banks can play an important role in serving the financial needs of historically underserved communities and minority populations. The Federal Deposit Insurance Corporation ("FDIC") defines an MDI as any federally insured depository institution for which 51 percent or more of the voting stock is owned by minority individuals or a majority of the board of directors is minority, and the community that the institution serves is predominantly minority.

Since Congress has determined that MDIs already play an important role in serving underserved communities and minority populations, the intent behind Section 1071 is already met by MDIs, and therefore, should not redundantly be applied to this special class of FIs. As such, ICBA urges the Bureau to exempt MDIs from the 1071 rule's coverage.

iii) Rural and Underserved Areas

The Bureau should exempt small lending institutions and those operating entirely outside of metropolitan statistical areas ("MSA"), such as community banks that operate in rural or underserved areas. This exemption would mirror the Home Mortgage Disclosure Act's ("HMDA") exemption for similarly situated banks.[11] Exempting these community banks from

[10] 78 Fed. Reg. 35464
[11] 12 CFR 1003.2(g)(1)(ii)

coverage would simplify and maintain congruency between Section 1071 and HMDA. Ultimately, no regulatory compliance is costless, and if these community banks are not exempted from Section 1071, those costs will be passed on to business borrowers. In some cases, this increase may make loans unaffordable and reduce access to credit.

2) While ICBA welcomes the use of Gross Annual Revenue as the determining factor of covered business applicants, the threshold should be $1 million rather than $5 million.

Though the statute uses section 3 of the Small Business Act to define a small business, the CFPB proposes to use a business's gross annual revenue ("GAR") to determine which businesses are covered by the law. The Bureau believes that using a GAR threshold to define a "small business" would facilitate compliance for FIs applying "a simple, broad definition...that would be practical...in the market."[12] The Bureau proposes to define the term as a business with gross annual revenue the preceding fiscal year of $5 million or less.

ICBA supports the Bureau's approach and agrees that using the bright line of a business's GAR is a convenient way for a bank to quickly determine whether an applicant will be covered by the rule. It is an efficient way for banks to comply. ICBA supports adopting a definition that is less complex than Small Business Administration's ("SBA") size standards based on 6-digit NAICS codes. However, ICBA does not support the proposed GAR threshold of $5 million, but instead, urges the Bureau to use a $1 million threshold, which will streamline compliance, cover the vast majority of businesses, and correspond to the public's general understanding of a "small business."

a) A $1 million threshold promotes simplicity and ease of compliance.

As part of its justification for setting a $5 million GAR threshold, the Bureau notes that larger FIs categorize loans made to businesses based on GAR, with loans to businesses up to $5 million categorized as small/retail customers. If the Bureau was willing to limit the coverage of this rule to those larger FIs, then perhaps a $5 million GAR threshold would be appropriate. However, since the Bureau is proposing to cover smaller FIs, then consideration of how larger FIs treat small business loans should not bear weight on regulations applying to community banks.

Instead of considering how larger FIs categorize their commercial lending, the Bureau should review existing regulations that use a $1 million threshold and align 1071's definition with those requirements. For example, Regulation B uses a $1 million GAR threshold to determine how a bank provides adverse action notifications to business applicants,[13] and CRA regulations use a

[12] 86 Fed. Reg. 56426
[13] 12 CFR 202.9(a)(3).

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

$1 million GAR threshold to determine which commercial loans meet community development loan requirements.[14]

In this analysis, the Bureau rightly focuses on ease of compliance, certainty of coverage, and bright-line assessments. The Bureau should truly prioritize these attributes and create a bright-line GAR of $1 million – in large part, due to the reasons laid out above. It is a threshold that is already widely understood and accounted for by community banks. Existing regulations already hinge on the $1 million GAR threshold. Creating a new "small business" threshold standard will almost certainly create confusion and difficulty with compliance, thus undercutting the benefits the Bureau outlines above.

b) A $1 million GAR threshold covers the vast majority of all businesses.

ICBA contends that not only does a $1 million threshold cover **most small businesses**, but a $1 million definition covers nearly **every business**, which should be more than sufficient to meet Congressional intent.

From the 2012 Census Survey of Business Owners, cited in the Bureau's own research on setting an appropriate threshold, approximately 95 percent of all businesses had less than $1 million in annual revenues.[15] Roughly, 97.7 percent of all minority-owned businesses and 98.3 percent of all women-owned businesses were similarly under $1 million in annual receipts.[16] A portion of this is worth emphasizing – a $1 million threshold would cover 95 percent of **all** firms, not just "small" ones. This context is important when considering the common usage and understanding of "small" businesses, which is discussed below.

c) Common usage of a "small business" implies a GAR of $1 million or less.

Apart from the simplicity and ease of compliance of using a $1 million threshold, the common understanding of a "small business" is one with revenues under $1 million. According to a research poll, commissioned by ICBA and conducted by Morning Consult, nearly 90 percent of respondents indicated that a "small business" is one with GAR of $1 million or less, with the

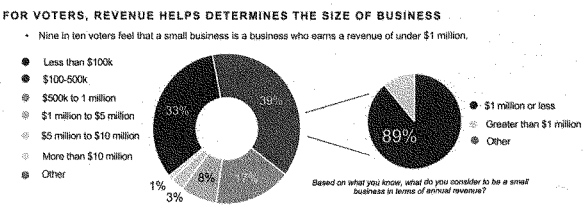
[14] 12 CFR 25.12(g)(3); 12 CFR 195.12(g)(3); and 12 CFR 228.12(g)(3).
[15] U.S. Census Bureau, Statistics for All U.S. Firms with Paid Employees by Industry, Gender, and Employment Size of Firm for the U.S. and States: 2012 More Information 2012 Survey of Business Owners, American Fact Finder, (last visited Feb 27,2017), available at http://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=SBO_2012_00CSA09&prodType =table/.
[16] *Id.*

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

vast majority of respondents indicating that a small business is one with less than $500,000 in revenue.[17]



As several consumer groups noted in response to the Small Business Regulatory Enforcement Fairness Act ("SBREFA") Outline, the Bureau must align its definition of a "small business" with congressional intent. Although the Bureau is not using the exact definition prescribed in the statute, its approach to use a simple revenue threshold should be lauded, but only as far as it retains a semblance to the general understanding of a "small business." As it deviates further from the common usage of the term "small business," the Bureau tacks father from congressional intent. Indeed, by setting a threshold that covers nearly *every* business, let alone "small," the Bureau diminishes the importance that Congress placed on the modifier "small."

d) Small farm and agricultural loans should be exempt from coverage.

ICBA recommends that the Bureau exclude small farm and agricultural loans from coverage. Not only is it unlikely that Section 1071 was enacted to cover small farm and agricultural lending, but their underwriting criteria are distinct and different from small business loans. The distinction is already codified in several laws and regulations. For example, the definition of small business loans and small farm loans under CRA have two different definitions, revealing the distinction between the two. HMDA also exempts rural lenders located in nonmetropolitan areas.

Because large banks often do not engage in significant agricultural lending, community banks are often the only option for small farms. If the burden of Section 1071 compliance forces small lenders to reduce their lending below the exemption threshold it may limit the access to credit

[17] This poll was conducted between November 1st and November 4th, 2021 among a national sample of 1996 voters. The interviews were conducted online, and the data were weighted to approximate a target sample of voters based on age, gender, educational attainment, race, and region. Results from the full survey have a margin of error of plus or minus 2 percentage points.

for these agriculture businesses unless farm loans are exempted from coverage under the definition of "small business."

3) The CFPB should limit the compilation of reportable data to that which is required by statute.

Although the statute requires FIs to "compile and maintain" records of information provided by applicants on enumerated data points,[18] the Bureau is using its authority[19] to require additional data points that the Bureau determines would aid in fulfilling the purpose of [section 1071] (hereinafter, "discretionary data points").

The Bureau is proposing to require collection and reporting of discretionary data points that it considered in the SBREFA Outline, including pricing, time in business, NAICS code, and number of workers. Further, the Bureau is proposing several additional discretionary data points that were not considered in the SBREFA Outline nor discussed among small entity representatives ("SERs"), including application method, application recipient, denial reasons, and number of principal owners.

While ICBA supports the Bureau's goal of eliminating illegal discrimination, we are concerned that many of the discretionary data points, such as number of workers, the application method and recipient, are not currently collected by community banks and will be an entirely new burden for them. Not only are many of these discretionary data points not relevant to creditworthiness, ICBA is concerned that the inclusion of these data points will increase the occurrence of misinterpretations or incorrect conclusions drawn from the data. If the Bureau is concerned about fair lending violations, then it should acknowledge that the prudential banking agencies conducting fair lending exams have the majority of these data points, along *with* the contextual information that would correct for otherwise erroneous conclusions. Community banks are already examined for compliance with fair lending laws – the collection of all these data points duplicates, or worse usurps, those prudential agency efforts.

Further, given the unprecedented nature of this regulation, it is uncertain whether the burden of collecting this new information will provide the benefit that the Bureau anticipates. If the Bureau opts to require some or all of the proposed discretionary data points, then ICBA urges

[18] Section 704B(e) of the Equal Credit Opportunity Act ("ECOA").
[19] Section 704B(e)(2)(H) of ECOA.

the Bureau to consider partial collection of data for community banks and other, similarly small FIs that are least likely to afford the additional burden that such collection would create. Requiring all 21 proposed data points for only the largest FIs would provide a mechanism for the Bureau to establish a baseline of data that could better inform future efforts to decide whether greater coverage or applicability to smaller FIs is warranted.

The cost of collecting and reporting the data points will include expensive data quality scrubs to avoid negative examination findings, costs that will be disproportionately borne by smaller FIs, such as community banks.

Given that much of this data is not currently collected by community banks, there are concerns that compliance with this rule will require the standardization and homogenization of small business lending, which is anathema to the customized and relationship-based lending for which community banks are valued. While some FIs already automate and standardize their small business lending departments, community banks will be left with a choice: standardize their small business lending to comply with this proposed rule or incur disproportionate costs to continue their customized and relationship-based approach.

Distinct from larger market participants that base their business models on scale and repeatability, community banks are relationship lenders. Community banks design products and services that are tailored to their small business customers' needs. These unique products and services are near-impossible to standardize, but they are often the only product or service available to small businesses – especially the small businesses that are most vulnerable and in need.

If all the proposed data points are uniformly required of all covered FIs, then many community banks will be forced to choose the standardization route. This harms community bank lending, but it most harms the small businesses that most benefit from the high-touch, relationship-based lending that community banks offer.

a) Ethnicity, Race, and Sex of Principal Owners

The Bureau is proposing to require FIs to collect and report the ethnicity, race, and sex of the applicant's principal owners as well as whether this information is being reported based on previously collected data. It is also proposing to require FIs to conduct a visual observation or surname analysis to determine the race and ethnicity of an applicant who declines to respond to the collection request. Proposed appendix G would include a requirement that a FI inform an applicant that the applicant is not required to respond to the FI's questions regarding its principal owners' ethnicity, race, or sex.

ICBA notes that the visual observation and surname analysis for applicants that do not self-report is one of the most controversial provisions of the proposed rule. We strongly recommend that the Bureau rescind the proposed requirement to conduct a visual observation and surname analysis, and instead, implement the approach that was contemplated in the SBREFA Outline.

Specifically, the Bureau should require that the collection and reporting of the race, sex, and ethnicity of small businesses' principal owners be based solely on applicant self-reporting. If an applicant provides a principal owner's race, sex, or ethnicity, the FI would report this information and would have no obligation to verify it.

Not only would this proposed requirement be extraordinarily uncomfortable for the bank employee conducting the visual observation, but it would be in direct contradiction to the applicant's wishes not to identify their race or ethnicity. This right is clearly stipulated in law, and the Bureau's proposed requirement would be an end-run around that right.

Further, and as noted in the SBREFA Outline, requiring reporting based on visual observation or surname could create unwarranted compliance burdens in the context of small business lending. These burdens may include the costs to create and maintain policies and procedures; costs of applying such policies and procedures in a consistent manner; costs to conduct ongoing training; and costs to audit compliance.

Finally, if the public is going to rely upon this dataset for policy decisions and a better understanding of the market, then the Bureau should do its best to ensure that the data is accurate and not subjective. Including guesses and hunches in a dataset do not lead to sound conclusions. ICBA strongly urges the Bureau to rescind its proposed requirement for banks to conduct visual observations and surname analyses of applicants.

The CFPB should allow for self-identification and not require FIs to supplant applicant wishes with their own guesses. Instead, if response rates to demographic inquiries are so low due to fear of discrimination, a better method of gathering data would be to provide the applicants with an online portal to self-identify that ensures their demographic anonymity (discussed further, below, in the firewall section).

b) Pricing Information

Also not required by statute, the CFPB is proposing to require FIs to report:

(1) the interest rate that is or would be applicable to the covered credit transaction;

(2) the total origination charges for a covered credit transaction;

(3) the broker fees for a covered credit transaction;
(4) the total amount of all non-interest charges that are scheduled to be imposed over the first annual period of the covered credit transaction;
(5) the difference between the amount advanced and the amount to be repaid for merchant cash advances; and
(6) information about any prepayment penalties applicable to the covered credit transaction.

The Bureau is proposing to include these discretionary data points because it believes that heightened risks to fair lending and small business development may arise from different pricing for the same products and the selective marketing of higher-priced or even predatory and unsustainable products.

ICBA has an issue with these proposed data points on two fronts discussed more fully below. First, though different pricing for the same products may evidence predatory or discriminatory lending, the proposed data points will not be gathering pricing for the same products. Second, pricing will not accurately capture the ancillary products and services that community banks offer to their customers, where a pricing premium is acceptable for the higher quality product and services.

i) Comparison of heterogeneous commercial products will not yield significant findings.

The Bureau believes pricing data are important because the statutory data points alone offer: (1) limited insight into underwriting disparities and (2) no insight into predatory prices or pricing disparities. The Bureau notes that pricing data in HMDA has been critical in identifying disparate pricing among protected classes.

However, instead of giving the Bureau and researchers the data set to make statistically sound findings, the collection of pricing information is much more likely to increase unsound findings and allegations. Pricing could be publicly reported with the assumption that like products are being compared against other like products, but without contextual information that would explain the pricing variations due to factors such as the nature of the collateral, credit scores, size of down payment, compensating deposit balances, bundled services, etc.

Unlike other types of consumer credit, each small business has its own distinctive characteristics with unique credit needs. Existing business lending practices do not conform to a standard data collection practice and would require extraordinary change to comply. Unlike the residential mortgage market, where there is a standard portfolio of products, each small

business is different from others, each has its own needs, and as such, each small business loan is similarly distinct from other small business loans.

Discerning discrimination based on pricing for consumer products is a much more established and tenable proposition. There are many fewer variables, and the market has largely been homogenized and standardized through a robust secondary market. Such a market does not exist to the same degree for commercial lending. ICBA is concerned that efforts to collect pricing data, as well as several other data points in this proposal, will push the industry in that direction. Thus, the customized, high-touch relationship bank model that community banks offer will be eradicated.

ii) Pricing premium data point would not reflect small business customers' preference for community banks.

Apart from providing credit to their small business customers, community banks overwhelmingly provide valuable ancillary services to their customers, such as acting as advisor or consultant. For example, community banks often know commercial zoning laws in their local community just as well as an official at city hall. They have the familiarity and local knowledge that is unparalleled, and small business customers depend on and benefit from that knowledge. As such, pricing data from a community bank may appear inflated when compared to other FIs, but that price premium includes these ancillary services. This is a data point, that like many other discretionary data points proposed, will lead to erroneous conclusions.

Apart from ICBA's objection to including pricing terms as a data point, ICBA stresses that the Bureau should eliminate pricing data points that are uniformly assessed to all credit applicants, or fees assessed from third parties. For example, if all applicants are charged a $50 annual fee or 0.25 percent broker fee, there is no disparate allocation of those fees, and as such, would not aid the Bureau or the public in determining fair lending violations. Therefore, if certain pricing data will not be useful toward the Bureau's goals, then it should not be collected.

c) NAICS Code

Even though it is not required by statute, the Bureau is proposing that FIs collect and report an applicant's 6-digit NAICS code. ICBA objects to the inclusion of this data point. Not only is it not required by statute, but it does not provide information that would inform fair lending scrutiny. Further, many community banks have expressed an unfamiliarity with NAICS or do not currently collect it - this would be an additional burden placed upon them.

The Bureau cites the identification of high-risk industries, such as those with high rates of businesses leaving the market or that deal primarily in cash transactions, as potential evidence

in determining fair lending violations. The Bureau should acknowledge that these decisions are indicative of risk tolerance – not of fair lending violations. Collecting this information could present disparities of lending to industries, but it would not portend disparate treatment of protected classes of borrowers.

Separately, and as discussed below, the combination of NAICS code with statutorily mandated data points is the most significant risk to customer privacy.

d) Application Method

The CFPB is proposing to require FIs to collect and report application method or the means by which the applicant submitted the application to the FI. ICBA strongly opposes this proposed requirement. Not only is this data point not mandated by statute, but it was also not considered in the SBREFA Outline and was only requested by one SER panel participant.

Currently, the vast majority of community banks do not collect nor record the application method. This would be a new data construct if finalized. The complexity of this data point will likely lead to unintentional errors. Additionally, including this data point is unlikely to achieve the CFPB's stated goals. This suggests that the Bureau should remove this proposed data point. This data point is needlessly complex and unlikely to provide the Bureau or public with meaningful evidence of discrimination. Other stated policy goals can be achieved by combining other statutorily mandated data points.

i) Needless Complexity

Though complying with "application method" by selecting in-person, telephone, online, or mail seems simple on its face, the lengthy official comments indicate that compliance will almost certainly not be simple. Proposed comment 107(a)(3)-1 would explain how FIs are to choose which application method to report, including via "waterfall approach" when they have contact with an applicant in multiple ways. The official comments then provide detail in the "waterfall approach" at which point the complexity of compliance becomes apparent.

- Proposed comment 107(a)(3)-1.i would provide that a FI reports the application method as "in-person" if the FI, or another party acting on the FI's behalf, meets with the applicant in person (for example, in a branch office, at the applicant's place of business, or via electronic media with a video component).
- Proposed comment 107(a)(3)-1.ii would provide that a FI reports the application method as "telephone" if the FI, or another party acting on the FI's behalf, did not meet with the applicant in person but communicated with the applicant by telephone or via electronic media, without a video component.

- Proposed comment 107(a)(3)-1.iii would provide that a FI reports the application method as "online" if it, or another party acting on the FI's behalf, did not meet with the applicant in person and did not communicate with the applicant by telephone but communicated with the applicant through an online application, electronic mail, text message, and/or some other form of online communication.
- Proposed comment 107(a)(3)-1.iv would provide that a FI reports the application method as "mail" if the FI, or another party acting on the FI's behalf, did not meet with the applicant in person and did not communicate with the applicant by telephone but communicated with the applicant in writing via United States mail, courier or overnight service, or hand-delivery (including hand-delivery of documents via an overnight drop box or at a teller window).
- Proposed comment 107(a)(3)-2 would provide guidance on what application method a FI would report for interactions with applicants, both online and by mail. A FI would report application method based on the method by which it, or another party acting on its behalf, requested the ethnicity, race, and sex of the applicant's principal owners.

Though likely intended to be comprehensive and illustrative, this "waterfall approach" is very complicated and prone to unintended errors. Apart from the subjectivity and differing trigger of "application" from FI to FI, there will undoubtedly be situations where the applicant initially meets with the FI telephonically, "submits the application" via mail or email, but only meets with the FI in-person at some point before a credit decision is made but after the "application" was submitted.

This is an incredibly complex data point that presents limited value. The CFPB should not include this data point in the final rule.

ii) Unlikely to Provide Evidence of Discrimination from Bad Actors

The Bureau contends that this data point will monitor for discouragement of applicants. This contention is reasonably based on the "bad actor theory" – that certain bad actors will discriminate against protected classes of people based on their appearance, and that correlating certain application methods (in-person or remote) with adverse credit decisions can ferret out that illegal discrimination. That theory, though, is based on the faulty assumption that bad actors will accurately report this data point.

For example, if a bad actor were indeed discouraging certain protected classes of applicants, it is likely that the bad actor would misreport other data points of this rule that would evidence their illegal activity. Only the good actors that do not illegally discriminate will accurately record

this data point, and therefore, the data is unlikely to show a correlation between application method and discouragement.

The Bureau also explains that data on application method would assist in analyzing data reported under, and assessing compliance with, proposed §1002.107(a)(20), which requires FIs to collect principal owners' ethnicity and race via visual observation or surname in certain circumstances. Yet, here again, the Bureau uses the faulty logic that a bad actor will accurately report the data that will evidence their non-compliance with other portions of the rule.

iii) Achieving Stated Policy Goals by Combining Already Collected Information

Finally, the Bureau believes that application method may help users of 1071 data analyze the extent to which FIs may be providing access to credit online or by telephone in "credit deserts" where FIs do not have branch operations. However, this data could easily be inferred by matching portions of 1071 statutorily mandated data with other publicly available data.

For example, collecting the census tract of the loan proceeds will indicate whether the loan was indeed originated in a credit desert or in an area where the FI does not have a branch presence. In either such case, the Bureau would be able to analyze the extent to which applicants are receiving credit online or by telephone without creating the additional burdensome data point.

e) Denial Reasons

Though not required by statute, the Bureau is proposing to require FIs to report the principal reason or reasons the FI denied the covered application. Proposed comment 107(a)(11)-1 explains that a FI complies with proposed §1002.107(a)(11) by reporting the principal reason or reasons it denied the application, indicating up to four reasons. The Bureau notes that its proposed approach for this data point largely mirrors the Regulation C approach for denial reasons.

Apart from the privacy concerns (noted below), ICBA continues to recommend that this data point should not be required but should be optional for FIs. If the Bureau believes that including denial reasons might reduce the risk of erroneous conclusions and fair lending actions, then the Bureau should grant FIs the discretion of including those data points, dependent on their own risk appetite and mitigation strategies.

However, if the Bureau elects to include this data point, ICBA believes that the denials reason categories listed constitute a full picture of reasons that credit is typically denied.

f) Number of Workers

Another data point not required by statute but being proposed by the Bureau is the number of workers that the small business applicant employs. The Bureau believes that this data point would aid in fulfilling the business and community development purpose of section 1071.

Once again, ICBA objects to the proposed inclusion of this discretionary data point. The Bureau is correct in recognizing that many banks that do not originate SBA loans do not typically collect the number of employees in a company. Making this more difficult, the Bureau has changed the SBREFA Outline contemplated "employee" data point and is now proposing "workers," which would include contractors and others that are not necessarily employed by the applicant. This information is not necessarily known by the applicant, will have little value toward enforcing fair lending laws, and will likely generate error and bad data.

If the Bureau proceeds to retain this proposed data point, ICBA recommends that the final rule allow principal owners to report themselves as workers, which would be more in line with common parlance and avoid confusion.

g) Time in Business

Though not required in statute, the Bureau believes that data providing the time in business of a small business applicant would aid in fulfilling both the business and community development and fair lending purposes of section 1071. The proposed rule would require a FI to collect and report the time the applicant has been in business, described in whole years, as relied on or collected by the FI.

The Bureau explains that time in business information could help explain differences in underwriting risk among small business applicants and thus avoid misinterpretation of the section 1071 dataset. However, this rationale is undercut by the Bureau's proposed requirement for the FI to report time in business using owner or management experience rather than the age of the business itself. Similarly, the Bureau's rationale is diminished by the proposed requirement that the owner with the greatest number of years is reported when the applicant has multiple owners with different numbers of years operating that business.

While ICBA agrees with the Bureau that the inclusion of time in business data could help mitigate the concerns of data misrepresentation, the proposed rule provides an example where data indicating that a small business applicant is a start-up with little experience, or financial history could provide a legitimate business explanation for why the FI denied the application or approved it for less credit than was applied for. ICBA urges the Bureau to make such data optional as a mitigant, not a requirement.

WASHINGTON, DC
1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

h) Application Recipient

The Bureau is proposing to require FIs to collect and report the application recipient, meaning whether the applicant submitted the covered application directly to the FI or its affiliate, or whether the applicant submitted the covered application indirectly to the FI via a third party. Proposed comment 107(a)(4)-1 would clarify that if a FI is reporting actions taken by its agent consistent with proposed comment 109(a)(3)-3, then the agent is considered the FI for the purposes of proposed §1002.107(a)(4).

Once again, this data point is not required by statute nor was it considered in the SBREFA Outline. The Bureau believes that the proposed collection of application recipient may help users of the data understand whether FIs making credit decisions are directly interacting with the applicant and/or generally operate in the same community as the applicant.

Though the Bureau might believe that this data point would "improve the public's understanding of the structure of small business lending originations across the market," it is a data point that, in the vast majority of cases, is not currently collected by community banks and would be an undue burden to achieve the Bureau's aspirational goal, contrary to the Bureau's belief that this data point should not be difficult to collect and report. Further, application recipient would not be dispositive evidence of fair lending violations. ICBA strongly recommends that the CFPB use their discretionary authority wisely and establish a compelling nexus between the statutory goals and discretionary data points.

i) Credit Type

The Bureau believes that three additional data fields should spring from "credit type," which is explicitly enumerated in statute. The Bureau is proposing to require FIs to collect and report the following information regarding the type of credit applied for or originated: (i) the credit product; (ii) the type or types of guarantees that were obtained for an extension of credit, or that would have been obtained if the covered credit transaction was originated; and (iii) the length of the loan term, in months, if applicable.

Despite the added complexity of requiring three data points for the one listed in statute, ICBA believes that the Bureau has accounted for and addressed some of the concerns that community banks have raised related to this data point. In particular, ICBA appreciates that the data points allow for the simple reporting of counter offers and the ability to mark fields as "not provided by applicant" in the case of incomplete applications.

However, ICBA continues to object to additional credit amounts, such as line increases, counting as a separate credit product. Not only will it be duplicative to capture the same information in a line increase as was captured from the initial origination, but it will also artificially inflate a FI's loan volume activity, thereby significantly increasing the number of community banks that would be covered FIs.

j) Credit Purpose

Section 1071 requires FIs to collect and report the type and purpose of the loan or other credit for which the applicant is applying. The Bureau is proposing to require that FIs collect and report the purpose or purposes of the credit applied for or originated. The Bureau is also proposing to add "not applicable" to the purposes list for use when an application is for a credit product that generally has indeterminate or numerous potential purposes, such as a credit card. Proposed comment 107(a)(6)-5 would also explain the use of "not applicable" as a response.

ICBA supports the proposed compilation of credit purpose, especially the flexibility of "not applicable" fields or "not provided by applicant and otherwise undetermined" options. ICBA also appreciates that FIs would be able to order the "credit purposes" according to their own discretion. ICBA believes that these accommodations will facilitate compliance while still achieving the policy goals of the law.

k) Amount Applied for

Section 1071 requires FIs to collect and report "the amount of the credit or credit limit applied for," and the Bureau is proposing in § 1002.107(a)(7) to require that a FI collect and report "the initial amount of credit or the initial credit limit requested by the applicant." Proposed comment 107(a)(7)-1 would explain that a FI is not required to report credit amounts or limits discussed before an application is made but must capture the amount initially requested at the application stage or later.

As ICBA discussed in response to the SBREFA Outline, an applicant will often state a specific amount early in the application process, but the amount will usually change during the process for various appropriate reasons. Arriving at an applied for amount is a complex, iterative process, and the reporting requirement should be flexible. As such, ICBA appreciates that the proposed rule accounts for this iterative process by not requiring FIs to report the amounts discussed before the application is made, thereby accommodating preliminary informal interactions.

However, it should be noted that applicants' stated credit desires can be arbitrary, and comparing the initial amount requested against the amount approved could be misleading and is not a reliable measure of the health or efficacy of small business lending. Though this cannot be addressed in the data reporting field, ICBA stresses that the Bureau should incorporate these concerns when determining which data to publish on a loan-level basis (discussed further, below).

l) Amount Approved or Originated

Section 1071 requires FIs to collect and report "the amount of the credit transaction or the credit limit approved." The Bureau is proposing that the amount approved or originated be collected and reported as follows:

(i) for an application for a closed-end credit transaction that is approved but not accepted, the FI collects and reports the amount approved by the FI;
(ii) for a closed-end credit transaction that is originated, the FI collects and reports the amount of credit originated; and
(iii) for an application for an open-end credit transaction that is originated or approved but not accepted, the FI collects and reports the amount of the credit limit approved.

This proposed treatment closely tracts with what was contemplated in the SBREFA Outline, and as such, ICBA has no suggested changes. It is important to highlight, though, ICBA's support for the proposed treatment of counteroffers pursuant to proposed comment 107(a)(8)-5. The proposed comment explains that if an applicant agrees to proceed with consideration of a counteroffer for an amount or a limit different from the amount for which the applicant applied, and the covered credit transaction is approved and originated, the FI reports the amount granted.

In contrast, if an applicant does not agree to proceed with consideration of a counteroffer or fails to respond, the institution reports the action taken on the application as denied and reports "not applicable" for the amount approved or originated. ICBA believes that this treatment of counteroffers appropriately allows for the negotiations that are prevalent in small business lending.

m) Action Taken

ECOA section 704B(e)(2)(D) requires FIs to report the "type of action taken" on an application. As such, the Bureau is proposing in §1002.107(a)(9) to require reporting of the action taken by

the FI on the covered application, reported as originated, approved but not accepted, denied, withdrawn by the applicant, or incomplete, which is largely consistent with Regulation C. [20]

ICBA supports the Bureau's proposal to categorize all incomplete applications as a single category of "incomplete," rather than incomplete denials separate from notices of incompleteness. This should provide FIs with easier compliance and less opportunity for error.

Regarding the treatment of counteroffers that are not accepted, ICBA believes that they should be reported as "approved but not accepted," as that classification would appropriately capture the situation where the applicant was approved for credit yet declined to accept the credit offer. This approach also more appropriately reflects the availability of credit in the market.

n) Action Taken Date

ECOA section 704B(e)(2)(D) requires FIs to collect and report the "date of such action." The Bureau is proposing to require "action taken date" to be reported as the date of the action taken by the FI, largely in coordination with Home Mortgage Disclosure Act implementing Regulation C approaches.

While ICBA has no recommendations related to the proposed treatment of "action taken date", ICBA strongly opposes the additional data points contemplated in the section-by-section analysis of the proposed rule. Specifically, ICBA objects to the requirement for FIs to record separate data points for the date the application was approved and the date of disbursement of funds (for term loans) or funds availability (for lines of credit). ICBA believes that to do so, the Bureau would be chasing ever-increasingly de minimis data points that have diminishing value. Reporting the time elapsed between when an application is approved, when the closing occurred or the account was opened, and when the applicant actually received the loan funds or access to funds adds inordinate degrees of complexity that draws out the compliance process much longer than needed to meet the objectives of the law.

o) Census Tract

Section 1071 requires FIs to collect and report "the census tract in which is located the principal place of business of the . . . applicant." The Bureau is proposing to require FIs to collect and report the census tract data point using a "waterfall" approach. Under the Proposal, FIs would report the census tract of the address or location where the proceeds of the credit applied for

[20] 12 CFR 1003.4(a)(8).

or originated will be or would have been principally applied. If that information is unknown, then the FI reports the address or location of the main office or headquarters of the applicant. Finally, if even that information is unknown, then the FI reports another address or location associated with the applicant.

This approach is similar to the one contemplated in the SBREFA Outline and of which ICBA is supportive. It adequately reflects banks' preference to match existing regulatory requirements, such as Regulation C and CRA. ICBA also welcomes the Bureau's proposed safe harbor, which would state that an incorrect entry for census tract is not a violation of ECOA or Subpart B if the FI obtained the census tract by correctly using a geocoding tool provided by the Federal Financial Institutions Examination Council ("FFIEC") or the Bureau. However, as discussed below, ICBA is significantly concerned about the risk to small business customer privacy if census tract and other data points are publicly reported.

p) Gross Annual Revenue

Section 1071 requires FIs to collect and report "the gross annual revenue of the business in the last fiscal year of the . . . applicant preceding the date of the application," and the proposed rule would require reporting of the gross annual revenue of the applicant for its preceding full fiscal year prior to when the information is collected.

ICBA supports the proposed comments that would clarify that a FI need not verify gross annual revenue information provided by the applicant and is permitted – not required – to report the gross annual revenue for the applicant that includes the revenue of affiliates as well.

q) Minority-owned and Women-owned Business Status

Consistent with its approach during the SBREFA process, the Bureau is proposing to require FIs to collect and report whether an applicant is a minority-owned business and/or a women-owned business. Proposed appendix F includes a requirement that a FI inform an applicant that the applicant is not required to respond to the FI's questions regarding the applicant's minority-owned and women-owned business status, and a prohibition on FIs requiring applicants to provide this information. Proposed appendix E, which is a sample data collection form, would include a question about minority-owned and women-owned business status and related information to assist applicants with responding to the question.

ICBA supports the Bureau's proposed approach in collecting this information and particularly welcomes the model forms in appendix F and E. ICBA also appreciates that the Bureau is keeping with the spirit of the law by allowing applicants to refuse to answer the question and permitting FIs to reflect that refusal in the data collection field.

r) Number of Principal Owners

The Bureau is proposing that FIs collect and report the number of principal owners of a business, defined as a natural person who directly owns 25 percent or more of the equity interests of the business. Additionally, while the ownership interest of a small business may be straightforward in certain cases and specified in a legal organizational document in other cases, certain legal structures make determining ownership equity extremely difficult, at best. ICBA questions the utility of this information, especially in cases that might inadequately describe or erroneously imply the ownership structure of the applicants.

s) Application Date

ECOA section 704B(e)(2)(A) requires FIs to collect and report the "date on which the application was received." Here, the Bureau is proposing to require reporting of the application date as the date the covered application was received by the FI, or the date on a paper or electronic application form. Proposed comments 107(a)(2)-1 and -2 would clarify the need for a FI to take a consistent approach when reporting application date and provide guidance on how to report application date for indirect applications.

Additionally, the Bureau is proposing a safe harbor, which would provide that a FI does not violate proposed subpart B if it reports on its small business lending application register an application date that is within three calendar days of the actual application date.

Given community banks' familiarity with Regulation C, ICBA supports the proposal's treatment of application date. However, while ICBA welcomes safe harbors, the utility of this safe harbor is difficult to envision. For example, it is not clear who would determine, or how it would be determined, that the "actual" application occurred on a date other than the one recorded by the FI. Given that the definition of "application" provides an inherent degree of flexibility and subjectivity, ICBA contends that the date the FI provides is the "actual" date. In the alternative, ICBA requests the Bureau to provide additional official commentary that illustrates how this safe harbor would operate.

t) Unique Identifier

Given that the ECOA section 704B(e)(2)(A) requires FIs to collect and report "the number of the application," the Bureau is proposing to require that FIs report an alphanumeric identifier starting with the legal entity identifier ("LEI") of the FI. This unique alphanumeric identifier would be required to be unique within the FI to the specific covered application and would be required to be usable to identify and retrieve the specific file corresponding to the application for an extension of credit.

Community banks have noted their preference not to be required to create this identifier too early in the credit origination process.

4) The Proposed Rule presents grave concerns regarding customer privacy.
The Bureau is required to annually make the data it receives from FIs available to the public in such form and in such manner as the Bureau determines by regulation[21]; however, the Bureau may, "at its discretion, delete or modify data collected under [section 1071] which is or will be available to the public, if the Bureau determines that the deletion or modification of the data would advance a privacy interest."

ICBA believes that the Bureau must be aggressive in protecting the privacy interests of small businesses and err on the side of caution. Publishing certain data points in unedited, application-level format will likely lead to the re-identification of small businesses and create risks to the privacy interests of applicants.

a) Sensitivity of Data Points When Combined

After the Bureau receives at least one full year of 1071 data from FIs following the compliance date of the final rule, the Bureau intends to issue a policy statement in which the Bureau would set forth its intended modifications and deletions of data that will be subject to public release. Before conducting the balancing test or collecting a year of data, the Bureau should run preliminary tests to understand the reidentification potential of NAICS codes and census tract data. These data create a unique set of records that can be accurately matched to records in other publicly available datasets identifying an applicant or a related natural person. It is illustrative to provide an example of how powerful the combination of NAICS code and census tract is in reidentifying small businesses.

For example, census tract 9668 has 3,726 residents in which the town of Lewisville, OH is located, with a population of 176 residents. In the town of Lewisville is the "Lewisville Vintage Farmhouse," with a Yelp page that describes it as an antique store. This implies it has a NAICS code of 453310 – used merchandise store. After searching Yelp and US Census Bureau websites, it does not appear as if another business with NAICS code 453310 exists in Lewisville, OH or anywhere else in census tract 9668. Therefore, if "Lewisville Vintage Farmhouse" sought a loan, the combination of its census tract and NAICS code makes reidentification a near certainty,

[21] Section 704B(f)(2)(C) of ECOA.

along with the owner's gross annual income, potential reason for denial, and sensitive demographic information.

Once again, the Bureau does not need to collect a year of data to determine the potential of reidentification from certain data points.

b) Opportunity to Comment on the Privacy-Balancing Test

The CFPB states its intention to issue a policy statement that addresses privacy concerns after the rule is in effect for at least one year. The Bureau states it does not intend to allow for or consider public comments in response to the policy statement, but in lieu, asks for comments on a partial and incomplete description of the privacy-balancing test.

A full explanation of the balancing test design and its application would help stakeholders consider the potential reputational risks associated with data disclosure. Additionally, the Bureau should issue the policy statement subject to public comment to provide opportunities for public feedback on privacy issues.

5) FIs should have a minimum of three years to comply, or the rule should be implemented on a staggered basis.

The Bureau is proposing a compliance date of 18 months after the rule's effective date. We do not believe 18 months provides community banks sufficient time to comply with a rule this complex. Compliance with Section 1071 will require significant investment in training and technology. For small banks, this process is made more difficult because they will be dependent on third party vendors to develop new systems, platforms and training modules, rather than developing them internally.

In our view, a compliance date three years after the rule's effective date is more appropriate. This will allow banks and their third-party processors to develop compliance systems – a process that they cannot begin in earnest until the rule is final. Having these systems in place will provide banks an opportunity to integrate new systems into their existing frameworks.

In the alternative, we advocate a tiered timeline for compliance. Larger FIs, those with assets in excess of $10 billion, could have a compliance date set two years after the rule's effective date, while smaller, lower volume lenders would be given 36 months to comply with the rule. This approach would allow the Bureau to collect a significant amount of small business data earlier, while also providing third party processors additional time to develop and integrate their compliance products.

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6) The "Firewall" provision demonstrates the need to exclude community banks from coverage.

ECOA section 704B(d)(1) states that "[w]here feasible," underwriters and other officers and employees of a FI or its affiliates "involved in making any determination concerning an application for credit" cannot have access to any information provided by the applicant pursuant to a request under 704B(b).[22] Additionally, under ECOA section 704B(d)(2), if the FI determines that an underwriter, employee, or officer involved in making a determination "should have access" to any information provided by the applicant pursuant to a request under 704B(b), the FI must provide a notice to the applicant of the underwriter's access to such information.

ICBA is concerned that small community banks will be disproportionately burdened by this firewall provision, as they are the most likely to have a limited sized staff that cannot feasibly firewall the information. Apart from the additional burden, smaller community banks might be adversely impacted from a competitive perspective if they are covered by this rule. For example, the notice to the applicant will presumably not be provided by large FIs or fintechs that could more easily create firewalls, and as such, there might be a perception among applicants that those FIs are less likely to discriminate because they have firewalled the information. This could lead applicants to seek credit only from larger FIs or fintechs.

Similarly, applicants might be uncomfortable in providing demographic information to banks if they receive notice that their information will not be firewalled, resulting in more applicants at community banks opting not to disclose their demographic information, and in turn, more community bank employees having to guess the applicant's race and ethnicity based on visual appearance or surname.

The Bureau should exempt small FIs, such as community banks, from the firewall requirement for the reasons discussed above. Alternatively, the CFPB could require all FIs to provide the notice to all applicants, regardless of whether the information is firewalled. This option would remove the regulatory, market, and misperceived reputational advantage that larger FIs would hold over smaller ones.

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[22] This includes information regarding the women-owned and minority-owned business status and the race, sex, and ethnicity of the principal owners.

ICBA suggests that the Bureau establish an online system or portal, where borrowers could input their sensitive, demographic information that is matched with a unique identifier. The unique identifier is used to match the applicant demographic with loan information. Not only would such a portal solve for the notice requirements, but it would also solve for the sensitivity of the data, providing applicants with assurance of confidentiality, and promoting self-reporting. If the Bureau chooses to not provide this portal, then it should allow for a private market solution that could facilitate this option that demonstrates compliance with these proposed provisions.

Finally, if the Bureau creates or allows for the use of a portal, it is imperative that FIs be able to match their records with the portal's records after a final decision has been made on the application so that FIs can perform back testing and internal audits to determine whether their operations are complying with fair lending laws. This would support the long-held tenet that self-identification and remediation are encouraged in the supervisory space.

7) Cost-Benefit Analysis

Section 1022 of the Dodd-Frank Act requires the Bureau to consider the costs and benefits of the regulations it prescribes.[23]

Certain regulations run the risk of becoming too costly and burdensome, and therefore frustrating their own purpose. If Bureau regulations impose costs on lenders that are too high, those lenders will inevitably be compelled to (1) pass costs on to consumers and/or (2) exit the market entirely. Both outcomes result in harming the consumers that the Bureau intends to protect and may leave them worse off than if the regulation had never been promulgated.

We do not contend that Section 1022 requires the Bureau to abstain from prescribing a regulation if it concludes that the costs outweigh the benefits. Indeed, as we believe is the case with Section 1071, the Bureau may be required by a separate provision to finalize a rule that results in costs that are self-frustratingly high. However, as a matter of public policy, it is incumbent on the Bureau to minimize the costs associated with implementing the law. **In the case of this rulemaking, that means not requiring the collection of data points that are not statutorily required and exercising its Section 1022(b)(3) authority to exempt certain small institutions that will be disproportionately impacted by new compliance obligations.**

[23] *See* 12 USC 5512(b)(2).

Having made the preceding general observations regarding the Bureau's cost-benefit analysis requirements, ICBA's comments regarding the analysis of cost and benefits for the Bureau's implementation of Section 1071 follow below.

a) Costs to Covered FIs

We agree with the Bureau's decision to analyze costs in two categories: "one-time" and "ongoing," with one-time expenses defined as "expenses that the FI would incur initially and only once to implement changes required in order to comply with the requirements of the new rule" and ongoing costs defined as "expenses incurred as a result of the ongoing reporting requirements of the rule, accrued on an annual basis."[24] Both categories are significant because the one-time costs of compliance may force existing small business lenders to exit the market and prevent new small business lenders from entering the market, both of which reduce consumer choice. Ongoing costs may also contribute to the decision to exit the small business lending market but are significant because they are most likely to be partially or wholly passed on to consumers in the form of application or origination fees or higher interest rates.

To estimate the cost to FIs, the Bureau relies on its previous experience with HMDA".[25] We agree that the HMDA data collection is the closest existing parallel to Section 1071 data collection but emphasize that there are significant differences between the mortgage lending and small business lending lines of business. Specifically, for community banks with a relationship lending business model, small business lending is likely to be much more individualized than mortgage lending.

Very few community banks have a standard small business application form or process, and every loan is unique. Some small businesses frequently borrow relatively small amounts from community banks. In these cases, so long as the business is healthy and is current on paying its outstanding loans, the amount of paperwork may be very low. On the other hand, where a business is new, or where the loan amount is high, the bank may conduct significant due diligence, far beyond what would be required to originate a home mortgage loan. Because of these differences, the point at which reporting requirements are triggered will vary from loan to loan. Additionally, bankers may collect much of the required information from some

[24] 86 Fed. Reg. 56542.
[25] *See* 86 Fed. Reg. 56545.

borrowers already, but not for others. This will require additional data collection from some borrowers, therefore complexifying the application process.

While it is difficult to estimate the one-time costs of compliance, which will vary significantly from institution to institution, the Bureau's estimate of $58,400 for small depository institutions is very likely on the low-end. We believe that one-time costs will likely be in the high-tens to low-hundreds of thousands of dollars for the smallest banks and will cost mid-sized community banks several times more (not less, as the Bureau estimates).[26] **It is likely that a significant portion of these startup costs for small lenders can be avoided if the Bureau exempts community banks under $1.3 billion, provides partial exemption from discretionary data points, or adopts tiered compliance dates, allowing third party providers time to bring their products to market.**

To estimate the ongoing costs of this regulation, ICBA surveyed its membership. Based on this survey, we believe that being required to hire new employees to manage compliance obligations will be the biggest cost associated with Section 1071. In contrast to large banks that employ thousands of employees to manage compliance, approximately 80% of community banks surveyed reported employing 25 or fewer full-time employees ("FTEs") dedicated to small business lending. 50% employed 10 or fewer FTEs in a small business lending role. These small staffs are already stretched thin and will require significant retraining to comply with the proposed rule. As a result, **58% of community banks surveyed reported that they will likely be required to hire additional FTEs to in order comply with the rule.**

If a bank is required to hire even one additional FTE, the cost estimate would exceed the Bureau's own estimated time commitment of 716 staff hours per year for small (Type A) depository institutions.[27] This time estimate amounts to 17.9 weeks of full-time work per year, or about 1/3 of a single FTE. Therefore, we believe the Bureau's estimate significantly understates the cost to small community banks.

b) Costs to Small Businesses

According to the NPR, "[t]he Bureau expects the direct costs of the proposed rule to small businesses will be negligible, especially compared to the overall cost of credit."[28] **We strongly disagree with the Bureau's characterization of the proposed rule's cost to small businesses.** If Section 1071 is implemented as proposed, it will result in fewer credit options for small businesses and a reduction in their ability to shop around for credit. To the extent that Section

[26] 86 Fed. Reg. 56556.
[27] *See* 86 Fed. Reg. 56556, Table 10.
[28] 86 Fed. Reg. 56543.

1071 prompts market exit or consolidation, small business borrowers may lose access to local lenders that understand their business and are willing to provide financial advice and tailored loan products. In addition, if lenders implement an application fee to offset the costs of 1071 compliance, borrowers will be less likely and less able to shop around for a loan with the best interest rate. This can result in significant long-run expense for the business.

In our survey of community banks, **64% of bank respondents indicated that they would be likely to charge a small business loan application fee to offset the cost of compliance.** This illustrates that the direct costs to small businesses are very real and not remote and speculative. **Fifty-five percent of bankers, who reported that they would charge an application fee, indicated that the fee would likely need to be $100 or more.** For the smallest businesses, a fee of this size is substantial enough to discourage shopping around for the best rate.

Additionally, small business borrowers will be required to provide additional data about their business which may require significant additional time to compile. Lenders will be unwilling or unable to proceed with loans without collecting the data required for Section 1071 reporting, and a portion of the burden of compiling this information will fall on small businesses themselves. In addition, borrowers will be asked questions about their race and demographic information that they may be uncomfortable with, chilling their desire to seek credit from a regulated institution.

However, the biggest cost to small businesses by far is the reduction of privacy this regulation will create. The data points required to be reported and disclosed by this regulation create the potential for re-identification of small business borrowers and public disclosure of sensitive financial and other information relating to their business. Community banks have repeatedly heard from their small business customers that privacy is a major concern. This concern is evident in the overwhelming pushback from small businesses to the IRS reporting provision recently proposed in Congress and by the Biden Administration, and from bankers' experience with PPP, where rates of compliance with the voluntary demographic disclosure were below 20%.

c) Benefits to Small Businesses and Covered FIs

On the other side of the ledger are the benefits supposedly created by the proposed rule. As the Bureau concedes, "[q]uantifying benefits to small businesses presents substantial

challenges."[29] The NPR goes on to say that the Bureau "is unable to readily quantify any of [the benefits of the proposed regulation] with precision, both because the Bureau does not have the data to quantify all benefits and because the Bureau is not able to assess completely how effective the implementation of section 1071 will be in achieving those benefits."[30]

In our view, the issue is starker. Section 1071 was enacted to ensure the credit needs of women-owned, minority-owned, and small businesses are being met in accordance with fair lending laws. This is a worthy policy objective, but it is poorly served by mandatory collection of demographic information that has been illegal to collect previously and that small business customers may prefer to keep private. We believe this regulation will ultimately decrease the willingness of small business customers to seek credit and increase the cost of credit for the small business borrowers it is intended to protect.

As for the benefits to FIs, we are skeptical of the Bureau's claim that this regulation will help them to "better understand the demand for small business credit products and the conditions under which they are being supplied by other covered FIs."[31] Community banks already have a high understanding of the small business credit markets in their local communities. Disclosure of Section 1071 data will not meaningfully increase this understanding because of the individualized nature of each small business loan. Important information about how competitors made credit decisions will still be missing from Section 1071 disclosures, therefore the additional market insight gained will be limited. Because the Bureau will not capture or publish all significant contextual information – arguably, rightfully so – there's no significant market benefit from the data's publication.

8) Enforcement

For banks $10 billion or less in assets, the requirements of Section 1071 will be enforced under Section 8 of the Federal Deposit Insurance Act by the appropriate Federal banking agency.[32] Enforcement actions can include the termination or suspension of deposit insurance, cease and desist orders, the removal, prohibition, or suspension of bank officers, directors, or affiliated parties, and civil money penalties.[33]

While we view these potential enforcement actions as appropriate and in-line with other regulations, we would urge them to be used sparingly in the 12 months following the rule's compliance date. Once systems are developed and integrated into small banks' framework,

[29] 86 Fed. Reg. 56543.
[30] *Id.*
[31] 86 Fed. Reg. 56543.
[32] 15 USC 1691c(a)(1).
[33] *See* 12 USC 1818.

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1615 L Street NW
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good faith errors may occur while they adapt to new complex collection and reporting requirements.

a) 112(b) Bona Fide Errors

The proposed regulation includes a provision that says an error in compiling, maintaining, or reporting data is a bona fide error if it was "unintentional and occurred despite the maintenance of procedures reasonably adapted to avoid such an error."[34] Bona fide errors are not a violation of ECOA. **ICBA supports the inclusion of this provision.**

b) 112(c) Safe Harbors

The Bureau is proposing to provide several safe harbors, creating a set of errors that would not constitute violations of ECOA. These safe harbors are:

i) Incorrect entry for census tract – Listing an incorrect census tract is not a violation if the FI obtained the census tract by correctly using a geocoding tool provided by the FFIEC or the Bureau. We support the inclusion of this provision but observe that it is quite narrow. It will be difficult to prove whether a geocoding tool was used correctly. Furthermore, we believe that latitude should be given if a census tract is reported for a business where that business has a physical location, even if it is not the business's main address or census tract where loan funds are spent.

ii) Incorrect entry for NAICS code – Entry of the wrong NAICS code is not a violation "provided that the first two digits of the NAICS code are correct and the FI maintains procedures reasonably adapted to correctly identify the subsequent four digits."[35] Once again, we strongly urge the Bureau not to require collection of NAICS data. However, if NAICS data is collected, the proposed tolerance level is appropriate. **We also urge the Bureau to allow lenders to rely on NAICS codes provided by the borrower, even if one of the first two digits of a borrower provided code is incorrect.**

iii) Incorrect determination of small business status – A bank that initially determines that an applicant for a covered credit transaction is a small business, but later concludes the applicant is not a small business does not violate ECOA if it collects information about whether the applicant is a minority-owned business or a women-owned business, or the ethnicity, race, and sex of the applicant's principal owners.

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[34] 86 Fed. Reg. 56579.
[35] 86 Fed. Reg. 56580.

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P.O. Box 267
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ICBA supports the inclusion of this provision as it will prevent punishments for banks that inadvertently collect sensitive demographic information about a larger business. We also urge the CFPB to allow banks to rely on revenue information supplied by borrowers when determining whether data collection under Section 1071 is required.

iv) Incorrect application date – Banks do not violate ECOA if the application date reported is within three calendar days of the actual application. ICBA believes this safe harbor is appropriate.

9) Section 1002.111 – Recordkeeping

a) 111(a) Record Retention

The small business loan data collected pursuant to the requirements of Section 1071 is required to be: retained for at least three years; made available to the public, upon request, in a form and manner prescribed by the Bureau; and made available to the public annually by the Bureau in a form and manner they prescribe by regulation.[36] According to the Proposal, FIs would be required to "retain a copy of its small business lending application register for three years after the register is submitted to the Bureau."[37] The Bureau is seeking comment on how to implement recordkeeping requirements "in a manner that minimizes cost and burden particularly on small FIs while implementing all statutory obligations."[38]

We believe that the Bureau could minimize the compliance burden on small institutions – while still satisfying all of the requirements imposed by statute – by creating a centralized database of small business loan data to which banks could report in real time. **We propose a system by which banks could, at their option, maintain a small business lending application register internally, reporting annually to the CFPB OR report small business loan applications as they are received through a secure online portal, so that records could be stored and maintained at the CFPB.**

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[36] *See* 15 USC 1691c-2(f)(2).
[37] 86 Fed. Reg. 56501.
[38] *Id.*

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1615 L Street NW
Suite 900
Washington, DC 20036

SAUK CENTRE, MN
518 Lincoln Road
PO Box 267
Sauk Centre, MN 56378

866-843-4222
www.icba.org

Small lenders may favor this latter approach because it would reduce the cost and risk associated with maintaining a register internally. Additionally, reporting small business loan applications to the Bureau could be integrated into the normal course of processing an application, potentially reducing the compliance cost.

Information on an online portal should be analyzed and published annually and not as data is submitted. Because banks cannot control the order that loan applications are submitted, inadvertent disparities may occur in partial year data that would disappear as more applications are submitted. The agency and members of the public should, of course, be able to view and bring actions based on lending data from banks that publish in real time from previous whole years.

Additionally, banks that choose to publish their data in real time should be able to view their own lending data in real time. This would allow them the opportunity to correct erroneous submissions and ensure more accurate data. It would also allow them to view their own record of small business lending and to self-correct before a fair lending violation based on discriminatory effect (also called disparate impact) occurs.

b) 111(b) Certain Information Kept Separate from the Application

According to the Bureau's interpretation of ECOA section 704B(b)(2),[39] information about "whether the applicant is a minority-owned business or a women-owned business and the ethnicity, race, and sex of the applicant's principal owners"[40] is required to be kept separate from the rest of the application. We agree with the Bureau's interpretation that this statutory provision should be understood to refer to applicants' responses to the inquiries regarding minority-owned and women-owned business status in proposed § 1002.107(a)(18) and (19), as well as the ethnicity, race, and sex of applicant's principal owners in proposed §1002.107(a)(20)."[41]

As the Bureau observes, these data points have no bearing on the creditworthiness of an applicant, and no FI would legally be permitted to inquire about this demographic information but for Section 1071. For institutions that are required to comply with Section 1071, these data points must be kept separate from the rest of the application to comply with the requirements of the statute.

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[39] 15 USC 1691c-2(b)(2).
[40] 86 Fed. Reg. 56501.
[41] 86 Fed. Reg. 56501-02.

The Bureau's proposed regulation notes that "such information could be collected on a piece of paper that is separate from the rest of the application form. To satisfy the requirement in §1002.111(b), an applicant's responses to the FI's request pursuant to §1002.107(a)(18) through (20) need not be maintained in a separate electronic system, nor need they be removed from the physical files containing the application. However, the FI may, nonetheless, need to keep this information in a different electronic or physical file to satisfy the requirements of §1002.108."[42] This section of the proposal is unclear, and we believe that the Bureau should further clarify the requirements around when lenders will need to maintain separate systems.

In considering implementation of this rule, we urge the Board to consider the implications of the requirements noted above for the smallest lenders. When describing such processes, it is easy to reduce, in the mind's eye, the idea of compliance to simply another form or another file. But in reality, the requirement to create and organize additional digital and physical files requires a significant investment of time, technology, and training. This investment of time imposes a real monetary cost, and once such a rule is implemented, the cost never goes away. It recurs, year after year, application after application.

In a rule like this, where the consumer benefit of incremental data collection from small lenders will be minimal, we strongly urge the Bureau not to dismiss these recurring costs to small lenders when conducting their cost-benefit analyses. To the extent that this rule drives consolidation and causes small, local lenders to merge or vanish, we believe a significant cohort of small business borrowers, including women-owned and minority-owned businesses, will be less well-served.

10) Use of previously collected data will provide efficiencies but will likely provide regulatory advantage to larger FIs and fintechs.

In the SBREFA Outline, the Bureau emphasized that it was seeking to provide FIs with discretion and flexibility in the timing of 1071 data collection considering their relationships with applicants and the need to avoid unnecessary costs.

Proposed comment 107(b)-1 explains that, depending on the circumstances and the FI's procedures, certain applicant-provided data could be collected without a specific request from

[42] 86 Fed. Reg. 56605.

the applicant. For example, gross annual revenue could be collected from tax return documents.

While this proposed comment and provision appears to be an accommodation, ICBA notes that this provision will mostly accrue benefit to the largest FIs and fintechs that are able to employ the use of data intermediaries to automatically populate much of the required data being proposed, thereby quickening the time it will take for a small business applicant to apply for credit compared to a traditional FI that will need to ask for and record every single data field. This essentially creates a competitive advantage for certain FIs, based on nothing more than a regulatory construct. If the Bureau cannot provide an appropriate remedy for this agency-created advantage, then it should serve as another rationale to exempt community banks.

11) The Bureau should not require the verification of applicant-provided information.
The Bureau is proposing that the FI would be able to rely on statements of the applicant when compiling data unless it verifies the information provided, in which case it would be required to collect and report the verified information.[43] ICBA proposes that the Bureau remove the second clause of this proposal and limit the requirement to the submission of applicant-provided information, regardless of whether it is verified by the FI.

As the Bureau notes, section 1071 does not speak to verification; rather it refers only to compiling and maintaining a record of certain information provided by an applicant. Though the Bureau believes that requiring FIs to collect and report information that they have already verified would not add operational difficulty, ICBA contests that belief. Requiring the reporting of verified data would increase operational difficulty, in that if data is verified, it would be done at a point in time that could be weeks removed from the date that the information was initially collected on the application. Additionally, information may be collected by different staff for different purposes on different platforms.

Though ICBA appreciates that the Bureau is not requiring FIs to verify information, compliance burdens would greatly be eased if the Bureau's final rule does not require the reporting of subsequently verified information unless the FI opts to do so.

[43] § 1002.107(b).

CONCLUSION

While ICBA supports the stated goal and intent of section 1071 and the Bureau's proposed rule, we cannot support this rule in its proposed form. While the concerns we raised are on community banks' behalf, the ramifications of this rule will adversely affect community banks' small business customers. Should you have any questions or would like to discuss this further, please do not hesitate to contact us at Michael.Emancipator@icba.org or Michael.Marshall@icba.org.

Sincerely,

/s/

Michael Emancipator
Vice President and Regulatory Counsel

/s/

Michael Marshall
Director, Regulatory Legal Affairs

NAFCU
3138 10th Street North
Arlington, VA 22201-2149
703 522 4770 | 800 336.4644
f 703.524.1082
nafcu@nafcu org | nafcu org
National Association of Federally-Insured Credit Unions

January 6, 2022

Comment Intake
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

RE: Section 1071 Small Business Lending Data Collection (RIN: 3170-AA09)

Dear Sir or Madam:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I am writing in response to the Consumer Financial Protection Bureau's (Bureau) Section 1071 Small Business Lending Data Collection Proposed Rule (Proposed Rule). NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve 127 million consumers with personal and small business financial service products. NAFCU and its members appreciate the Bureau's dedication to ensuring small businesses are adequately protected under the *Equal Credit Opportunity Act* (ECOA) and section 1071 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (Dodd-Frank Act). NAFCU's members have a proud history of looking beyond traditional financial metrics to serve their communities' small businesses, including many woman- and minority-owned businesses that may not be served by national banks and online-only financial technology companies (fintechs).

However, there is widespread concern that the Proposed Rule's complexity and significant one-time and ongoing compliance costs will weigh disproportionately on credit unions in ways that ultimately lead to fewer and less favorable outcomes for all small business borrowers. The likely net effect of the Proposed Rule's expansive coverage and intensive data collection and reporting requirements is that the credit unions that have supported millions of small business successes across the country will quickly become uncompetitive and may be forced out of small business lending altogether.

NAFCU urges the Bureau to adopt common sense definitions, right-sized thresholds, and a reasonable, phased mandatory compliance schedule to ensure that credit unions' support of their small business members is not jeopardized by unnecessary section 1071 compliance burdens. NAFCU also recommends that the Bureau delay any further section 1071 rulemaking until it is clear the COVID-19 pandemic has ended. The Bureau cannot accurately assess the likely impacts of an intensive rulemaking until America's "new normal" is established and reliably measurable.

General Comments

Section 1071 of the Dodd-Frank Act amended the ECOA to require that covered financial institutions collect and report certain information regarding credit applications made by women-owned, minority-owned, and small businesses. In section 1071, Congress charged the Bureau with

developing and implementing regulation reasonably designed to facilitate the enforcement of fair lending laws and to enable communities, governmental entities, and creditors to identify business and community development needs and opportunities of women-owned, minority-owned, and small businesses. The Proposed Rule would require covered financial institutions to collect and report on a total of 21 discrete small business lending data points, including eight discretionary data points.

Small businesses, as the Bureau recognizes, are irreplaceably important. The strength and resiliency of our national and local economies fundamentally depend on the diversity of their small businesses and those small businesses having adequate access to affordable, high-quality credit. This access, in turn, depends on the competitiveness and diversity of the small businesses lending market. Congress plainly recognized this relationship when it charged the Bureau with developing regulation that enables small business stakeholders to track the lending outcomes and likely capital needs of communities' small businesses.

Unfortunately, the Proposed Rule, if adopted as written, risks irreparably undermining the competitiveness and diversity of today's small business lending market – a market that has changed significantly since the Dodd-Frank Act's passage more than a decade ago. As the Bureau explains, when the Dodd-Frank Act was passed, credit unions and banks represented nearly all of the small business lending market. Few fintechs even existed, let alone specialized in small business products. In recent years, however, as the Bureau points out, fintechs' small business lending is estimated to have grown by as much as 90 percent year-over-year. Fintechs' partnering with national banks and fervent promotion of invoice factoring as a small business credit alternative further fuel shifts away from more traditional, in-community small business borrowing.

Even if loan originations under the Small Business Administration's (SBA) Paycheck Protection Program (PPP) serve as only a rough indication of small business lenders respective market shares, the program's startling evidence of big banks' and fintechs' pronounced and growing dominance is relevant. JP Morgan Chase Bank, N.A. (JPM Chase) executed in excess of 250,000 PPP loans. BlueVine, a fintech younger than the Bureau, executed roughly 155,000 PPP loans. It is a simple economic fact that any adopted form of the Proposed Rule will raise compliance costs for all covered financial institutions. The net effect of increased compliance costs on different types of covered financial institutions, however, is neither as simple nor uniform. For such firms as JPM Chase and BlueVine, the Proposed Rule's one-time and ongoing costs will be negligible, if noticeable – not only because such behemoths can cost-effectively develop complex compliance tools in-house but because even those costs will be allocated across hundreds of thousands of transactions.

Many credit unions, on the other hand, are themselves small businesses, well below the SBA's $600 million total assets threshold. Some credit unions will not only be forced to purchase comparatively expensive third-party information technology (IT) solutions but will be rendered captive to IT vendors' development, redeployment, and cross-testing timelines over which the credit unions will have no meaningful control. For other credit unions, automated section 1071 compliance tools are likely out of reach, and the process of manually collecting and reporting section 1071 data is likely to result in greater borrower confusion as well as lengthier, more

complicated application processes. Credit unions, too, have little or no capacity to absorb increased compliance costs. 89 percent of respondents to NAFCU's October 2020 *Economic & CU Monitor Survey* said they will be forced to charge higher fees on business products to offset the costs of their collecting and reporting section 1071 data. 44 percent of respondents expected the costs of other credit products to rise as well. Additionally, a majority of respondents indicated that they would expect to change either the set of small business products offered or their underwriting practices in response a section 1071 final rulemaking.

Furthermore, unlike banks and fintechs, federally-insured credit unions are constrained by the *Federal Credit Union Act* (FCU Act) and the *Credit Union Membership Access Act* (CUMAA). The FCU Act provides that a federally-insured credit union may serve only those within the field of membership described in its charter. The CUMAA codified the definition of a member business loan (MBL) and limited a well-capitalized, federally-insured credit union's MBLs to the lesser of either 1.75 times the credit union's net worth or 12.25 percent of its total assets. So constrained, credit unions cannot, unlike banks and fintechs, rapidly ramp up small business lending activities to minimize or wholly offset the Proposed Rule's significant one-time and ongoing costs. The Bureau's ultimate publication of reported section 1071 data also risks credit unions, statutory constrained in whom they may serve and in the scale of their business lending, appearing to run afoul of fair lending laws when no such impropriety, in fact, exists.

Despite many individual credit unions' modest small business lending activity, the credit union industry as a whole brings to bear significant, necessary competitive market pressures that benefit all small business borrowers, not just credit unions' borrowers. For those small businesses in their field of membership, credit unions offer unparalleled in-community support, competitive rates, low fees, and tailored, flexible terms. This nation's credit unions collectively serve roughly one half of all American adults, and the vast majority of American adults not yet served by a credit union are likely eligible for membership in at least one credit union. Credit unions, therefore, represent a real and affordable alternative to big banks and fintechs and, consequently, exert downward pressures on these for-profit lenders' small business loan pricing. NAFCU's *Economic Benefits of the Credit Union Tax Exemption to Consumers, Businesses, and the U.S. Economy*, released in September 2021, shows that the combined benefit to credit union members and bank customers from credit unions' presence in U.S. financial markets was $153 billion over the period 2011 to 2020. In fact, in six of the ten years, benefits to bank customers exceeded benefits to credit unions members, and in two other years, benefits to bank customers and credit unions members were effectively equal.

While the Bureau may regard the prospect of a consolidated and homogenized small business lending market with ambivalence, the Bureau should not assume too much about the ultimate trajectory of small business borrower outcomes under the Proposed Rule. Data collected through the Federal Deposit Insurance Corporation's (FDIC) *Small Business Data Collection Survey* strongly suggests that borrowers satisfaction levels with fintechs is "far lower than with traditional lenders". Fintechs received a net satisfaction score of 33 percent while small depository institutions came in at 73 percent and large depository institutions at 55 percent. In a December 2019 Federal Reserve study of small business borrowers, 63 percent of online lender applicants reported challenges working with their lender. More than half of those respondents reported high interest

rates, and nearly one third of those respondents reported concerns related to unfavorable repayment terms. If the Bureau is to deliver on its section 1071 responsibilities, it must remain careful not to further speed the consolidation and homogenization of the small business lending market.

Covered Financial Institutions

While section 1071 defines "financial institution" to include a reasonably expansive list of different types of entities that may engage in small business lending, section 1071 establishes neither a metric nor a threshold by which to identify those from whom Congress anticipated the Bureau would collect small business lending data. Under the Proposed Rule, any entity meeting section 1071's definition of a financial institution that originated at least 25 covered credit transactions for small businesses in each of the two preceding calendar years would be a covered financial institution. The Proposed Rule's 25 loan-volume threshold was the lowest, non-zero loan-volume threshold considered by the Bureau in prior section 1071 rulemaking exercises.

The Bureau anticipates it could lower one-time section 1071 compliance costs by roughly $120 million and still collect section 1071 data for approximately 94 to 95 percent of all small business loans made by depository institutions if it establishes a 100 loan-volume threshold. However, it is obvious that a 100 loan-volume threshold is much too low still. For decades, mortgage market stakeholders have drawn statistically significant conclusions about the health and fairness of the mortgage market from data collected and reported subject to the *Home Mortgage Disclosure Act* (HMDA), which, the Bureau has estimated, captures something just shy of 90 percent of all available mortgage data. Establishing a 100 loan-volume threshold or any other loan-volume threshold that operates to capture more section 1071 data than is necessary at the expense of small business borrowers runs perfectly counter to the Bureau's section 1071 responsibilities.

Compounding this concern is the Bureau's reliance on NCUA 5300 Call Report data and similar banking industry data. A great deal of small business lending occurs below the relevant $50,000 reporting thresholds. The Bureau may welcome larger covered financial institutions' being required to report even more section 1071 data than the Bureau now projects. However, the Bureau should be deeply concerned that its overreliance on Call Report data risks the Bureau materially underestimating how many credit unions would likely be covered financial institutions under artificially low 25 and 100 loan-volume thresholds.

NAFCU encourages the Bureau to adopt a covered financial institution loan-volume threshold not lower than 500 covered credit transactions.

Chilling Effect on New and Modest Small Business Lenders

The Bureau acknowledges that some credit unions, faced with the Proposed Rule's significant one-time and ongoing compliance costs, may simply be forced to exit small business lending altogether. Other credit unions, the Bureau anticipates, will attempt to manage their small business lending activities so as to narrowly avoid crossing whatever loan-volume threshold the Bureau ultimately adopts. While it is theoretically possible that a credit union or bank could manage its small business lending activity in such a way as to avoid crossing a loan-volume threshold, the

theory quickly erodes when one considers the fluidity and iterative nature of most small business lending.

Small business lending, particularly at credit unions, is often the product of a lengthy, relationship-intensive process that unfolds over weeks, months, and, sometimes, years. Credit unions and entrepreneurs work diligently alongside one another to understand small businesses' strengths and capital needs and identify appropriate small business solutions. Consider the simplest context, one in which a credit union has never engaged in a credit transaction covered by the Proposed Rule. Aware that not all credit applications are approved and not all approved credit applications result in a member accepting the approved terms, the credit union would rationally work to cultivate small business relationships in excess of its targeted loan-volume. During years-long periods in which application approvals and borrower acceptances are above average, or emergencies press a credit union to redouble its commitment to its community, can the credit union truly be expected to abandon or stall its small business members the moment it unexpectedly meets its target loan-volume?

Next, consider one of the thousands of credit unions that may wish to better support their small business members by beginning to offer an affordable small business credit card product. If a credit union was simultaneously managing its small business lending activity to ensure it is not exposed to section 1071 compliance costs it is unable to afford, every new small business credit card account would represent one fewer traditional small business loan it could make, irrespective of a small business member's need. Similar examples are not in short supply, but the effect of each is the same. Credit unions' reliably managing small business lending activity to a specific loan-volume is simply implausible, if not impossible. More likely, these credit unions, too, would be forced to avoid or exit small business lending altogether.

In conversations with members, NAFCU has observed that anxiety regarding section 1071's future costs may already be having a chilling effect on future plans to expand small business lending operations. After the passage of the *Coronavirus Aid, Recovery and Economic Security Act* (CARES Act), credit unions expressed optimism that public awareness of the PPP's funding might enhance general demand for SBA loans. Credit unions who had never previously sought to promote small business loan products also expressed interest in sustaining small business lending even after the PPP was exhausted. However, after the Bureau's section 1071 rulemaking efforts were more widely publicized in September 2020, some credit unions expressed hesitancy about pursuing small business lending due to uncertainties surrounding the costs of section 1071 compliance.

According to a 2011 study from the SBA[1], while banks tend to reduce lending during economic stress, credit unions continue to lend to small businesses. During the Great Recession, credit union lending offset a proportional reduction in bank lending.[2] The Bureau's January 2020 data point found the number of credit unions offering small business lending products doubled since 2004, from 10 percent to 20 percent. As big banks continue to avoid historically-disadvantaged

[1] James A. Wilcox, The Increasing Importance of Credit Unions in Business Lending, SBA Office of Advocacy (Sept. 2011).
[2] NCUA, Member Business Loans; Commercial Lending; Final Rule, 81 Fed. Reg. 13530, 13532 (March 14, 2016).

communities and desert short-lived efforts in others and as community banks continue to merge, the Bureau must be keenly aware of the Proposed Rule's ability to chill small business lending by credit unions, sometimes the only in-community option remaining for small businesses.

Covered Applications

NAFCU appreciates the Proposed Rule's providing that "a financial institution has latitude to establish its own application process or procedures". Small business lending, particularly at credit unions, is often an iterative process tailored to borrowers' unique needs and not a rote walk-through or fill-in-the-blank template.

NAFCU is, however, concerned by the Proposed Rule's not adopting Regulation B's definition of a "complete application". The Bureau's adopting a "complete application" definition, as opposed to the Proposed Rule's comparatively open-ended definition of an application, would alleviate the significant burden covered financial institutions would have in collecting section 1071 data from unengaged applicants who have no intention of completing the application process. Unnecessary compliance costs that would in short order translate to higher small business borrowing costs would be avoided, and the integrity of valuable section 1071 data on the most important small business lending activity would be protected.

While it may be convenient for the Bureau to have data regarding incomplete applications when it explores fair lending issues related to borrower discouragement, there is no indication that Congress intended for section 1071 to mirror the requirements found in the HMDA and Regulation C. Furthermore, it appears plausible that many incomplete applications could be the product of borrower confusion regarding the need to supply unfamiliar, deeply personal data points rather than the product of borrower discouragement. To the extent that borrower discouragement intersects with more easily measurable fair lending concerns, the Bureau will have more than sufficient section 1071 data, in addition to its existing examination authorities, to investigate ECOA violations involving small business lending products.

Small Business Definition

The Proposed Rule would define a small business as any business with prior-year gross annual revenue of $5 million or less. NAFCU supports regulation that enables credit unions to more quickly and confidently support their communities' small businesses. Also, as previously expressed, NAFCU appreciates the obvious benefits of any easy to apply small business definition based on gross annual revenues. However, as discussed more fully in other sections, credit unions generally anticipate being forced to pass along their section 1071 compliance costs to small business borrowers in the form of higher fees.

Small business lending fees are, like many sales taxes, regressive in nature, disproportionately expensive for small businesses borrowing the least. It is altogether possible that fees for the smallest dollar small business lending products could increase to such a proportion that the smallest dollar products altogether disappear from the small business lending market or are offered only by the least scrupulous, least regulated small business lenders. A gross annual revenue

threshold must, therefore, operate to cost-effectively capture only the data reasonably necessary to enable stakeholders to draw statistically significant conclusions about the health and financial needs of truly small businesses.

Based on the underwriting experiences of its members, NAFCU recommends that the Bureau adopt a small business definition based on a $1 million prior-year gross annual revenue threshold.

Covered Credit Transactions

The Proposed Rule broadly defines a covered credit transaction to include any extension of business credit other than trade credit, public utilities credit, securities credit, and incidental credit, which are expressly excluded. The Bureau anticipates explaining in the Official Commentary that factoring, leases, consumer-designated credit used for business purposes, and credit secured by certain investment properties are not covered credit transactions. Under the Proposed rule, credit unions' small business loans, lines of credit, and credit cards would all be covered credit transactions. If a credit union offers its small business members a merchant cash advance (MCA) product, that too, would be a covered credit transaction under the Proposed Rule. To gauge the size and distribution of the small business lending market comprised of these products, the Bureau relied on 2019 NCUA Call Report data and similar banking industry data. However, the Proposed Rule offers no *de minimis* threshold below which an otherwise covered credit transaction would not count toward a financial institutions' loan-volume threshold.

NAFCU recommends that the Bureau put its assumptions into practice and establish a *de minimis* threshold applicable to all covered credit transactions that tracks the NCUA Call Report threshold, currently $50,000. Congress' decision to exclude member loans under $50,000 from credit unions' MBL caps and the NCUA's corresponding decision to exclude such loans from Call Reports reflect a general, reasoned understanding that burdensome reporting requirements frustrate very small businesses' access to affordable, high-quality small dollar loans. Small dollar loans are particularly important to sole proprietorships. And, as the Bureau makes extensive note, the majority of women- and minority-owned businesses are sole proprietorships. In the alternative, NAFCU recommends that the Bureau delay any further section 1071 rulemaking until the Bureau is prepared to present a more transparent methodology describing the likely coverage of financial institutions based on lower covered credit transaction thresholds.

NAFCU also recommends that the Bureau expressly exclude small business credit cards from the Proposed Rule's definition of a covered credit transaction. An informal survey of a cross section of NAFCU members suggests that the vast majority of credit unions' new small business credit card account limits are well below the NCUA 5300 Call Report threshold – with median limits hovering tightly around $10,000. NAFCU understands from other industry stakeholders that similar trends persist in nearly every identifiable sub-section of the banking industry.

Under the Proposed Rule, as written, a credit union's approving even marginal small business credit card account limit increases would push the credit union closer toward whatever loan-volume threshold the Bureau ultimately adopts. It seems likely, therefore, that absent the Bureau either establishing a meaningful *de minimis* threshold or expressly excluding small business credit

cards from the Proposed Rule's definition of a covered credit transaction, every credit union that offers even a single small business credit card product will ultimately become a covered financial institution on that basis alone. Furthermore, the Bureau estimates that roughly three-quarters of credit unions do not yet offer a small business credit card product. Any one of that number that subsequently offers its small business members an alternative to high-fee, high-interest small business credit card products pushed by big banks and fintechs would likely find itself soon exposed to the Proposed Rule's extraordinary compliance costs, irrespective of any other small business activities.

NAFCU supports the Bureau's exclusion of consumer-designated credit transactions from the Proposed Rule's definition of a covered credit transaction and recommends that the Bureau further clarify that it will not challenge a credit union's designating an otherwise covered credit transaction to be a consumer-designated credit transaction. NAFCU believes that preserving such discretion is critical to mitigating overall section 1071 compliance risks given covered financial institutions have no reliable method for validating a latent business purpose in an application for a consumer-designated credit transaction.

Finally, because NAFCU believes it is unlikely Congress intended to include commercial real estate loans made to investors within the scope of section 1071, NAFCU again recommends that the Bureau consider expressly exempting such loans from the Proposed Rule's definition of a covered credit transaction rather than rely on the Official Commentary's operation. It is often the case that these loans' relevant data are already reported under the HMDA. Additionally, commercial real estate loans made to investors are typically made to business entities with complex ownership structures that make it difficult for financial institutions to determine even the identity of all of a borrower's principal owners.

Mandatory Data Points

Credit Purpose

NAFCU recommends that the Bureau further clarify how covered credit transactions should be reported when they are made directly to the sole proprietor of a business, not to the business directly. Credit unions engaged in small business lending to sole proprietors individually may find it confusing to report a loan purpose that implies that the business itself is the recipient.

Amount Applied For

NAFCU recommends that the Bureau grant financial institutions the discretion to report an "amount applied for" that is determined at later stage, rather than at the first request of the applicant, because reporting the first initial credit request could inaccurately represent the lending process. Particularly in transactions involving real estate or equipment, many small businesses will request a much higher loan amount than what is ultimately approved after evaluation of collateral. For startups and sole proprietorships, a lack of sophistication can also lead to similarly unrealistic initial requests. In these cases, credit unions work diligently with applicants to arrive at a more reasonable amount, but such education could take place over a period of weeks or months.

Census Tract

The geocoding requirement will be a source of significant burden for many credit unions, the vast majority of which do not collect census tract information for small business loans. Although some Community Financial Development Institution (CDFI) credit unions collect census tract information, many are completely unfamiliar with how to collect this information—particularly those that are exempt from the HMDA's reporting requirements. Those credit unions that do not use the Federal Financial Institutions Examination Council's (FFEIC) geocoding tool to collect census-tract information will need to acquire a separate software license from a vendor to implement geocoding. There may also be separate related costs for periodic system upgrades.

The FFIEC geocoding tool also does not permit batch inputs, which further slows more manual application processes at credit unions. For credit unions with limited staff, such a bottleneck could mean losing business as members frustrated by longer approval times look elsewhere. NAFCU, therefore, recommends that the Bureau develop a free tool for use by covered financial institutions that permits batch inputs and better enables covered financial institutions to more efficiently, cost-effectively fulfil their section 1071 responsibilities.

Protected Demographic Information and Visual Observation

Under the Proposed Rule, in certain circumstances, a covered financial institution's employee would be forced to determine the ethnicity and race of a small business applicant's principal owner via visual observation.

NAFCU unequivocally opposes the Bureau's adoption of any regulation or examination practice that operates to require that any individual make any visual observation concerning any protected demographic information or similarly sensitive data of a small business applicant's owners. Humans have immense and persistent difficulties accurately and precisely identifying others' race and ethnicity[3]. Routinely inaccurate visual observations of this sensitive data would not only threaten the integrity of other valuable section 1071 data but would add unnecessary friction to small business relationships and give rise to avoidable, unreasonable fair lending risks.

The Proposed Rule's requiring, in certain instances, that a covered financial institution's employee make visual observations of protected demographic information may, too, expose covered financial institutions to compliance costs related to an evolving patchwork of state personal data privacy laws. While some states' personal data privacy laws provide financial institutions an institution-level exemption, at least one state, California, provides financial institutions only an information-level exemption.[4] To the extent protected demographic information is deemed not to be collected "subject to" or "pursuant to" the *Gramm-Leach- Bliley Act*, Californians may have

[3] Goldstein, A. G., and Chance, J. (1978). *Judging face similarity in own and other Races*. J. Psychol. 98, 185–193; Meissner, C. A., and Brigham, J. C. (2001). *Thirty years of investigating the own-race bias in memory for faces a meta-analytic review*. Psychol. Public Policy Law 7, 3–35.
[4] Cal. Civ. Code § 1798.145(c)

certain robust personal data privacy rights with respect to their visually observed protected demographic information collected and maintained by covered financial institutions.

Discretionary Data Points

Section 1071(e)(2)(H) requires financial institutions to collect and report "any additional data that the Bureau determines would aid in fulfilling the purposes of [section 1071]." The Proposed Rule would require covered financial institutions to collect and report the following eight discretionary small business lending data: pricing, time in business, North American Industry Classification System (NAICS) code, number of workers, application method, application recipient, denial reasons, and number of principal owners.

In light of the significant one-time and ongoing section 1071 compliance burdens already facing covered financial institutions with respect to their collection and reporting of mandatory data, NAFCU opposes the Bureau's adoption of any discretionary section 1071 data points. The Proposed Rule's discretionary data points represent data that is neither materially useful in fulfilling the ultimate objectives of section 1071 nor reliably obtainable by cost-effective means. NAFCU anticipates that any section 1071 final rulemaking will tend to widen the competitive gulf between credit unions and big banks and fintechs that have the economies of scale and the technological sophistication to automate complex functions. The Bureau's requiring covered financial institutions to collect and report even more, discretionary section 1071 data will only compound credit unions' competitive disadvantages.

For example, NAFCU members who participated in the PPP noted that many small business applicants either did not know what a NAICS code was or how to determine which NAICS code most closely matched their business. Manually collecting just this data point will require a credit union to devote a significant amount of time and resources to ineffective education. One statutory purpose of section 1071 is to facilitate enforcement of fair lending—a goal that is not sector dependent. The identification of business and credit needs can be accomplished without explicit reference to NAICS codes, such as by leveraging already existing data sources and voluntary surveys of business owners. Furthermore, sector-specific analysis of business credit supply and demand is best left to the SBA, which already collects NAICS information through its lending programs.

The risks of the Bureau's collecting the Proposed Rule's discretionary data is not limited to increased compliance costs that drive small business lending costs higher. The Bureau's collection and ultimate reporting of small businesses' time in business, NAICS code, and number of workers, coupled with census tract information, raises serious concerns about small businesses' privacy. Such discretionary data, when made public, could be used to re-identify small business borrowers and help competitors gain impermissible insight into financial information directly bearing on small businesses' long-term financial health and competitive goals.

Firewall

Section 1071 generally contemplates the existence of an information firewall between employees handling inquiries about a small business applicant's status as a women-owned, minority-owned, or small business and those employees engaged in underwriting. Under section 1071(d)(2), if a financial institution discovers that an underwriter or others involved in making a determination regarding an application "should have access" to such information, it must provide an applicant a notice of "the access of the underwriter to such information, along with notice that the financial institution may not discriminate on the basis of such information."

Unfortunately, the Proposed Rule's low loan-volume threshold and expansive covered credit transaction definition will likely operate to require the distribution of the proposed section 1071 information firewall disclosure far more often than Congress intended. Too frequent distribution will produce untenable, negative real-world effects that weigh most heavily on those the regulation is intended to protect.

Many credit unions have small business lending departments comprised of three or fewer employees. Small business lending at such credit unions across the country is more often than not an all-hands-on-deck effort. In operation, the Proposed Rule threatens to create the powerful illusion that these modestly-staffed credit unions are incapable of guaranteeing that protected demographic information will not affect an underwriting decision. The effect will likely be particularly pronounced with respect to women- and minority-owned small businesses, the entrepreneurs of which routinely come face-to-face with the realities of their relative economic disadvantages. A rational entrepreneur of a women- or minority-owned small business would be forced to consider accepting higher interest rates and other onerous credit terms in exchange for the relative peace of mind that a big bank's or fintech's seemingly limitless technology and personnel budgets ensure that protected demographic information remains shielded from underwriters.

The Bureau cannot eliminate the section 1071 information firewall disclosure's giving the appearance that credit unions are incapable of adequately shielding protected demographic information from underwriters. But the Bureau should reduce the need for its distribution by adopting section 1071 regulation with common sense definitions and right-sized thresholds.

Reputational Risks Related to Statutory Limitations and Future Balancing Test

As NAFCU has noted more fully in prior comment letters, the publication of small business data from credit unions risks presenting a misleading portrait of overall credit availability due to variables such as field of membership and aggregate MBL limits. As a result of these unique statutory restrictions, credit union lending patterns may not translate easily when compared to other institutions. Accordingly, it is imperative that the Bureau supply a transparent description of the methods and analysis it will apply when evaluating section 1071 data for supervisory purposes.

The Bureau should also recognize that some credit unions may respond to perceived reputational risks associated with data publicization by eliminating certain product offerings or modifying

underwriting practices in a way that reduces the overall diversity of small business products. In such a scenario, small businesses could ultimately find it more difficult to acquire credit on favorable terms if financial institutions seek to flatten pricing artificially because they are concerned by the outward appearance of such discrepancies, even when no discrimination, in-fact, exists.

Credit unions may also need to allocate additional resources to respond to inquiries about section 1071 data from NCUA examiners, who will be performing fair lending analysis of section 1071 data for the first time. To help credit unions better assess possible reputational concerns, the Bureau must also provide a full and complete explanation of any balancing test it intends to use to limit public disclosure of section 1071 data. Merely referencing a conceptual framework and then articulating the full policy later, as the Bureau does in the Proposed Rule and did with the HMDA, will not suffice. For credit unions to accurately assess the full range of privacy and reputational impacts that might be associated with any proposal, there must be a complete understanding of how the balancing test will be applied. For example, credit unions might approach their assessment of the costs of collecting certain data items by considering how it might be used to reidentify a borrower. The risk of reidentification cannot be fully known unless the Bureau provides a complete description of how a balancing test or other methodology for limiting public disclosure works.

One-Time and Ongoing Compliance Costs

NAFCU is significantly concerned that the Bureau has materially underestimated the one-time and ongoing costs credit unions are likely to face under the Proposed Rule. While, like others, NAFCU's members have had insufficient opportunity to explore all options, early indications are that third-party training, information technology, and auditing expenses are likely to be several multiples higher than the Bureau's estimates.

The Bureau's estimates with respect to training, for example, tend to reflect a scenario in which the only staff trained on section 1071 compliance are those staff for whom section 1071 data collection and reporting are a primary, largely autonomous job function. Such a scenario may be realistic at the smallest credit unions that have only two or three staff engaged in business lending and at the very largest credit unions with dedicated fair lending compliance departments. However, for credit unions with modest but not minimal staff, such an expectation ignores the fact that it is often the case that all or most employees are trained on all compliance issues to promote cross-functional efficiencies. Expenses may be driven higher still if the Bureau adopts an insufficient mandatory compliance schedule.

Mandatory Compliance Schedule

The Proposed Rule's 18-month mandatory compliance schedule would be aggressive even for the largest, most technologically savvy credit unions. As discussed above, the vast majority of credit unions likely to be covered financial institutions under the Proposed Rule will be forced to rely on multiple IT vendors to develop, redeploy, and cross-test section 1071-compliant small business lending programs and tools. Furthermore, many credit unions, because they are exempt from the HMDA's reporting requirements, have no preexisting HMDA software solutions or IT vendor

relationships to leverage. These credit unions will require even more time to come into compliance with robust, technology-intensive section 1071 regulation.

Past experience with the Bureau's implementation of the HMDA suggests that the Bureau is likely underestimating the time required for IT vendors to adapt their products to comply with major rulemakings. Relatedly, many NAFCU members who entered the small business lending market for the first time through the PPP to help local businesses reported having done so by relying on existing resources, not new technologies or other efficiencies. That some credit unions may now provide a more diverse range of products does not necessarily equate to greater sophistication or reduced reliance on manual systems. Credit unions across the country have simply worked harder for longer to support their communities' small businesses during the COVID-19 pandemic.

NAFCU strongly encourages the Bureau to adopt a phased mandatory compliance schedule based on covered financial institutions' loan-volumes that begins no sooner than three years following the Bureau's adoption of a section 1071 final rulemaking. The credit unions, which have the least bargaining power with powerful third-party IT vendors are often the last to receive core system upgrades and must have the time necessary to become fully compliant with a section 1071 final rulemaking.

Coordination of Examinations

Unlike mortgages, which are largely homogenous consumer products, small business loans can vary widely in design and purpose. Accordingly, prudential regulators' examiners applying the same analytical techniques and examination approaches applicable to the HMDA's enforcement to small business data may yield erroneous results. Absent a clear description of the methodologies that might be employed to perform fair lending analysis using section 1071 data, there will likely be a period where prudential regulators' examiners' expectations are in flux and, perhaps, materially inconsistent. To the extent that credit unions are subject to section 1071 reporting, the Bureau must coordinate with other FFIEC agencies, including the NCUA, to develop model examination procedures in advance of the Bureau adopting a section 1071 final rulemaking.

Small Business Lending Data Collection and the SBA

If the SBA again engages in direct small business lending, as a legislative proposal contained in the *Build Back Better Act* would permit, small business borrowers would face two material, perhaps not obvious, risks – higher borrowing costs and a consolidated small dollar lending market. The Bureau cannot be held responsible for the actions of agencies, but the Bureau must remain keenly aware that its section 1071 rulemaking has significant impacts on a small business lending market shaped by powerful private and public competitive pressures.

First, the Proposed Rule's Official Commentary specifically includes "governmental lending entities" within the definition of a financial institution. While the SBA's balance sheet and reach may more closely resemble those of big banks and fintechs than those of a credit union, the SBA, as the PPP made clear, is significantly reliant on manual information processing and the smooth functioning of the individual offices within its vast network. If the SBA engages in direct lending,

it will no doubt meet the Proposed Rule's definition of a covered financial institution. With the lessons of the last two years firmly in mind, the SBA would likely find it necessary to train nearly all employees on section 1071 compliance to ensure modestly staffed offices can meet their section 1071 responsibilities in times of pronounced small business needs. To offset these and other costs related to the collection and reporting of section 1071 data, the SBA would likely be forced to raise the costs of small business lending products that are, for some borrowers, the best available option.

Second, if the SBA again engages in direct small business lending, the SBA would threaten all credit unions' disintermediation in the increasingly important small dollar segment of the business lending market. Not only does the legislative proposal lack the statutory guardrails to prevent the SBA from becoming credit unions' direct lending competitor, but the legislative proposal also risks fintechs, who have never been permitted to originate 7(a) loans, driving credit unions entirely out of 7(a) lending. The legislative proposal's net effect of increasing private-sector competition for ever fewer private sector SBA lending opportunities will chill credit unions' 7(a) lending and lead to a consolidation of small dollar lending to the detriment of small businesses.

As the Bureau contemplates its section 1071 final rulemaking, NAFCU encourages the Bureau to remain keenly cognizant that its decisions will bear mightily on a profoundly complicated and rapidly changing small business lending market. The Bureau cannot be expected to alleviate all the ill-effects of a potential SBA direct lending program, but the Bureau should ensure that its section 1071 final rulemaking does not unnecessarily compound small dollar lending price increases or speed the small dollar lending market's consolidation.

Relatedly, NAFCU encourages the Bureau to oppose an SBA direct lending program and expressly exclude loans extended by depository institutions and backed by a governmental entity from its section 1071 final rulemaking's definition of a covered credit transaction.

Conclusion

NAFCU appreciates the opportunity to comment on the Bureau's Proposed Rule. Section 1071 of the Dodd-Frank Act was written to address economic inequalities much older than even our first form of federal government. That the Bureau approaches such an awesome responsibility at a time when the small business lending market has changed more in the last two decades than in the preceding two centuries makes the Bureau's task all the more challenging. As the Bureau helps this nation move meaningfully along a path to economic inclusion for all, the Bureau must avoid speeding the small business lending market's consolidation and homogenization, particularly at a time when many truly small businesses are only beginning to recover from the shocks of the COVID-19 pandemic.

NAFCU strongly encourages the Bureau to adopt common sense definitions, right-sized thresholds, a reasonable, phased mandatory compliance schedule, and other changes to the Proposed Rule that protect small businesses' access to affordable, high-quality credit from trusted, in-community credit unions.

If you have any questions or concerns, please do not hesitate to contact me at dbaker@nafcu.org or 703-842-2803.

Sincerely,

Dale Ross Baker

Dale R. Baker
Regulatory Affairs Counsel



March 30, 2023

VIA ELECTRONIC FILING

Representative Nydia M. Velázquez (NY-7)
2302 Rayburn House Office Building
Washington, DC 20515
Phone: (202) 225-2361
Sent Via Email: Peter.Johnson2@mail.house.gov

RE: Testimony for House Committee on Small Business hearing titled "The End of Relationship Banking? Examining the CFPB's 'Small Business Lending Data Collection' Rule" held on March 28, 2023

Thank you for this opportunity to submit a written comment on behalf of the National Community Reinvestment Coalition (NCRC) and our over 600 community organization members that work with financial institutions and government agencies to expand economic opportunity in their neighborhoods. We are submitting this as part of the official record for the hearing on March 28th, and more information on our analysis of the Consumer Financial Protection Bureau's (CFPB) proposed 1071 rule can be found in our submitted comment on the CFPB's proposed Section 1071 rulemaking, also available on our website.[1]

The implementation of Section 1071 (1071) is a tremendous opportunity that will have widespread benefits. By increasing transparency of pricing, terms and conditions, and action taken on applications, 1071 data is likely to curb excessive pricing, reduce abusive terms, and increase access to credit for traditionally underserved small businesses. Lenders will also realize benefits in terms of improved ability to gauge their competitive position in the market and opportunities for them to serve new customers and identify untapped market segments.

Improvements to HMDA data in 1990 and 1993 corresponded with a 70% increase in conventional home purchase lending to African Americans, and a 48% increase in lending to Latinx borrowers, from 1993 to 1995.[2] Furthermore, a study by Citigroup estimates that fair access to lending for African American-owned small businesses alone would have resulted in $650 billion in additional business revenue per year, as well as created an additional 6.1 million jobs per year.[3] These massive increases in revenue and jobs will benefit the entire economic system, including lenders.

The proposed rule by the Consumer Financial Protection Bureau (CFPB) achieves the statutory purpose of Section 1071 of Dodd-Frank, and costs associated with compliance are

[1] "NCRC Comment on Proposed Section 1071 Small Business Lending Data Collection." NCRC. January 5, 2022. Available online at https://ncrc.org/ncrc-comment-on-proposed-section-1071-small-business-lending-data-collection/

[2] "Home Loans to Minorities and Low- and Moderate-Income Borrowers Increase in the 1990s, but then Fall in 2001: A Review of National Data Trends from 1993 to 2001." NCRC. Available upon request.

[3] "Closing the Racial Inequality Gaps: The Economic Cost of Black Inequality in the U.S." Citigroup. Available online at https://ir.citi.com/NvIUklHPilz14Hwd3oxqZBLMn1_XPqo5FrxsZD0x6hhil84ZxaxEuJUWmak51UHvYk75VKeHCMI%3D

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minimal when factoring in the income lenders generate from originations. Using costs calculated by the CFPB and minimum estimates of income from originations, one time and ongoing costs of compliance to deposit taking banks range from just .1% to 2.5% of annual income from originations of small business loans, which is just a portion of a depository institution's total income. Any passed-on costs to small business borrowers will also likely be modest, ranging from $7 to $28 in expected additional closing costs.

One Time Costs

Type of Bank or Savings Association	Minimum # of Originations For This Type	Net Income Per Origination - Minimum Estimate	Minimum Total Annual Income from Originations	Estimated One Time Costs	Ongoing Costs Percentage of Minimum Total Annual Income
A	25	$105,000	$2,625,000	$58,400	2.22%
B	150	$50,000	$7,500,000	$44,500	0.59%
C	1000	$237,000	$237,000,000	$75,700	0.03%

Ongoing Costs

Type of Bank or Savings Association	Minimum # of Originations For This Type	Net Income Per Origination - Minimum Estimate	Minimum Total Annual Income from Originations	Estimated Ongoing Costs	Ongoing Costs Percentage of Minimum Total Annual Income
A	25	$105,000	$2,625,000	$7,386	0.28%
B	150	$50,000	$7,500,000	$35,476	0.47%
C	1000	$237,000	$237,000,000	$243,266	0.10%

Combined One Time and Ongoing Costs

Type of Bank or Savings Association	Minimum # of Originations For This Type	Net Income Per Origination - Minimum Estimate	Minimum Total Annual Income from Originations	Estimated One Time and Ongoing Costs	Ongoing Costs Percentage of Minimum Total Annual Income
A	25	$105,000	$2,625,000	$65,786	2.51%
B	150	$50,000	$7,500,000	$79,976	1.07%
C	1000	$237,000	$237,000,000	$318,966	0.13%

The CFPB estimates that the proposed threshold of 25 loans would cover about 70% of all banks, and this threshold must be finalized in the upcoming final rule. The fair lending and community development purposes established by Dodd-Frank would be frustrated if the threshold of loans was increased to 50 or 100 loans. Setting thresholds this way would only cover 52%-56% of banks and savings associations at the 50 loan threshold, and just 33% at the 100 loan threshold. 1071 data would no longer be statistically representative of actual lending and would not be able to accurately reveal whether credit needs were being met in all communities, particularly in smaller urban areas and rural counties where smaller banks tend to be headquartered.

Also important to keep the proposal for lenders to provide demographic information when not provided by the applicants, and when a lender had an in person or teleconference meeting with one or more of the principal business owners. Without a visual observation and/or surname collection requirement when demographic information is not provided by the applicant, meaningful analysis of the 1071 data could be difficult and significantly undermine section 1071's fair lending purpose. Small Business Administration data from the first and second round of PPP loans, where demographic information was voluntary in the application, reveals that

about 75% of loan applications did not contain demographic data.[4] If anywhere near 75% of small business loans lack demographic data, section 1071 will be useless and not satisfy its statutory purpose of identifying fair lending risk. Furthermore, mortgage loan officers have experience reporting race based on visual observation and/or surname because the Home Mortgage Disclosure Act (HMDA) requires it, and small business loan officers will be able to do the same in meetings with one or more of the principal owners. The CFPB's proposed rule also establishes a firewall where lending staff involved in the credit decision would not have access to demographic data. CFPB offers an exception to the firewall when a lender determines it is not feasible to maintain this separation, which is likely for smaller lenders that have fewer staff. In these instances, the proposal is to notify applicants that staff involved in approving the loan would have access to demographic information, and that it is illegal for the lender to discriminate. We believe this is a reasonable exception.

The CFPB must also retain the discretionary variables it has chosen for collection in the final rule. Discretionary data points have been carefully chosen and reflect key factors in the loan approval process. Dropping the discretionary data points is estimated to save only $2-$6 on a per application basis. This is certainly not worth the price reduction, considering the loss in explanatory power the data would experience.

Implementation of 1071 will greatly increase understanding of the small business landscape, which has significant benefits for lenders, business owners, government agencies, and researchers. 1071 data will reduce the compliance burden of fair lending reviews for banks that are effectively lending to businesses owned by people of color and women since there will now be a reliable data source for analyzing lending and making comparisons to other lenders in the market place. Besides costs, which as already discussed are minimal when factoring in income from originations, only banks that have fair lending compliance issues in their small business lending should be concerned about improvements to small business lending data, and protecting discriminatory lending practices is an unacceptable policy position favored by no one. Furthermore, banks will now have a great data set that will allow them to assess demand and how small business needs are being served locally, including identifying untapped markets, which will greatly enhance the ability of banks to make sound business decisions as it relates to expansion plans and development of products.

Government agencies will be able to use 1071 data to identify additional opportunities to create new, or tailor existing, programs to advance their small business lending policy objectives. For example, government agencies often create programs that specifically target businesses owned by people of color and women, such as those that reserve government contracts, or provide grants. Government agencies could use 1071 data to improve existing programs or create new ones to meet the needs of these business owners.

For researchers, the 1071 data set will be similar to HMDA data that is regularly used in academic studies on the mortgage industry. 1071 data will greatly expand the ability of academic research to further understand the landscape of small business lending, which will also benefit lenders and government agencies as already discussed.

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[4] U.S. SMALL BUS. ADMIN., PAYCHECK PROTECTION PROGRAM (PPP) LOAN DATA – KEY ASPECTS – UPDATED AUGUST 20, 2020 2 (2020), https://www.sba.gov/sites/default/files/2020-08/PPP%20Loan%20Data%20-%20Key%20Aspects%2008212020-508.pdf.

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Finally, the implementation of Section 1071 is highly unlikely to reduce small business lending or discourage lenders from establishing relationships with businesses that present sound lending opportunities. The tendency of smaller banks to voluntarily report small business and small farm data suggests that data disclosure helps rather than hinders them as they assess marketplace opportunities and comply with CRA. In 2018, 157 or 22% of the 700 institutions reporting CRA small business loan data were smaller banks voluntarily reporting the data.[5] HMDA data was also enhanced in 2004 to require reporting of price information along with additional data points such as lien status. In 2004, 8,121 lenders reported HMDA data and by 2007 the number of reporters increased by 765 to 8,886. Over time, therefore, the number of HMDA reporters grew, which is inconsistent with the argument that data reporting and/or additional reporting requirements causes a decrease of lending or lenders.

Thanks again for the opportunity to submit this comment to the official record. Implementation of section 1071 data is a great opportunity to reduce ongoing disparities in access to small business credit, which has been well documented in studies conducted by NCRC, as well as many other studies conducted by agencies including the Federal Reserve and the Minority Business Development Agency.[6] Addressing these disparities will make economies more vibrant, and bring substantial benefits to all stakeholders, including lenders.

Thank you kindly for consideration of our views in this important matter. If you have any questions, please contact Kevin Hill, Senior Policy Advisor, at khill@ncrc.org or myself at jvantol@ncrc.org.

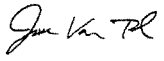
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[5] NCRC analysis of 2018 CRA small business data found via https://www.ffiec.gov/hmcrpr/cra_fs19.htm.

[6] "Disinvestment, Discouragement, and Inequity in Small Business Lending." NCRC. Testing results indicate that White testers were given significantly better information about business loan products, particularly information regarding loan fees where white testers were told about what to expect 44% more frequently than Hispanic testers and 35% more frequently than black testers. Available online at https://ncrc.org/disinvestment/. Also "Lending Discrimination with the Paycheck Protection Program." NCRC. Our report that found a difference of treatment in 27 out of 63 (43%) matched-pair tests with the White tester being favored over the Black tester in the pre-application arena. Available online at https://www.ncrc.org/lending-discrimination-within-the-paycheck-protection-program/ Also "Mind the Gap: Minority-Owned Small Businesses' Financing Experiences in 2018". Federal Reserve Banks of Atlanta and Cleveland. Finds that black-owned firms are less likely overall to be approved for financing, or to be approved at large or small banks, compared with white-owned firms. Relatively large share of minority-owned firms face potentially large unmet financing needs, as black-, Asian-, and Hispanic-owned firms are less likely than white-owned firms to report having sufficient levels of financing in place. Black- and Latinx-owned firms are less likely to turn to small banks and, contrary to previous analysis of 2016 Small Business Credit Survey data, are just as likely to turn to online lenders compared with white-owned firms after controlling for other firm characteristics—likely driven by the growth of online lender applicants among white-owned firms. Available online at https://www.atlantafed.org/community-development/publications/discussion-papers/2018/03-mind-the-gap-financing-minority-owned-firms-2018-09-14 Also "Disparities in Capital Access between Minority and Non-Minority-Owned Businesses." Minority Business Development Agency (MBDA). Finds that businesses owned by people of color received lower loan amounts than white-owned firms. This finding remained even after controlling for the sales level of firms. The average loan received by high-sales firms owned by people of color was $363,000 compared to $592,000 for white-owned firms. Available online at https://www.mbda.gov/sites/default/files/migrated/files-attachments/DisparitiesinCapitalAccessReport.pdf

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Sincerely,

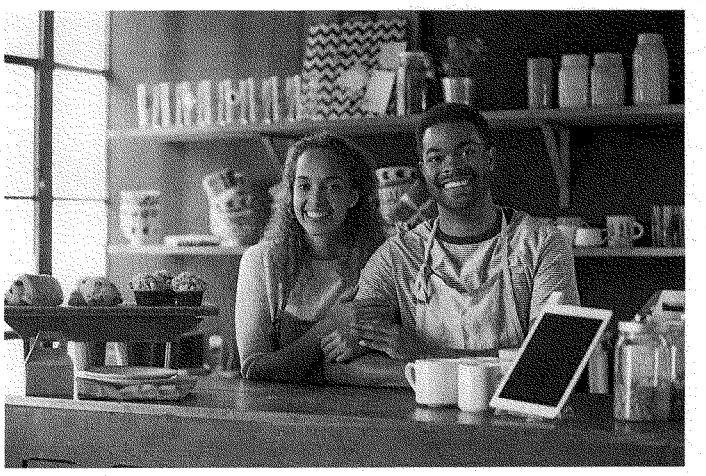


Jesse Van Tol
President and CEO

Three Bills Would Significantly Weaken Section 1071 Small Business Loan Disclosures » NCRC

ncrc.org/ncrc-fact-sheet-three-bills-would-significantly-weaken-section-1071-small-business-loan-disclosures/

February 24, 2022



Introduction

According to its statutory language, Section 1071 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 is designed to "facilitate enforcement of the fair lending laws and enable communities, government entities, and creditors to identify business and community development needs and opportunities of women-owned, minority-owned, and small businesses."[1]

The law requires the Consumer Financial Protection Bureau (CFPB) to collect and publicly disseminate data on applications and loans to small businesses. It mandates the collection of demographic data and other data on the characteristics of small business applicants, the action taken on applications and the census tracts in which the small businesses operate.

The philosophy behind Section 1071 is similar to that of the Home Mortgage Disclosure Act (HMDA) data: the public release of data will identify which lenders are making good faith

efforts to serve small businesses and which lenders lag their peers, encouraging the laggards through public accountability to increase their lending to traditionally underserved businesses. HMDA has had a significant impact on increasing home lending to people of color and modest-income borrowers, particularly in the years after 1989 when Congress mandated more demographic information in the HMDA data.[2] We expect a similar benefit from Section 1071 in narrowing the significant racial and gender disparities present in small business lending.[3]

Bills that Would Weaken Section 1071

H.R. 6732: The Small Lender Act: The bill would dramatically reduce the number of lending institutions that would report Section 1071 data, gutting its statutory purposes. In its proposed rule, the CFPB required lenders making more than 25 loans annually to report data. H.R. 6732 would raise this threshold to 500 annual loans that would need to be exceeded over two consecutive years.[4] Rep. French Hill (AR-02), the sponsor of the bill, and the bank trade associations supporting the bill claim that it will significantly reduce data collection costs for smaller lenders.

- Only a small minority of lenders would report data: The CFPB estimated that 70% of banks and savings and loans would be covered under the 25 loan threshold. This bill would drop coverage to less than one third of banks.[5] The resulting data would no longer enable the CFPB or the public to effectively monitor the fair lending performance of most banks, which directly frustrates the statutory purpose of Section 1071. In addition, assessing whether community needs are being met by lenders, which is the other major purpose of the law, would be thwarted in smaller cities and rural areas where these smaller loan volume banks are disproportionately located and have a significant market presence.
- Cost savings are minimal: The bank trade associations and the bill sponsors claim that data collection costs are so high that scores of community banks would cease making small business loans. This rhetoric glosses over the historical evidence. From 1996 through 2004, smaller banks were required to report CRA small business loan data. Their ranks were stable throughout this time period; data disclosure did not prompt widespread closures.[6] In addition, CFPB survey research reveals modest costs, which might cost borrowers from $7 to $30 in additional fees, minimal compared to the thousands of dollars of a typical loan. Lenders, including those from rural areas, told the CFPB that they were unlikely to exit the marketplace.[7] Finally, Community Development Financial Institutions (CDFIs), which are often smaller than community banks, already report this type of data to the CDFI Fund and do not find this reporting onerous.[8]

- Coverage of small business applicants would shrink: H.R. 6732 would also reduce the number of loans in the database by requiring that the data only be collected for small businesses with revenues of $1 million or less. The CFPB had proposed a threshold of $5 million, stating a "$1 million threshold…likely would not satisfy the Small Business Administration's (SBA's) requirements for an alternative size standard across industries and **would exclude too many businesses** designated as small under the SBA's size standards."[9] By eliminating too many businesses, H.R. 6732 would result in Section 1071 database not accurately revealing the experiences of small businesses applying for loans.
- Compliance date delayed: H.R. 6732 would delay the compliance date for three years after publication of the final rule in the Federal Register. The CFPB had proposed an 18 month time period. Congress passed Dodd-Frank and Section 1071 in 2010. Small businesses cannot afford to wait any longer for this important fair lending tool. Banks have had plenty of time to anticipate and plan for this data reporting requirement.

H.R. 6739: The Business Loan Privacy Act: Rep. Blaine Luetkemeyer (MO-03) erroneously maintained upon introduction of his bill that, "The Bureau refuses to tell us what information they will or will not make public, or even share how they plan to make that determination. Yet again, they are skirting the legal rulemaking process, this time threatening the privacy of small business owners across America."[10] Section 1071 requires the CFPB to assess privacy risk, the possibility that the data could inadvertently identify a particular small business applicant, and modify the data accordingly before public release. This bill would require the CFPB to propose a rule and ask for public comment on its privacy protection procedures.

- The CFPB has already asked for comment on privacy issues: The bank trade associations and their members have had plenty of time to comment just as the rest of the public. The CFPB released its proposed rule in early September; comments were due on January 6, 2022. This is a four month time period, which is longer than most public comment periods. The CFPB also described privacy issues over about 100 double-spaced pages, providing plenty of information from which the public could judge and use in their comments. Another public comment period would not be productive and only further delay the rulemaking.

- Privacy risks are minimal: The federal agencies implementing HMDA data over more than 40 years have yet to report a single instance of a borrower's identity being identified through use of HMDA data. The CFPB concluded that Section 1071 data would be very similar to HMDA data and would not pose a privacy risk.[11] In addition, just as with HMDA, some data points are likely to be modified upon public release to safeguard borrower privacy. Public sector datasets that advance a fair lending purpose have not led to identities being revealed. Lawmakers ought to focus more on private sector databases like Equifax, which revealed the identities of 143 million people through a hack of their database.[12]

H.R.6802: The Preventing Racial Profiling in Lending Act: Sponsored by Rep. Roger Williams (TX-25), this bill would prevent lenders from guessing upon visual observation the race or ethnicity of small business applicants in cases in which the applicants decline to provide this information.[13]

This procedure has been part of the HMDA regulation for decades.[14] It is an attempt to provide more data on the race and ethnicity of the loan applicant. The CFPB discussed in its proposed rule that data collected in this manner would not be used to identify small businesses as minority-owned and that its purpose was to provide the public with more data on race and ethnicity of small business owners.[15] The agency also discussed whether data collected in this manner should be "flagged" or identified as collected in this manner in the database so members of the public could use it at their discretion.[16] This is not an attempt to racially profile borrowers. Stakeholders have legitimate differences of opinion regarding this particular procedure but its intent is not malicious as the title of the bill suggests.

Josh Silver is a Senior Policy Advisor at NCRC.

Photo courtesy of Shutterstock.

[1] Section 1071 – Small Business Data Collection, Public Law 111–203—July 21, 2010, Dodd-Frank Wall Street Reform and Consumer Protection Act.

[2] NCRC Comment On Proposed Section 1071 Small Business Lending Data Collection, January 2022, https://www.ncrc.org/ncrc-comment-on-proposed-section-1071-small-business-lending-data-collection/

[3] For information about racial and gender disparities in small business lending, see NCRC comment and Acting Comptroller Discusses Modernization of the Community Reinvestment Act, OCC News Release 2022-15, February 14, 2022, https://www.occ.gov/news-issuances

/news-releases/2022/nr-occ-2022-15.html

[4] Press Release: Reps. Hill, Luetkemeyer, and Williams introduce bill to Protect Small Banks and Lenders, https://hill.house.gov/news/documentsingle.aspx?DocumentID=8895

[5] The CFPB estimated that a 100 loan threshold would result in about one third of banks reporting. Estimates were not provided for a 500 loan threshold. The public cannot readily estimate the impact of this dramatic proposal due to a lack of publicly available data, see CFPB Proposes Rule to Shine New Light on Small Businesses' Access to Credit, Proposal Would Increase Transparency in a $2.4 Trillion Sector of the American Economy and Bolster Fair Lending, September 1, 2021, p. 239, https://files.consumerfinance.gov/f/documents /cfpb_section-1071_nprm_2021-09.pdf

[6] Josh Silver, *Will Section 1071 Data Reporting Boost Lending To Underserved Small Businesses Or Lead To Consolidation And Reduce Product Choice?*, NCRC, February 4, 2022, https://ncrc.org/will-section-1071-data-reporting-boost-lending-to-underserved-small-businesses-or-lead-to-consolidation-and-reduce-product-choice/

[7] CFPB proposed rule, pp. 739 and 748.

[8] Comment letter of HOPE Enterprise Corporation, pp. 13-14, https://www.regulations.gov /comment/CFPB-2021-0015-1557

[9] CFPB proposed rule, see above for link, p. 273.

[10] Press Release, Luetkemeyer, Hill, Williams Conduct Oversight of CFPB's Small Business Data Collection, February 16, 2022, https://luetkemeyer.house.gov /news/documentsingle.aspx?DocumentID=400651

[11] CFPB proposed rule, pp. 607-609.

[12] Josh Silver, The Big Red Herring: The Home Mortgage Disclosure Act (HMDA) Will Help Predators Identify You!, NCRC, February 2018, https://ncrc.org/big-red-herring-home-mortgage-disclosure-act-hmda-will-help-predators-identify/

[13] Independent Community Bankers of America letter to Congress, February 2022, https://www.icba.org/docs/default-source/icba/advocacy-documents/letters-to-congress/letter-supporting-bills-to-modify-section-1071-proposal

[14] CFPB, *Collection and Reporting of HMDA Information about Ethnicity and Race*, January 2017, https://files.consumerfinance.gov/f/documents/201701_cfpb_hmda_ethnicity-and-race-collection_v2.pdf

[15] CFPB proposed rule, pp. 432-433, 446-449.

[16] CFPB proposed rule, p. 793.



Testimony for the Record

Submitted to the
House Committee on Small Business
Subcommittee on Economic Growth, Tax, and Capital Access

For the Hearing "The End of Relationship Banking? Examining the CFPB's 'Small Business Lending Data Collection' Rule'"
March 28, 2023

Submitted by the Responsible Business Lending Coalition

Chairman Meuser and Ranking Member Landsman, The Responsible Business Lending Coalition (RBLC) thanks you for convening an important hearing on the Consumer Financial Protection Bureau's (CFPB or "the Bureau") proposed rule to implement a small business financing data collection framework. We are grateful to the Ranking Member for inviting RBLC member Luz Urrutia, CEO of Accion Opportunity Fund, to serve as a witness in this hearing.

The Responsible Business Lending Coalition (RBLC) is the leading cross-sector voice on small business financial protection. The coalition includes nonprofit and for-profit fintechs, community development financial institutions, investors, and small business advocates who all share a commitment to innovation in small business lending as well as serious concerns about the rise of irresponsible small business lending.

We believe that every entrepreneur deserves access to responsible, affordable capital that will help their business thrive, not force them out of business. That belief is why the coalition created the Small Business Borrowers' Bill of Rights: the first cross-sector consensus on the rights that small business owners deserve and the standards of practice that financing providers should abide by to uphold those rights. Over 110 small business lenders, brokers, lead generators, and advocacy organizations have endorsed these standards.[1]

We appreciate that the U.S. House Small Business Committee convened this important hearing about the Small Business Lending Data Collection Rule, or Section 1071, as the

[1] Members of the RBLC include Accion Opportunity Fund, Camino Financial, Community Investment Management, Funding Circle, LendingClub, National Association for Latino Community Asset Builders, Opportunity Finance Network, Small Business Majority, and the Aspen Institute. For more information, including the responsible lending standards found in the Small Business Borrowers Bill of Rights, and the full list of Signatories and Endorsers, please visit www.borrowersbillofrights.org.

committee dedicated to supporting and growing a healthy, national small business economy. Whether we live in a small town or a big city, we can all agree that thriving small businesses enrich our communities and our lives. Small businesses need access to capital so they can grow and thrive. In order to support them, we need evidence-based data to develop smarter, commonsense policy solutions. Currently, there is no comprehensive information about how much small business financing is happening, who is receiving business financing products, and at what terms. By providing the first comprehensive and accurate information about the small business lending market, including where gaps exist, Section 1071 will spur innovation within banks, community organizations, fintech companies, and others, to address these gaps and improve small businesses' access to responsible capital. Section 1071 aims to fulfill this goal by mandating a national system to collect data about how small businesses access capital.

We view Section 1071 as a market-based, pro-innovation rule. More information will empower financing providers and the broader small business support ecosystem to better meet business owners' needs. Pricing transparency will increase competition in the market, driving down the cost of credit for small businesses and incentivizing providers to offer attractive terms. We believe the transparency created by Section 1071 will also spur innovation by encouraging adoption of the products and practices that the data reveal are effective in supporting underserved market segments.

It will also provide vital information on fair lending concerns that will enable regulators to identify and address violations. Specifically, this long-needed data collection will increase equity in the commercial financing marketplace by enabling regulators to identify Equal Credit Opportunity Act (ECOA) violations and by illuminating unmet credit needs that financing providers can help fill.

Having access to comprehensive data on small business financing applications will foster fairness and opportunity for all small businesses by illuminating the types of financing sought, approval rates, and pricing. Access to this data will allow financing providers and community development organizations to determine unmet credit needs and increase the supply of capital where needed. These reasons for the RBLC's support of Section 1071 are discussed further in our comment letter submitted to the Bureau in September 2017.[2]

To ensure full transparency within the small business financing market and adequately address gaps in small business capital access, it's critical that the rule apply to all business financing providers. We strongly support the proposed scope of applications subject to the data collection, including the broad definition of covered financial institutions; the collection of

[2] Responsible Business Lending Coalition, "Section 1071 and the Small Business Lending Market (Docket No. CFPB-2017-
0011)" Sept 2017.
http://www.borrowersbillofrights.org/uploads/1/0/0/4/100447618/final_rblc_letter_to_cfpb_on_1071.pdf

pricing data; the inclusion of merchant cash advances (MCA) under covered credit transactions; and the ultimate goal of establishing the first national repository of small business credit application and nondepository provider data. We emphasize the need to also include factoring financing as a type of product that is subject to the data collection.

The RBLC supports the Bureau's efforts to define "financial institutions" broadly, so that all financial institutions are required to comply with Section 1071's data collection and reporting requirements. This approach is simple and comprehensive, and enables regulators to assess the business and community development needs and opportunities for women-owned, minority-owned, and small businesses, as well as facilitate enforcement of fair lending laws across all institutions.

While nondepository lenders play a critical role in expanding access to capital for small businesses, the small business owners that RBLC member organizations serve have encountered particular issues with some nondepository financing products due to harmful terms and misleading pricing information. As the December 2021 Section 1071 Notice of Proposed Rulemaking (NPRM) notes, the design of both MCAs and factoring enables these products to avoid a formal designation as "credit" and resulting regulation, despite the fact that small businesses use both products to obtain credit.[3] However, there is currently a dearth of available data on nondepository credit applications, and particularly on commonly-used alternative products such as factoring and MCAs.

In order to fulfill Section 1071's congressional mandate of establishing the nation's first comprehensive small business lending database, the RBLC has advocated that the final rule include universal transaction coverage. If any commonly-used products are excluded under the final rule, researchers and policymakers will continue operating without a complete picture of the commercial financing market, and regulators will lack the data needed to enforce borrower protections on excluded industries. We strongly recommended that the Bureau include factoring as a covered product.

Factoring should be subject to the data collection framework because of fair financing concerns. No matter who they are, where they live, or how wealthy they are, every business owner deserves access to capital that will enable them to grow their venture. Factoring, as an available financing option, is identified in Federal Reserve research as a "potentially higher-cost and less transparent credit product" that has a disproportionate impact on minority-owned businesses, and Black-owned businesses in particular.[4] "Black-owned business applicants applied

[3] Consumer Financial Protection Bureau, "Small Business Lending Data Collection Under the Equal Credit Opportunity Act (Regulation B) Proposed Rule," December 2021. https://www.federalregister.gov/documents/2021/10/08/2021-19274/small-business-lending-data-collection-under-the-equal-credit-opportunity-act-regulation-b

[4] Federal Reserve Bank of Atlanta, "Small Business Credit Survey: Report on Minority-Owned Firms," Dec 2019. https://www.fedsmallbusiness.org/medialibrary/fedsmallbusiness/files/2019/20191211-ced-minority-owned-firms-report.pdf

for factoring more frequently compared to White-owned firm applicants (7% and 3%, respectively)."[5] We support factoring's inclusion in Section 1071 so that we can better understand how factors help or hurt vulnerable small businesses, just like any other financing product.

Conclusion

We look forward to continued dialogue with Members of the Committee on the need for more information about the challenges and opportunities that businesses encounter in the changing small business financing landscape. We believe that implementation of Section 1071 will result in a more innovative, inclusive, and fair financial system, particularly if all financing providers and products are subject to the data collection effort. Thank you again, Chairman Meuser and Ranking Member Landsman, for convening this important hearing.

Signed,
The Responsible Business Lending Coalition

Members include:
Accion Opportunity Fund
Camino Financial
Community Investment Management
Funding Circle
LendingClub
National Association for Latino Community Asset Builders
Opportunity Finance Network
Small Business Majority
The Aspen Institute

[5] *Id*

Testimony of Nick Powell,
Chairman, Colt Energy
Before the
Small Business Committee
Subcommittee on Rural Development, Energy, and Supply Chains
Highlighting the Role of Small Businesses in Domestic Energy Production
Room 2360
Rayburn House Office Building

March 29, 2023

Chairman Hunt, Ranking Member Perez, and Members of the Subcommittee, thank you for holding this important hearing and for allowing me the honor of testifying before you.

My name is Nick Powell, chairman and majority shareholder of Colt Energy.

I acquired the Mack C Colt Company in 1986. The Colt family started the business in the 1920s. It's an almost 100-year-old company that has always operated in Eastern Kansas. Our headquarters for operations is Iola, Kansas with a population of approximately 5,500. Iola is located in Allen County with a population of 12,500. It is engaged in oil and gas exploration, development, and production and gas gathering in eastern Kansas. Colt owns and operates over 150 producing oil and gas leases throughout the region with approximately 400 barrels of oil and 1,800 mcf of gas produced daily. Our wells are generally less than 1,200 feet in depth. Typically, 500 to 1,300 feet for oil, and for gas a little deeper. Our average oil well produces a little over 1 bbl per day and our average gas well produces 15 mcf per day. Colt currently employs 39 full time field, office, and management personnel. We also maintain our own service units including construction, drilling, well pulling and well washing crews.

Our employee wages average approximately $75,000 on top of which we add the following benefits: profit sharing, health insurance, 401k retirement plan with a 4% company match, short-term and long-term disability, paid vacation and sick leave, and life insurance.

We and other small oil and natural gas producers provide an important source of good-paying jobs in small communities throughout Kansas. We also provide tax revenue to counties in which we operate and to thousands of royalty owners who rely on their monthly checks.

So why is the current administration clearly trying to make it so hard and expensive to stay in business and produce the oil and natural gas that this country will need for decades to come.

In all my years in the business, I have never seen an administration take such a callous and unrealistic approach to energy policy. We have been hit with costly and confusing regulations from the day Biden became president. Many of which we have no idea how much it will cost to implement.

It used to be that previous administrations and congresses tried to protect small oil and gas operators from onerous regulations that had no real benefit for their cost. Now it seems just the opposite. Trying to eliminate percentage depletion, removing the marginal well exemption from Methane leak regulations and taxes to be collected on methane by the EPA to name a few.

The only purpose served by shutting down small producers while oil demand is still strong and will be for decades is to ship those jobs, revenue and secure energy supply to many of our adversaries that cause

much more environmental harm by their production process than US producers taking us back to dependency for our nation's energy supply.

President Biden opened the SPR and released 200 million bbls of oil into the market. This is an artificial and temporary increase in oil supply driving down prices hurting investment in long term real supply. This of course will lead to even higher prices in the future than existed before the release.

Percentage Depletion

While I recognize percentage depletion is outside the jurisdiction of this committee, its critical you and your colleagues understand its value and purpose.

It was established a number of years ago to provide a minimal but critical simple tax deduction to a limited scope of producers, those small upstream operators producing 15 bbls of oil or 90 mcf of natural gas per well per day with total production under 1,000 bbl/d.

Unlike other revenue producing assets, an oil or natural gas well after quickly reaching peak production goes into a study decline as it depletes the reserve from which it is producing. The only way to maintain production and therefore revenue levels to meet operating costs is to continue to drill more wells. The percentage depletion allowance was put in place to account for this situation in oil, natural gas and mineral extraction.

In terms of percentage depletion for these stripper wells, they are also low-margin wells because it costs a lot more in terms of man-hours to manage so many wells to get so little oil, so we've got higher operating costs per barrel, high lifting costs, whereas the majors might be $10 a barrel, we've got thinner margins, no cost depletion, and so that percentage depletion of 15% of gross income on a well has a big impact on your taxable income and allows needed income that can be put back into drilling and hiring.

So, maintaining percentage depletion is key to maintaining cash flow and continued efforts to drill. Because, if we drill less, production declines we have slower to no growth rates, and fewer, if any, people hired. Loss of domestic supply and the cascading adverse impacts.

Kansas, in particular, is almost exclusively a stripper well state. We have a lot of old wells where if you eliminated percentage depletion, you'd take a big chunk of wells and they'll just knock-off into the uneconomic category. We're people-intensive, when we're putting dollars into new wells, the ratio of that money going to people instead of steel and drilling rigs is much more people-intensive. A bigger share of our investment goes back into jobs instead of steel that is imported from overseas, it drives right back into local hiring. That hiring helps small communities that are struggling. In states like Kansas, we've become a pretty good employer in the areas we operate in.

Pending Taxes and Regulations

With the number and complexity of the regulations and tax proposals threatening our company we have to rely on our industry associations to monitor and keep us informed of these possible threats. We can't afford to have in house lawyers and regulatory and tax specialists on our payroll.
Two big regulation and tax issues they have been having us follow are the regulation of monitoring and repairing methane leaks and taxes to be collected by the EPA on methane.

Regarding the EPA's pending methane inspection and testing rule. I and many others I know on the small energy company spectrum, believe that under any regulation EPA issues, stripper/marginal wells should continue to be exempt as we have been under the previous rule issued during the Trump Administration (any operator that produced 15 barrels a day or less was exempt). However, the pending testing and inspection EPA rule eliminates that exemption.

It is important to note that generally emissions from our wells are minimal and often almost immeasurable. Don't take my word for it: The Biden Administration's DOE released a study of methane emissions from small producers has determined as much.

Oil leases owned and operated by our company were used in this DOE study. I have included with my written testimony a letter from our Executive Vice President who was on site to witness the tests. Once the test started they were concerned that their equipment was reading little if any methane and stopped the test to check their equipment. Turns out the equipment was good, there just was not much methane there to register on their equipment. And this turned out to be true for most low producing wells.

What is worse, is the level and frequency of inspection required of each facility and the nature of the reporting is truly unknow at this point. For a marginal operator, how those kinds of questions are answered are critical. And frankly, I and others are very concerned.

Second, let's take the Inflation Reduction Act's methane fee of $900 per ton, based on a CO2 emitted calculation and conversion which begins to kick in next year and would be a twin hit on top of the testing and inspection regulation, which could also significantly impact operations in terms of cost etc.

There are too many questions and concerns regarding the fee to take the committee's time here, but I can tell you that as I have looked at it, in terms of my company, I am very concerned about the cost, time and effort necessary to determine if I am covered.

These two examples don't take into consideration other costs of doing business that increased as supply issues surround shortage of steel pipe and casing for exploration for example have gone up, looming additional regulatory requirements associated with remediating and monitoring inactive or terminated wells, as well as general labor, fuel and operating costs.

So, when we are continuing to face some of the highest inflation rates we have seen in 40 years, small operators can ill afford any additional unnecessary costs or regulatory burdens..

Thank you, Mr. Chairman, once again for holding this hearing on the serious issues facing small energy companies.

I look forward to answering your questions.

Sincerely,

Nicholas K. Powell

Nicholas K. Powell, Chairman
Colt Energy, Inc.

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