Federation
Credit Unions United to Serve the Underserved

September 12, 2017

Ms. Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

Dear Ms. Jackson,

The National Federation of Community Development Credit Unions (the Federation) respectfully submits this letter in response to the Bureau's Request for Information, docket number CFPB-2017-0011, on the small business lending market required by Section 1071 of the Dodd-Frank financial reform legislation that requires financial institutions to compile, maintain, and report information concerning credit applications made by women-owned, minority-owned small businesses.

The Federation is the national trade association and community development financial institution (CDFI) intermediary for credit unions serving predominantly low-income and underserved consumers and communities. The Federation's more than 200 member community development credit unions (CDCUs) deliver safe and responsible financial products and services in low-income communities, often serving as the only alternatives to high-cost and predatory fringe lenders for consumers and businesses.

As a community development financial institution, the Federation firmly believes in the value of data collection to better understand the marketplace and to help identify and direct capital to address the gaps in the marketplace. This is particularly critical when reviewing lending to women and minority businesses that have historically lacked access to the capital necessary to grow and build their businesses.

The Federation is an intermediary and therefore not a direct lender to businesses. As such we will focus our comments on two principles that our members believe should guide the CFPB's deliberations and then provide responses to a handful of the questions contained in the RFI that most impact the ability of CDCUs to continue to offer high-quality, affordable loans to small businesses. The overarching principles are:

- **Data Collection efforts should be qualitative as well as quantitative.** Recent history has demonstrated that an influx of capital in underinvested areas and to economically disenfranchised populations can be destructive if the lending practices are irresponsible and the rates and terms are exorbitant. The CFPB data collection efforts should not only track the numbers of applicants; approvals and volume of lending to underserved business but also the rates and terms of that activity. It is important to track the terms and rates on lending to track where historical lack of access to capital to minority and women businesses does not give way to high-cost subprime lending. Given that the best lenders are often small local financial institutions it is important to not provide overly burdensome reporting hurdles and where possible to provide easy to use tools that can be integrated into core systems to be able to seamlessly extract the data.

- **Too narrow focus on decline rates could distort the bigger picture of how well financial institutions are trying to serve the marketplace.** As CDFIs our work is often focused on building a marketplace. To do this effectively, we must seek to reach as many potential borrowers as possible. Many of whom may not be able to productively use capital but can be provided with technical assistance and other supports while their building a strong and successful business plan. A strict focus on applications and declines could dissuade this type of development lending. We therefore urge the CFPB to track the overall activity of institutions as part of this data collection effort.

Below are responses to select questions in the RFI:

- **Defining a Small Business Loan for the Purposes of Data Collection**: Among our member CDCUs that lend to small businesses there are varying perspectives on the challenges involved with reporting based upon the SBA NAICS definition. Some lenders already track and report that data, others do not. The most straightforward and least burdensome method of tracking data on small business financing would be to simply track the activity by loan size. Credit unions define member business loans as those business loans exceeding $50,000. If the Bureau were to establish a threshold of $50,000 - $350,000, it would be accurately capturing the marketplace of small business lending in credit unions with no additional tracking burdens. If the definition had to be related to the business itself, we would recommend considering a small business as a business with fewer than 500 employees. Definitions should take into account entities that are related to the small business applicant, such as parents, subsidiaries and so on.

- **Data Collection varies for CDCUs:** Some CDCUs track data directly through their core data processing system or through a loan origination system integrated into the core. Others track this information manually and transfer the loan information in separately to the system. Any rules should take into account capacity limitations among lenders that are already filling critical gaps and should therefore be crafted to facilitate institutions of all sizes to be able to easily track and report information sought.

- **Data Sources:** For the most part, the information is self-reported by the borrowers with some data points verified by financial statements and third parties. Several CDCUs (particularly those that already report to the CDFI Fund) report tracking loans made in low-income and distressed target markets. Tracking information based upon geography could be an important source, however we would strongly urge that the Bureau either invest in or partner with a provider to offer a free tool for producing those reports based upon location of the business.

- **Identification of misinterpretation by regulators:** As with all lending in low-income and underserved markets, CDCUs constantly face misunderstanding and misinterpretation of risk from the NCUA. Additional data collection in small business lending could easily backfire if it provides a tool to overzealous examiners seeking to limit or even prohibit CDCU lending. Despite the fact that CDCUs that target their activities in underserved markets maintain equal loan portfolio performance to their peers serving higher income individuals, CDCUs must constantly educate their examiners about the viability and sustainability of serving low-income and\or credit challenged borrowers. The Bureau will need to take a proactive and comprehensive approach to educating their fellow regulators about the need and opportunity in serving underserved business borrowers. Moreover, data collection efforts should serve to provide the empirical evidence base that this type of lending activity does not carry higher risk.

- **Collecting and reporting information** on whether an applicant is a women-owned, minority-owned, or small business and the ethnicity, race, and sex of the principal owners of the business will be important to determine both capital gaps and potential for unfair access to capital for minority and women owned businesses. There are concerns that seeking data on loan applications on race and ethnicity of a borrower may have an adverse effect on borrower demand, with business principals fearing it would be used in the underwriting**.** It will be important for the process of data collection at financial institutions clearly stress that underwriting will remain based on the financial data of the business and some data collection efforts request information from the principals related to their status as women or minority are for the sake of federal reporting and fairness in lending.

- **Steps the Bureau can take to minimize burden** on financial institutions and applicants and facilitate compliance with the requirements to collect and report business demographics include simple, easy to use tools that can be easily integrated into business loan origination systems; providing the analysis of information such as geocoding of business location and

Barriers for Minority- and Women-owned Businesses

Access to responsible financing is essential for entrepreneurs to build and grow their business. Focusing on addressing capital gaps for minority and women owned businesses can greatly advance efforts to bridge the growing racial and gender wealth divides in this country. It is well documented that minority and women business owners have access to less formal credit and in smaller amounts. For example, the median dollar amount approved for black business owners are is less than half the loan amounts approved for white business owners. The plethora of online business lending has made capital more available than ever before for businesses. But similar to the subprime mortgage crisis and the explosion of consumer payday lending, the costs and terms can exacerbate existing inequities.

Toward this end, the collection and reporting on lending cannot be limited to the quantity of capital but must include the structure, terms and conditions of the financing. With the growth of new products such as short-term merchant cash advances, the rate a business can pay on such loans can exceed 50% annualized APR. These types of products may become the last resort of businesses in need of capital to sustain their operations but result in stripping those very businesses of the capital needed to invest in growth and future sustainability.

We support this effort and encourage the CFPB to define the scope of data collection to essential information on the business principals, provide easy to use tools to support those collection efforts, track quality of lending and finally to share the aggregated information publicly to allow CDFIs and other responsible lenders to continue to learn how to best address those capital needs.

Thank you for this opportunity to share our perspective.

Sincerely,

Cathie Mahon
President and CEO