November 3, 1999

Jennifer J. Johnson
Secretary, Board of Governors of the Federal Reserve System
Docket No. R-1008
20th Street and Constitution Avenue, NW
Washington, D.C 20551

Dear Ms. Johnson

Re: Comments on Regulation B Proposed Rule

The premise that governs Woodstock Institute's position on the proposed Regulation B rule is that small business loan disclosure should mirror the provisions in the Home Mortgage Disclosure Act for home mortgage disclosure data. Those data have permitted important analyses of the patterns of financial institutions home lending which in turn have been partly responsible for significant increases in that lending to lower-income and minority households.

There is plenty of evidence, some it presented at the Board of Governors' conference on small business lending earlier this year, that low-income neighborhoods and minority business owners suffer from disparate treatment in access to small business loans. Analyzing data from the Characteristics of Business Owners (CBO) database, Timothy Bates finds that banks make smaller loans to start-up firms located in minority areas than to firms in non-minority areas while controlling for financial equity, owner education, race, age, and experience. In a more recent study, Bates (1997) again finds that white-owned firms are able to attract larger amounts of debt than similarly situated black-owned firms. Woodstock Institute research on small business lending flows to different types of neighborhood in the Chicago metropolitan area, shows that lower-income and minority areas receive fewer loans after accounting for firm density, firm size, and industrial mix (Daniel Immergluck, 1999). David Blanchflower et al., (1998) using data from the 1993 National Survey of Small Business Finances show that even after controlling for differences in credit-worthiness and other factors that exist between black- and white-owned firms, blacks are still about twice as likely to be denied credit.

These studies, taken together, indicate the existence of the racial characteristics of owners and the income characteristics of neighborhoods still seriously affect the extension of small business credit. In consequence, the Federal Reserve Board and other regulatory agencies should be doing everything in their power to describe and eliminate disparate treatment and discrimination in small business lending. But without race data, it will in fact, be impossible for the bank regulators to effectively enforce ECOA. Again the parallel with home lending data is instructive. The U.S. Department of Justice and the regulators use HMDA data to identify lenders to investigate further.

<u>Voluntary Disclosure of Race and Gender Data, sec. 202.5</u>

In the absence of mandatory disclosure, the Institute supports the withdrawal of the prohibition on the collection of race and gender data. We view that withdrawal, however, as a first step towards mandatory disclosure. Mandatory disclosure has to be the final goal because of the enormous damage that disparate treatment and discrimination still cause in lower-income and minority communities and given the Board's responsibilities to enforce the Equal Credit Opportunity Act. Moreover, mandatory data disclosure is the only way to ensure that race and gender data are collected in a consistent, standardized form.

Privileged Data, sec. 202.15(b)(3)

Privilege from discovery now applies to certain data used by financial institutions to self-test against discriminatory practices. Data collected in the normal course of business and contained in regular loan files are not so privileged. The proposed rule maintains this key distinction. The Institute regards some banks' claims that all data collected in consequence of the removal of the race and gender prohibition should be so privileged as an *outrageous* diminution of ECOA and Regulation B. Financial institutions opposed HMDA and its revisions on the grounds that they knew they did not discriminate. Analyses of HMDA and other data proved them wrong and existing research strongly suggests claims of no discrimination in small business lending to be false. Small business race and gender data are needed to fine-tune those analyses as a tool for reducing discrimination and disparate treatment.

Definition of a Creditor, sec. 202.2(1)

Discrimination in lending often occurs at the point that brokers interact with prospective clients. Discrimination by a lending institution is encouraged when its loans are purchased by another institution if that second institution fails to analyze the loan packet for discriminatory or disparate lending practices. For these reasons, the language regarding assignees and referrals to creditors should be strengthened to indicate a *presumption* that all brokers and all purchasers are responsible under ECOA.

Pre-applications, sec. 202.4

The Institute is concerned that pre-application marketing is an opportunity for creditors to "cream" prospective borrowers by excluding certain groups. Those exclusions can effectively limit the market choices for those groups to subprime and predatory lenders. In consequence we believe that the Regulation should apply to pre-applications. Such an extension will not reduce credit availability if the extension is appropriately implemented. The Board should certainly require creditors to specify and keep a record of the criteria used to select potential customers and the text of the solicitations.

Sincerely,

Malcolm Bush
President