



*Advancing Economic Security
and Community Prosperity*



September 14, 2017

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

Re: Docket No. CFPB-2017-0011

Dear Ms. Jackson:

Woodstock Institute, California Reinvestment Coalition (CRC), Main Street Alliance, and People's Action Institute (the "Collaborative")¹ offer this comment in response to the Consumer Financial Protection Bureau's (CFPB's) request for information (RFI) regarding the small business lending market. In addition to providing information responsive to the five categories in the RFI, this letter offers additional insight and information to support expedient and comprehensive rulemaking pursuant to Section 1071 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) (rulemaking referred to throughout as "1071"). We stand with many allies in support of 1071, and we are strongly opposed to efforts to repeal 1071 or to develop carve-outs or exemptions.

With the support of the Collaborative, Woodstock has released three research reports this year about small business lending in different regions of the country.² A fourth report will be released later this year. The reports paint a compelling picture of the need for reform in small business lending. The data analyzed in the reports reveal at least two major findings relative to 1071: (1) the scale of small business

¹ Short descriptions of the Small Business Collaborative and its member organizations is provided in Appendix A.

² When a page citation is required, the page indicated will be from the third report (Woodstock Report #3) even though the same information can likely also be found in the other two reports. The reports can be found in the research section of Woodstock's website: www.woodstockinst.org.

lending by banks has not recovered to pre-recession levels, which, along with other research,³ indicates that small business lending by banks does not meet the demand for access to capital, and (2) communities of color and low-/moderate-income communities do not receive their proportionate share of small business loans from banks. Section 1071 is needed to delve more deeply into this situation. Discrimination may be a factor here, but we need more data.

Small businesses, themselves, recognize the need for data collection. CRC conducted a recent survey of small businesses.⁴ Nearly all (95 percent) indicated that small business data collection is of critical importance (57 percent) or very important (38 percent).⁵ Another telling statistic from the survey is that 90 percent of respondents indicated that small business owners often (57 percent) or sometimes (33.3 percent) face discrimination.⁶ The patterns, trends, and views that exist on the ground are indications of a serious problem. Data collection is necessary to address it.

Small Business Definition

Section 1071(h)(2) of Dodd-Frank states that the term “‘small business’ has the same meaning as the term ‘small business concern’ in section 3 of the Small Business Act (15 U.S.C. 632)” (the “SBA Definition”). The SBA Definition of “small business concern” is intricate, applying different size standards to different industries. 15 U.S.C. 632. The vast majority of businesses – 99.7 percent of businesses according to the SBA – fall within the definition of small business.⁷ At first blush, a definition that covers nearly every business may seem a bit ridiculous,⁸ but the definition seems far more reasonable when one considers that 99.7 percent of all businesses employ 48 percent of private sector employees.⁹ Thus, while the number of businesses covered by the definition is quite broad, the number of employees covered is considerably more moderate. Besides, under the rules of statutory construction, we must assume Congress knew what it was doing when it incorporated the SBA definition of small business into 1071. In other words, Congress intended the definition of small business in 1071 to cover nearly all businesses. CFPB may choose to devise a different or simpler definition, but it must be largely consistent with the legislative intent in 1071, which was for nearly all businesses to fall within the definition of small business.

³ Federal Reserve Banks of Atlanta et al., *2016 Small Business Credit Survey: Report on Employer Firms* (April 2017): “[S]maller firms are . . . notably less successful at obtaining financing from large banks (45% success).” <https://www.newyorkfed.org/medialibrary/media/smallbusiness/2016/SBCS-Report-EmployerFirms-2016.pdf>

⁴ Kevin Stein & Gina Charusombat (California Reinvestment Coalition), *Displacement, Discrimination and Determination: Small Business Owners Struggle to Access Affordable Credit - Results from a State-Wide Survey in California* (Sept. 2017). <http://www.calreinvest.org/system/resources/W1siZiIsIjIwMTc5MDk5MTMvMjMvMTc5MDYvODk5L0NSQ19TbWFsbF9CdXNpbmVzc19SZXBvcnQucGRmIl1d/CRC%20Small%20Business%20Report.pdf>

⁵ *Ibid.* at 3.

⁶ *Ibid.* at 12.

⁷ Presumably to enable businesses and the public to grasp the meaning of “small business,” the SBA uses a working definition of “small business,” which is businesses with less than 500 employees. We assume the businesses covered by this definition is essentially the same as the number of businesses covered by the statutory definition. *Frequently Asked Questions*, SBA Office of Advocacy, June 2016. https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2016_WEB.pdf

⁸ See, e.g., Steve Cooper, *The Government Definition of Small Business is B.S.*, *Forbes* (Sept. 20, 2012). <https://www.forbes.com/sites/stevecooper/2012/09/20/the-government-definition-of-small-business-is-b-s/#6e5c71f5360a>

⁹ SBA FAQs.

Nothing in the statute would preclude, and sound data collection and reporting principles might dictate, that sub-categories be developed within the definition. Certainly the lending experience of “micro-businesses,” which the SBA defines as firms with one to nine employees,¹⁰ is different than the lending experience of larger businesses. Smaller, or “micro,” businesses, for example, are less able to withstand disruptions in daily cash flows that can be created by loans from some financial technology (fintech) lenders.¹¹ Thus, we recommend the CFPB develop sub-categories with the definition of small business for the purpose of data analysis and dissemination.

Other methods of defining small business would get close to covering 99 percent of all businesses and thus would be largely consistent with the legislative intent of 1071. For example, we support a definition of small business based on annual revenues so long as the revenue figure is high enough to encompass the vast majority of businesses. As the RFI itself points out, defining small business as a business with annual revenues of \$1 million or less covers approximately 95 percent of all firms. Therefore, this definition would be largely consistent with the legislative intent of 1071. This definition and a definition of small business based on the number of employees (discussed next) bear the beauty of simplicity. In our experience, simplicity not only aids individuals and groups, like ours, that are involved in developing and recommending policy solutions, but also improves compliance. When both the regulators and the covered entities have a shared understanding of their responsibilities, it makes the regulatory system function more smoothly.

We also support a definition of small business based on the number of employees. The number of employees needs to be high enough so that the vast majority of all businesses are covered, consistent with the legislative intent of 1071. Further, we suggest that a business be counted as “small” if the number of full-time employees at any one point in the preceding calendar year falls within the definitional size. This method is consistent with the intentionally broad scope of the definition.

As for the number-of-employees cut-off for the definition, we recommend the SBA’s working definition of small business, which is a business having fewer than 500 employees.¹² For data analysis and dissemination, we recommend the use of sub-categories to enable a clearer understanding of the different borrowing experiences of differently sized businesses, e.g., “micro-businesses.”

Data Points¹³

At the outset, we acknowledge and do not object to the fact that a new data collection regime, like this one, may need to be implemented in phases. The data points mandated in the statute could be rolled out first, and then, after the data collection and dissemination apparatus is up and running for a time, the discretionary data points could be added. The data collection regime developed and implemented pursuant to the Home Mortgage Disclosure Act (HMDA) is a good comparison in terms of a phased-in approach and in many other respects, which will be discussed throughout this response.

¹⁰ Brian Headd, *The Role of Microbusinesses in the Economy*, Small Business Facts (Feb. 2015).

https://www.sba.gov/sites/default/files/Microbusinesses_in_the_Economy.pdf

¹¹ *Analysis of Business Loan Terms*, Woodstock Institute, July 12, 2016.

http://www.woodstockinst.org/sites/default/files/attachments/Woodstock_Analysis_of_Online_SB_Loan_Terms.pdf; Woodstock Report #3 at 3-4.

¹² SBA FAQs.

¹³ This section will address the *collection* of data. The dissemination of data is addressed in the privacy section.

Woodstock has some experience in Illinois devising a data collection system in the payday and installment lending context.¹⁴ Some of us in the Collaborative have remarked to policymakers and others that fintech loans to small business are tantamount to payday loans for small business, so data collection in the payday lending context can shed light on data collection in the small business lending context. While the Illinois database was not created for fair lending purposes, the data collected in that database is a good example of a data collection framework that is useful for regulators and the public and is not overly burdensome on the industry. Woodstock and others have been able to use the data to, for example, provide comments on the CFPB's proposed payday lending rule.¹⁵

Mandated Data Points

Some of the mandated data points are vague, so we encourage the CFPB to use its rulemaking authority to clarify vague terms. A discussion of each mandated data point follows.

1. Race, Ethnicity, and Gender

We recommend using the 2015 HMDA Rules as a model in this area. The 2015 HMDA Rules require the reporting of racial and ethnic subcategories. This is important because, in the case of Hispanics and Latinos, for example, Hispanic/Latino is not a homogenous group, and one subcategory could be subjected to differential treatment as compared to another subcategory. Under the 2015 HMDA Rules, instead of simply indicating "Hispanic or Latino," the mortgage applicant is asked to choose one of the following subcategories: Mexican, Puerto Rican, Cuban, or Other Hispanic or Latino. For "Asian," the mortgage applicant is asked to choose one of the following subcategories: Asian Indian, Chinese, Filipino, Japanese, Korean, Vietnamese, or Other Asian. A helpful sample data collection form is found at Attachment A of the CFPB's HMDA Small Entity Compliance Guide.¹⁶

Section 1071 requires the collection of this data with respect to the "principal owners." The plural usage here suggests that data should be collected on more than just the primary or controlling owner. We suggest that ownership greater than or equal to ten percent of the company could be an adequate definition of this term.¹⁷ We further suggest that race, ethnicity, and gender data be collected from the loan applicant. NCRC conducted recent research showing that loan applicants were subject to differential treatment on the basis of their race.¹⁸ Thus, collecting data about loan applicants would further the fair lending purposes of 1071.

¹⁴ Payday Loan Reform Act, 815 ILCS 122; Consumer Installment Loan Act, 205 ILCS 670

¹⁵ Woodstock Institute, Letter to Dir. Richard Cordray re: Consumer Financial Protection Bureau's proposed rule on payday, vehicle title, and certain high cost installment loans (Oct. 7, 2016). <http://www.woodstockinst.org/sites/default/files/attachments/161007%20Formatted%20Payday%20Comment%20v2.pdf>

¹⁶ CFPB, *Home Mortgage Disclosure (Regulation C) Small Entity Compliance Guide*, Dec. 2015. http://files.consumerfinance.gov/f/201512_cfpb_hmda_small-entity-compliance-guide.pdf

¹⁷ "Principal owner" means an owner or beneficial owner of at least 10 percent of a corporation, firm, partnership, limited liability company, or association." https://definedterm.com/principal_owner

¹⁸ National Community Reinvestment Coalition (NCRC), *Can Mystery Shopping Change America ?* (2017) (unpublished findings cited in NCRC letter to CFPB re: 1071, <http://www.ncrc.org/resources/testimony-a-regulatory-comments>).

2. Gross Annual Revenue of Business

This data point is sufficiently specific as to not warrant significant discussion. We concur with NCRC's thorough discussion of this data point in its White Paper.

3. Census Tract

In the context of HMDA, census tract is an unambiguous data point. In the 1071 context, however, there could be ambiguities. For example, a small business may have multiple locations and a small office in a separate location that operates as the business's headquarters. In that type of situation, what is the "principal place of business?" We recommend the CFPB conduct research to determine the standard practice used in this area by Community Development Financial Institutions.

4. Action Taken on Application.

This is another area in which HMDA should serve as a model. Attachment B to CFPB's HMDA Small Entity Compliance Guide provides information on how to determine the reportable action taken and date of action taken.¹⁹

5. Type and Purpose of Loan

"Purpose" is a vague term. For example, "refinancing" reflects a loan purpose, but could also be considered a loan type. To describe the purpose as "origination" would not provide much information about the loan. Accion Chicago lists the following as loan purposes on its web site: buy an existing business, equipment, furniture & fixtures, inventory, leasehold improvements, refinancing current loan, refinancing other debt, vehicles, working capital, and other.²⁰ We believe these would be adequate categories to provide meaningful description of the loan purpose.

As for loan type, we discuss in a later section of this response our position that 1071 should capture a vast array of product types, including, for example, merchant cash advances. The recent series of Woodstock reports on disparities in small business lending points to the Community Reinvestment Act (CRA) small business data collection system's failure to differentiate among loan types.²¹ In addition to merchant cash advances, credit cards and term loans are clear examples of product types that small businesses use for financing, so they, too, should be included as loan types. This letter will not attempt to provide an exhaustive list of all types of products. Rather, we encourage the CFPB to compile an expansive list of types based on the types identified by other commenters and in the research on and marketing of financing options for small businesses. Some of the types overlap with one another, so the financial institution should be given the option of reporting that a product falls within multiple "type" categories. To make room for new product types, which is likely in a highly innovative industry, this data point should include "other" as an option.

¹⁹ Small Business Compliance Guide, Attach. B.

²⁰ <https://apply4businessloan.com/#/ACCIONCHICAGO/1>

²¹ Woodstock Report #3 at 6 n. 34.

6. Amount of Credit Applied for and Received

The CRA small business data collection system fails in this area, too, in that it does not collect and report data about the amount of credit for which the borrower applied. Thus, we are unable to measure demand. We believe that the example set by HMDA should be followed with respect to this data point.

Discretionary Data Points

As discussed above, we recognize that it may be prudent to implement the mandatory data points first, and then, once the reporting systems are up and running, the discretionary data points could be implemented. On the data points listed here, we concur a 2014 NCRC White Paper on 1071.²² Our thoughts on these points follows.

1. Pricing

Discriminatory conduct is not confined to whether a loan application is approved. It can also be found in loan terms, especially higher interest rates and “junk fees.”²³ This data point needs to be constructed so it captures all expenses connected to the loan, including, for example, the costs of ancillary products that are financed by the loan.

In the fintech space, in particular, loan interest and fees span a wide range and reflect an industry run amok. The small sample of fintech loans analyzed by Woodstock reflects these wild gyrations. The lowest interest rate in that sample was 26 percent; the highest was a whopping 368 percent.²⁴ As a general matter, we believe triple-digit interest rates to be predatory. Shining a light on these practices may cause the industry to rein in some of the most glaringly excessive interest rates and fees.

2. Reasons for denial

In the employment context, to refute a charge of discrimination, an employer must offer a legitimate, nondiscriminatory basis for its actions. A court will then determine whether the employer’s stated reasons are a pretext for discrimination. The same system should be applied in the lending context. In order to complete a fair lending analysis in the case of a loan denial, the court or regulator must be able to know and then evaluate the lender’s stated reasons for the denial.

3. Industry

Without knowing the industry classification of borrowers, differences in loan amounts could suggest the discriminatory treatment of borrowers. A fair lending analysis would need to control for this variable. In the NCRC White Paper, NCRC, citing the Minority Business Development Agency, points out that,

²² NCRC, *White Paper - Small Business Loan Data: Recommendations to the Consumer Financial Protection Bureau for Implementing Section 1071 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010* (NCRC White Paper) (2014). <http://www.ncrc.org/images/PDFs/recommendations-to-cfpb-on-small-business-loan-data.pdf>

²³ CFPB, “CFPB and DOJ Reach Resolution with Honda to Address Discriminatory Auto Loan Pricing” (July 14, 2015). <https://www.consumerfinance.gov/about-us/newsroom/cfpb-and-doj-reach-resolution-with-honda-to-address-discriminatory-auto-loan-pricing/>

²⁴ Woodstock Institute, *Analysis of Business Loan Terms* (July 12, 2016). http://www.woodstockinst.org/sites/default/files/attachments/Woodstock_Analysis_of_Online_SB_Loan_Terms.pdf

higher loan amounts to white-owned businesses could be attributable to the fact that minority-owned business are less prevalent in construction and manufacturing, where businesses tend to receive higher loan amounts as compared to retail businesses due to the nature of those respective businesses.²⁵

4. Credit Score

Credit scores are not always reliable indicators of a person's or business's creditworthiness, and reliance on them can lead to unfair and unjust outcomes for small businesses seeking access to credit. But, reporting credit score data, if it is obtained by the lender, is important for at least two reasons related to fair lending: (1) to determine whether, even when controlling for credit score, there are disparities in lending to women and minorities; and, (2) to determine the extent to which loan approvals and terms that are based in part on credit scores have a disproportionately negative impact on minorities, consistent with research done by Woodstock and others.²⁶

It is well known that traditional credit scoring has a disproportionately negative impact on communities of color.²⁷ Further, the impacts of having a lower credit score are not confined to credit situations, but are also applied in contexts such as employment and auto insurance rates.²⁸ In part for these reasons, Woodstock and others have advocated for alternative scoring models such as VantageScore,²⁹ which uses additional data points and can score more people and improve the creditworthiness profile of individuals who do not fare well under the traditional model.

In the 1071 context, the existence of alternative scoring models presents an obvious challenge to the CFPB. Comparing a traditional credit score to a VantageScore is an "apples-to-oranges" comparison. To allow for an "apples-to-apples" comparison, the CFPB would need to "normalize" the scores, as suggested by NCRC in its White Paper.³⁰ We suggest that the regulations on this data point, if possible, be drafted to allow for the evolution of credit scoring.

The Woodstock Institute *Patterns of Disparity* series of reports describe the fact that not all small businesses have commercial credit scores and that, for such businesses, the personal credit scores of the owners may be used instead.³¹ For lenders that do not rely on credit scores at all, the lender can simply report "Not Known." However, a lender should not be permitted to collect the credit score and then claim to not be relying on it. In all instances in which a lender collects a credit score, the lender should be required to report it.

²⁵ NCRC White Paper at 31.

²⁶ Geoff Smith & Sarah Duda, Woodstock Institute, *Bridging the Gap: Credit Scores and Economic Opportunity in Illinois Communities of Color* (Sept. 2010).
http://www.woodstockinst.org/sites/default/files/attachments/bridgingthegapcreditscores_sept2010_smithduda.pdf

²⁷ *Ibid.*

²⁸ See, e.g., Amy Traub & Sean McElwee, *Bad Credit Shouldn't Block Employment* (2016).

<http://www.demos.org/sites/default/files/publications/BadCreditShouldntBlockEmployment.pdf>

²⁹ See <https://www.vantagescore.com/>.

³⁰ NCRC White Paper at 31.

³¹ Woodstock Report #3 at 1.

5. Number of employees

As discussed previously, given that the definition of small business is broad, the CFPB will want to know the number of employees to account for the fact that “microbusinesses,” for example, have different lending experiences than businesses with hundreds of employees.

6. Collateral

The existence, type, and extent of collateral can be a significant factor in loan approval and loan terms. Even personal collateral, as opposed to business collateral, that may be used to secure a loan should be reported. We recognize that establishing a comprehensive and specific list of possible entries for lenders to provide on this data point would be challenging. “None of the above” should clearly be one of the choices.

7. Tenure of business

It is both logical and widely known that businesses with a shorter tenure, as compared to established business, have a more difficult time accessing credit. Controlling for the tenure of the business would be important for a fair lending analysis.

Burden

Having completed our discussion of the various data points, we feel it is appropriate here to touch on the issue of regulatory burden. The most important fact relative to regulatory burden is that lenders already collect most of this data anyway. Emilia DiMenco, a former Executive Vice President at a national commercial and corporate bank, who is now President and Chief Executive Officer of the Women's Business Development Center in Chicago, said, “Any reasonably conscientious lender would be collecting this data anyway. The added burden of having to report it is small and is far outweighed by the benefits to the responsible lenders who should want to cast a light on the bad practices of others in the industry.”

Covered Financial Institutions

There is no policy justification for excluding a *type* of financial institution from the requirements of 1071. By “type,” we mean to draw a distinction between “type” as in community bank, credit union, fintech lender, etc., and “volume” in terms of a financial institution that, independent of its type, makes a de minimis number of loans (or extensions of credit). We acknowledge that it may be appropriate to establish a de minimis exemption analogous to the current thresholds in HMDA. The thresholds must be set to exclude only the truly de minimis institutions. Going beyond de minimis simply compromises the completeness of the data set, which undermines the entire data collection endeavor. An incomplete data set can make things worse by painting an inaccurate picture of market activity and behavior. This is why we also oppose raising the thresholds in the HMDA context.³²

The damage to the data set that can be done by exempting smaller institutions, for example, is exemplified by looking at the data in rural or smaller communities. For example, community banks and

³²See Woodstock et al., Letter to the U.S. Senate re: “Oppose S. 1310, ‘The Home Mortgage Disclosure Adjustment Act’” (July 19, 2017).

<http://www.ncrc.org/images/letter%20in%20opposition%20to%20senate%20bill%20s%201310.pdf>

intermediate small banks are important in the rural areas, smaller cities, and mid-size cities that make up the Rochester MSA. In 2015 in the Rochester MSA, three such banks accounted for 36 to 22 percent of the small business lending by dollar volume of loans.³³ Therefore, we are opposed to exemptions for small banks.

There is a popular narrative about community banks and credit unions that (1) they are, by their nature, not inclined to engage in discriminatory or predacious conduct, and (2) they are in need of regulatory relief because their relative small size and lack of sophistication make them less equipped to shoulder regulatory burdens. This is a bogus generalization. It is, in our opinion, subterfuge, i.e., a “foot in the door” tactic by the financial industry as a whole to deregulate itself.

Georgetown law professor Adam Levitin offered testimony to the U.S. Senate Banking Committee on June 8, 2017, that, we believe, should dispose of this false narrative.³⁴ On point #1 of the narrative, that the community banks and credit unions are “good guys,” this is just a simplistic and naïve view. Good actors and bad actors exist in every conceivable industry and occupation. Dostoyevsky said, “Bad people are to be found everywhere, but even among the worst there may be something good.”³⁵ A recent case in point is the CFPB’s October 2016 \$28 million consent order with Navy Federal Credit Union “for making false threats about debt collection to its members, which include active-duty military, retired servicemembers, and their families.”³⁶ Even among the many actions by financial institutions that have been subject to CFPB enforcement action, false threats to members of the military rank among the more egregious.

Point #2, the need for regulatory relief, is just false. Levitin’s testimony objectively and entirely refutes this claim. Levitin backs up with specific data his position that “since the Dodd-Frank Act, community banks and credit unions have been doing extremely well as measured *by all traditional measures of health of the banking industry*” (our emphasis).³⁷ Deregulation advocates point to the consolidation of institutions as an indicator of the need for regulatory relief. On this argument, Levitin makes several apt points. Here are three of them: (1) consolidation is a long-term, steady trend that pre-dates Dodd-Frank; (2) megabanks are to blame because they have unlevelled the playing field, placing smaller institutions at a severe disadvantage because they lack the economies of scale to compete; and (3) *community banks and credit unions already receive regulatory relief*. Levitin lists specific examples of ways in which community banks and credit unions already receive special treatment.³⁸

Products Covered

The purpose and language of 1071 call for casting a wide net so as to capture the array of products that small businesses rely on to fulfill their need for capital. Subsection (b) of 1071 applies the data

³³ Empire Justice Center, Letter to CFPB re: Request for Information Regarding the Small Business Market (Sept. 7, 2017) (unpublished letter).

³⁴ Adam Levitin, Written Testimony before the U.S. Senate Committee on Banking, Housing, and Urban Affairs, “Fostering Economic Growth: The Role of Financial Institutions in Local Communities” (June 8, 2017).

<https://www.banking.senate.gov/public/cache/files/cfee4732-9f53-4a58-86f1-27a25d9086f4/E8DC189DC1FD5D1D6EBAB7D28241185A.levitin-testimony-6-8-17.pdf>

³⁵ Fyodor Dostoyevsky, *The House of the Dead* (1860).

³⁶ CFPB, “CFPB Orders Navy Federal Credit Union to Pay \$28.5 Million for Improper Debt Collection Actions” (Oct. 11, 2016). <https://www.consumerfinance.gov/about-us/newsroom/cfpb-orders-navy-federal-credit-union-pay-285-million-improper-debt-collection-actions/>.

³⁷ Levitin at 4.

³⁸ *Ibid.* at 8-9.

collection requirement to “any application to a financial institution for *credit*” (our emphasis). Subsection (e)(1) states that the data will be provided by the “*loan applicant*” (our emphasis). Then, the data point for loan “type,” which falls in Subsection (e)(2)(B) of 1071, applies to “the loan or other credit.” We believe the statute’s use of both the terms “loan” and “credit” reflects a legislative intent to not constrict 1071 to a strict and narrow definition of the term “loan” or “credit,” but rather to apply 1071 to a broad range of products that a small business may receive to help finance the business. A merchant cash advance is an example of a product that should fall within the requirements of 1071 even though a strict and narrow definition of the term “loan” may, in the opinion of some, exclude it. Excluding products such as merchant cash advances from 1071 would contravene the fair lending concerns of 1071, which is plainly meant to capture all transactions in which a small business applies for financing from a financial institution because in all such transactions a small business may experience the type of discrimination that 1071 is designed to detect.

In addition to furthering the fair lending goals of 1071, there is another policy justification for construing the requirements of 1071 broadly so as to include merchant cash advances and other products that could conceivably fall outside a strict and narrow definition of the term “loan.” Failing to include a product within the requirements of 1071 would effectively create a loophole that would incentivize financial institutions to gravitate toward offering that product. In other words, some financial institutions would prefer to offer products that are less regulated and less transparent. Illinois has experienced this phenomenon in a related context. While Illinois’ Payday Loan Reform Act³⁹ was moving through the legislature, the bill was amended such that the PLRA applied only to loans of 120 days or less. This made the 120-day provision in the definition of payday loan a loophole that lenders exploited by making 121-day loans. In April 2008, Woodstock and the Public Action Foundation released a report called “The Illinois Payday Loan Loophole.”⁴⁰ The report found that after the PLRA went into effect, lenders switched to longer-term installment loans not subject to the PLRA’s consumer protections. To avoid this type of effect, the scope of 1071 should be as broad as possible.

Privacy

Privacy issues are systematically addressed with all federally-produced publicly available data, and collection of small business lending data should have similar privacy procedures as other data sets. Privacy concerns as they relate to small business data collection in no way prohibit the release of these data to the public. Loan volumes as currently collected under the CRA are sufficiently large in many geographies to assuage concerns of data users being able to identify individual loan applicants, and these numbers would be augmented if more lenders were required to report under 1071. Small business data collected under 1071 should never be ‘deleted’ or ‘modified,’ as this undermines the data collection process and leaves ambiguous what data are and are not included in the figures. Instead, data for census tracts deemed to pose privacy concerns can be systematically addressed to protect privacy while still providing meaningful disclosures. The following techniques are employed by other federally-produced publicly available data that can be utilized to address privacy issues:

Aggregation to higher levels of geography

Data for areas where there are too few loans applicants per census tract (for example, in sparsely populated rural areas) could be reported at a higher level of geography, namely, at the zip code or

³⁹ 815 ILCS 122.

⁴⁰ Woodstock Institution & Public Action Foundation, “The Illinois Payday Loan Loophole,” (April 2008) <http://www.woodstockinst.org/research/illinois-payday-loan-loophole>.

county level. The American Community Survey employs this technique to limit the disclosure of information about individual respondents and to reduce the number of estimates with unacceptable levels of statistical reliability. The Census Bureau releases basic data for its smallest levels of geographies (blocks/block groups), and reserves more detailed data cuts for larger ones.⁴¹

Masking using categorical or range reporting

Sensitive data points could be reported in categories or ranges to mask the actual data point value. An example of this technique is employed by the Census Bureau's County Business Patterns. Paid employee figures for NAICS codes with a very small number of establishments in a given geography are presented in ranges (e.g. 0-19 employees, 20-99 employees, etc.) to prevent disclosure of individual firms' employment figures.⁴²

Noise infusion

Noise infusion is a method of disclosure avoidance in which values are perturbed prior to data tabulation by applying a random noise multiplier to the magnitude data. This technique is employed in data products such as the Census Bureau's Longitudinal Employer-Household Dynamics (LEHD) Program. Noise infusion should be used with caution and should preserve analytical validity.⁴³

This sounds familiar

Opponents of comprehensive regulatory solutions to problems repeatedly point to privacy concerns, and consumer advocates have repeatedly responded to them. For example, Woodstock, NCRC, and other consumer advocacy groups provided a detailed, nearly 10-page discussion on the privacy issue in the HMDA context to the CFPB.⁴⁴ It is worth noting, also, that not one privacy violation has come to light in over forty years of HMDA enforcement.

Additional Considerations

The Woodstock Institute *Patterns of Disparity* series of reports bear directly on the need for 1071. The reports provide solid evidence of racial disparities in small business lending. For example, businesses in predominantly minority census tracts in the Los Angeles and San Diego region constitute an average of 31.8 percent of businesses, but they receive only 21.5 percent of the number of loans and only 20.6 percent of the total amount of such loans.⁴⁵ Similar disparities have been found in every region analyzed by the reports. The promulgation of 1071 rules is one of many policy recommendations that we offer in the reports.

⁴¹ See U.S. Census Bureau American Community Survey Data Suppression available at https://www2.census.gov/programs-surveys/acs/tech_docs/data_suppression/ACSO_Data_Suppression.pdf.

⁴² See County Business Pattern Technical Documentation for information on record layout and suppression values available at <https://www.census.gov/programs-surveys/cbp/technical-documentation.html>.

⁴³ For more information about noise suppression see *Using Noise for Disclosure of Limitation of Establishment Tabular Data* available at <https://www.census.gov/prod/2/gen/96arc/iaevans.pdf>.

⁴⁴ National Consumer Law Center *et al.*, Letter to Ren Essene re: Public disclosure of new HMDA data points. https://www.nclc.org/images/pdf/foreclosure_mortgage/predatory_mortgage_lending/letter-re-hmda-benefits-and-privacy.pdf

⁴⁵ Woodstock Report #1 at 20.

NCRC's recent "mystery shopping" project gives the 1071 rules additional urgency.⁴⁶ The NCRC project, which is described fully in NCRC's response to this RFI, provides shocking evidence of differential treatment based on race.

Many opponents of 1071 may agree that discrimination exists, but feel that a comprehensive data collection regime is an overly burdensome tool and that it will have the net effect of constricting access to credit. The HMDA experience provides compelling evidence as to the link between data collection and fair lending detection and analysis. A Winter 2007 "Supervisory Insight" by the FDIC offers a succinct explanation of the role HMDA plays in combating discrimination: "While the HMDA pricing data do not include underwriting criteria (such as loan-to-value ratios, debt-to-income ratios, or credit scores) necessary to reach conclusions about discriminatory lending, the data can be used to identify situations that indicate a need for further review."⁴⁷

The emergence of the fintech industry is another reasons why the need for data collection is clear and urgent. The research by Woodstock and others prove that communities of color have a more difficult time than white communities in gaining access to credit.⁴⁸ We are concerned that, just as in the case of sub-prime mortgages and payday loans, some fintech lenders are targeting communities of color because they, too, know that communities of color have greater difficulty than white communities in receiving financing from a bank. We need data to (1) know whether communities of color are being targeted, and, if they are, to (2) develop solutions to the problem. We already know what can happen if we take too long to act. In the context of mortgages and the mortgage crisis, HMDA data showed that "[t]he foreclosure crisis . . . disproportionately affected African-American and Latino borrowers, who [were] 76% and 71% more likely, respectively, to have lost their home to foreclosure than non-Hispanic white borrowers."⁴⁹ We need to know the full extent of (and ultimately the reason for) the disparities that exist in the small business lending context.

Just as in the mortgage context, differential treatment based on race is not just an issue of morals and justice, which it most certainly is; it also has broad economic implications as entire communities may be decimated by wealth-stripping predatory and unsustainable loans. Given small businesses' role as job creators, these impacts spill over into the overall economy. It is urgent that we get a handle on what is happening to women-owned and minority-owned that are unable to obtain access to traditional credit. Correspondingly, we urge the CFPB to move expeditiously in promulgating the rules under 1071.

Very truly yours,

WOODSTOCK INSTITUTE
CALIFORNIA REINVESTMENT COALITION
MAIN STREET ALLIANCE
PEOPLE'S ACTION INSTITUTE

⁴⁶ NCRC Mystery Shopping (unpublished findings cited previously).

⁴⁷ Samuel Franklin, "Using the HMDA Data to Evaluate Fair Lending Concerns," *Supervisory Insights*, at 33 (Winter 2007). <https://www.fdic.gov/regulations/examinations/supervisory/insights/siwin07/winter07.pdf>

⁴⁸ Woodstock Report #3 at 27 (citing other research on lending disparities).

⁴⁹ Debbie Gruenstein Bocian, Wei Li, and Keith S. Ernst, *Foreclosures by Race and Ethnicity: The Demographics of a Crisis*, at 8 (June 8, 2010). <http://www.responsiblelending.org/mortgage-lending/research-analysis/foreclosures-by-race-and-ethnicity.pdf>

Appendix A

About the Small Business Collaborative

The Collaborative is comprised of Woodstock Institute, California Reinvestment Coalition, Main Street Alliance, and People's Action Institute. The purpose of the Collaborative is to promote equitable access to capital for women-, people of color-, and LMI-owned small businesses and small businesses in LMI areas through national research and advocacy.

About Woodstock Institute

Woodstock Institute is a leading nonprofit research and policy organization in the areas of equitable lending and investments; wealth creation and preservation; and safe and affordable financial products, services, and systems. Woodstock Institute works locally and nationally to create a financial system in which lower-wealth persons and communities of color can safely borrow, save, and build wealth so that they can achieve economic security and community prosperity. Our key tools include: applied research; policy development; coalition building; and technical assistance. Woodstock Institute has been a recognized economic justice leader and bridge-builder between communities and policymakers in this field since it was founded in 1973 near Woodstock, Illinois.

About California Reinvestment Coalition

CRC builds an inclusive and fair economy that meets the needs of communities of color and low-income communities by ensuring that banks and other corporations invest and conduct business in our communities in a just and equitable manner.

About Main Street Alliance

The Main Street Alliance is a national network of small business owners. MSA works to provide small businesses a voice on the most pressing public policy issues across the nation. Our advocacy promotes vibrant businesses and healthy communities, and fosters leadership development of socially responsible business leaders.

About People's Action Institute

People's Action Institute is a leading voice for fair lending and economic justice. People's Action Institute, formed through a merger uniting Alliance for a Just Society, Institute for America's Future, National People's Action, and USAction Education Fund, is a national grassroots network comprised of over 50 affiliated membership organizations in 30 states and dedicated to fighting for racial, economic and climate justice. Nationally, our members have always stood on the side of economic justice against the strip-mining of our communities by Wall Street and against racist and discriminatory lending. In our more than forty year history, our legacy organizations spearheaded organizing campaigns that led to landmark policy changes fighting for fair lending and economic justice, such as the Home Mortgage Disclosure Act (1975) and the Community Reinvestment Act (1977). More recently, our work was instrumental in laying the groundwork for critical financial reform initiatives such as the Dodd-Frank Wall Street Reform and Consumer Protection Act (2010) and the \$26 billion Attorneys General Mortgage Fraud Settlement (2012). Our million plus members stand united in demanding that people and planet must come before profits and that we must banish institutional racism from our financial system.