

Subject Matter Hearing:  
HB 3064 (Huynh) - Small Business TILA  
Illinois House of Representatives, Committee  
on Financial Institutions & Licensing  
Testimony of Brent Adams  
March 28, 2023

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Access to safe and affordable credit has been at the core of Woodstock’s work since our founding 50 years ago. For as long as the U.S. has been a nation, disparities in access to safe and affordable credit have exacerbated racial and ethnic wealth gaps. These gaps contribute to a host of negative impacts. Our research, policy positions, and advocacy campaigns are undertaken with an eye toward eliminating these disparities and improving the quality of life in underserved communities.

*Non-bank lenders target Illinois small businesses with high-cost financing that is not transparent.*

Today, Illinois small businesses are beset by high-priced financing that does not disclose its pricing in a transparent way. This high-rate financing market has developed over the last fifteen years and is, in many ways, like payday lending for small businesses. However, unlike payday loans, this small business financing is not covered by basic consumer protection laws. HB 3064 would help remedy that.

Woodstock has conducted research on small business financing and found loans charging interest rates that ranged from 26% to 368%!<sup>1</sup> The lenders charging these rates did not disclose them to the borrowers.

Woodstock’s analysis was based on a sample of small business loan contracts. In the absence of a requirement to disclose an annual percentage rate — or APR — online, financial technology — or “fintech” — lenders employed a variety of different disclosure mechanisms. A common one — often used for merchant cash advances — is to disclose a percentage of the business’s daily revenue that will go towards repayment. So, for example, one contract disclosed 10% as a “Specified Percentage” in a box similar to a TILA disclosure box. Ten percent as an APR sounds affordable, and Federal Reserve research has found that small businesses tend to mistake these

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<sup>1</sup> Woodstock Institute, *Analysis of Business Loan Terms* (July 12, 2016).  
<https://woodstockinst.org/research/fact-sheets/analysis-business-loan-terms/>

percentages for an interest rate or APR.<sup>2</sup> But we calculated that the undisclosed, annualized interest rate of this transaction was actually 323.9%!

Small businesses should know upfront what the price of each financing option would be, so that they can make informed price comparisons between their different options. Being able to make informed business decisions impacts the business, its employees, its current and potential customers, and the community in which the business resides.

*This higher-cost, less-transparent financing targets Black, Brown, and lower income communities.*

Woodstock has also researched who bears the brunt of small business loans with predatory interest rates. The evidence strongly suggests that predatory fintech small business loans, similar to consumer payday loans, disproportionately target Black, Brown, and lower income neighborhoods. This conclusion draws on five reports Woodstock published from 2017 to 2019 that looked at small business lending by banks based on data reported by banks under the Community Reinvestment Act.<sup>3</sup> Bank loans, compared to nonbank loans, are much more likely to have affordable terms, better disclosures, and higher rates of customer satisfaction.

For the 18 regions we covered in those reports — seven areas outside Illinois, nine areas inside Illinois, Illinois as a whole, and the United State as a whole – the number of small business loans by banks is inversely proportional to the percentage of Black, Brown, or lower income people in a census tract. In other words, small business lending by banks goes down as the percentage of Black, Brown, or lower income residents goes up. Lack of access to bank loans, researchers agree, makes underserved small businesses more vulnerable to fintech loans that are predatory and/or lack transparency.

Our finding that less-transparent lenders target communities of color is also supported by the Federal Reserve’s research.<sup>4</sup> Their research finds that Black- and Hispanic-owned firms are more likely than white- and Asian-owned firms to apply for financing online that the Federal Reserve describes as “potentially higher cost and less transparent.”

*TILA for small businesses is a common sense, measured solution.*

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<sup>2</sup> See Fed. Reserve Bd. Of Governors, *Uncertain Terms: What Small Business Borrowers Find When Browsing Online Lender Websites* (Dec. 2019). <https://www.federalreserve.gov/publications/what-small-business-borrowers-find-when-browsing-online-lender-web-sites.htm> Lipman and Wiersch Federal Reserve Board of Governors, *Browsing to Borrow: ‘Mom & Pop’ Small Business Perspectives on Online Lenders* (June 2018). <https://www.federalreserve.gov/publications/files/2018-small-business-lending.pdf>

<sup>3</sup> See, e.g., Lauren Nolan and Brent Adams, *Patterns of Disparity: Small Business Lending in Illinois* (Aug. 6, 2019). <https://woodstockinst.org/research/reports/patterns-of-disparity-small-business-lending-illinois/>

<sup>4</sup> See, e.g., Federal Reserve Bank of Atlanta, *Small Business Credit Survey: Report on Minority-Owned Firms* (Dec. 2019); <https://www.fedsmallbusiness.org/survey/2019/report-on-minority-owned-firms>. Federal Reserve Banks, *Small Business Credit Survey: 2021 Report on Firms Owned by People of Color*; <https://www.fedsmallbusiness.org/survey/2021/2021-report-on-firms-owned-by-people-of-color>.

Requiring lenders to small businesses to disclose an APR is a common sense and moderate approach to this issue. More aggressive policies that could be pursued to tackle this problem include establishing a licensure framework for non-bank lenders and imposing rate caps on small business loans. Advocates worked on a licensure bill with former State Senator Jacqui Collins in 2016. The opposition was fierce. One publication said it was the “world’s strangest bill.” TILA for small businesses is a substantially more measured approach. Bills like HB 3064 would empower small businesses to make informed business decisions and create greater transparency within the market, which would benefit consumers and communities.