RESPONSIBLE BUSINESS LENDING COALITION

September 14, 2017

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

Re: Section 1071 and the Small Business Lending Market (Docket No. CFPB-2017-0011)

Dear Ms. Jackson,

The Responsible Business Lending Coalition ("RBLC") writes to express our strong support for a well-considered implementation of Dodd-Frank Section 1071. Small businesses today find themselves between a rock and hard place. They struggle for access to capital on the one hand, and face a rise in irresponsible lending on the other. Section 1071 will help address these problems by bringing much-needed transparency and insight to the small businesses lending market.

Currently, there is limited understanding about how much small business lending is happening, who is receiving loans, and at what terms. By providing the first comprehensive and accurate information about what market gaps exist, Section 1071 will spur innovation within banks, community organizations, fintech companies, and others, to address those gaps and improve small businesses' access to responsible capital.

In the following letter, the Responsible Business Lending Coalition offers a cross-sector industry and nonprofit perspective on how Section 1071 may be implemented while avoiding unnecessary reporting burdens and achieving Congress' intent to "enable communities, governmental entities, and creditors to identify business and community development needs and opportunities of women-owned, minority-owned, and small businesses."[1]

[1] 15 U.S. Code § 1691c–2 - Small business loan data collection

The RBLC and the *Small Business Borrowers' Bill of Rights*

The Responsible Business Lending Coalition ("RBLC") is a diverse association of non-profit and for-profit organizations serving small businesses that have joined together out of concern about the need for increased access to capital, and about the rise of irresponsible small business lending practices.

The mission of the RBLC is to drive responsible practice in the small business lending sector. RBLC's members are the Aspen Institute, a nonpartisan policy studies organization and the facilitator of the coalition; Funding Circle and Lending Club, two leading FinTech innovators in marketplace lending; Accion and Opportunity Fund, the two largest nonprofit CDFI small business lenders; Fundera, a leading small business loan broker; Community Investing Management, an impact-driven investor in small business financing; and Small Business Majority, a nonprofit trade association and advocate for small businesses.

In 2015, we came together to create the *Small Business Borrowers' Bill of Rights*, a cross-sector consensus on the responsible lending practices that all small businesses deserve. The *Small Business Borrowers' Bill of Rights* has been signed by over 80 for-profit FinTech innovators, nonprofit CDFIs, advocacy and community groups, investors, small banks, lenders, brokers, and marketplaces.[2] These organizations, who have wide ranging opinions on many issues related to small business lending, all agree that small businesses deserve the following six rights:

1. The Right to Transparent Pricing and Terms
2. The Right to Non-Abusive Products
3. The Right to Responsible Underwriting
4. The Right to Fair Treatment from Brokers
5. The Right to Fair Collections Practices
6. The Right to Inclusive Credit Access

In the *Small Business Borrowers' Bill of Rights*, each of these rights is described in detail with specific practices that lenders, marketplaces, and brokers should abide by to uphold these rights for their small business customers. The full text of the *Small Business Borrowers' Bill of Rights* and a list of signatories and endorsers are attached and available online at www.ResponsibleBusinessLending.org.

To become a "Signatory" of the *Small Business Borrowers' Bill of Rights*, the CEO or chief executive of a lender, marketplace, or broker must sign an attestation form affirming that the organization abides by each and every relevant practice set forth in the Small Business Borrowers' Bill of Rights. There is no option to abide by certain requirements and ignore others. A signatory's CEO is required to sign a standard Attestation Form designed for either a lender or marketplace, or a broker. Organizations that do not provide lending or brokering services, such

[2] Note that while these 80+ organizations have signed or endorsed the Small Business Borrowers' Bill of Rights, this letter represents the views of the RBLC, and does not necessarily represent the views of all signatories or endorsers of the Small Business Borrowers' Bill of Rights.

as think tanks and advocates, may become "Endorsers" of the *Small Business Borrowers' Bill of Rights*.

The Need for Section 1071 (Responsive to Question 15)

Small businesses face a gap in access to capital, and we believe that Section 1071 can help. In the 2016 Small Business Credit Survey of the Federal Reserve, small business employer firms said that the top financial challenge they face is "credit availability or securing funds for expansion."[3] Currently, there is no comprehensive information anywhere about how much small business lending is happening, who is being served, and at what terms. Some of the better data available, such as the volume of bank commercial loans under $1 million to both small and large firms, suggests that small business loans as a share of bank lending has fallen from 40% in 1995 to 21% in 2016.[4] The Federal Reserve's 2016 survey concludes that 57% of employer small businesses are experiencing a funding shortfall or may have unmet funding needs![5] This lack of access to capital is a critical problem for small businesses, and is preventing significant job creation and economic growth that small businesses could contributing to our economy.

The lack of access to capital is even more pronounced for women- and minority-owned businesses. Research suggests that similarly situated loan applicants fare differently depending on their race and/or gender.[6,7] Women- and minority-owned businesses operate with much less financial capital on average than their peers, even after controlling for credit score and other factors.[8] Black entrepreneurs are nearly three times as likely as White entrepreneurs to have their profitability hurt by lack of capital, and more than twice as likely to have profits negatively impacted by the cost of capital.[9]

Women and minority business owners report at greater rates that they are discouraged from applying for credit due to a fear of denial.[10] New research by the National Community Reinvestment Coalition illuminates some of the reason why. Over the Spring and Summer of 2017, NCRC performed civil rights testing in which Black and White "mystery shoppers," representing small business owners, visited a series of bank branches in two MSAs. Whether as a result of unconscious bias or for other reasons, notable differences in the service received

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[3] "2016 Small Business Credit Survey," Federal Reserve Banks of Atlanta, Boston, Chicago, Cleveland, Dallas, Kansas City, Minneapolis, New York, Philadelphia, Richmond, St. Louis and San Francisco (April 2017). https://www.newyorkfed.org/medialibrary/media/smallbusiness/2016/SBCS-Report-StartupFirms-2016.pdf

[4] Mills, Karen Gordon and McCarthy, Brayden (2016). The State of Small Business Lending: Innovation and Technology and the Implications for Regulation. Harvard Business School Working Paper 17-042.

[5] "2016 Small Business Credit Survey," Federal Reserve. https://www.frbatlanta.org/research/small-business/survey/2016/report-on-employer-firms.aspx?panel=1

[6] Ibid

[7] Alsos, G. A., Isaksen, E. J. and Ljunggren, E. (2006). New Venture Financing and Subsequent Business Growth in Men- and Women-Led Businesses. Entrepreneurship Theory and Practice, 30: 667–686.

[8] Ibid.

[9] Ibid.

[10] Robb, Alicia (April 2013). Access to Capital among Young Firms, Minority-owned Firms, Women-owned Firms, and High-tech Firms. Developed under contract for the Small Business Administration, Office of Advocacy.

emerged. For example, bank staff offered to help a White business owner complete a loan application 27% of the time, and offered to help a Black business owner only 12% of the time. Staff offered to schedule a future appointment for the White business owner 23% of the time, as compared to 8% of the time for a Black business owner. Other differences in treatment took place. For example, on a number of occasions the bank loan offer servicing a Black small business owner checked a government website during the conversation to verify that the business was registered and in good standing. This did not occur for any White business owner.[11]

This difference in treatment may be one reason that minority-owned small businesses are disproportionally pessimistic about applying for traditional bank loans. It may also be one reason why some community development lenders and fintech lenders using nontraditional models are sometime better at reaching underserved small businesses. For example, 88% of the small business owners borrowing from Opportunity Fund, the largest nonprofit microlender in the U.S., are ethnic minorities.[12] Two thirds of the loans made in the U.S. by Accion, a leading nation-wide nonprofit lender to small businesses, support business owners in low- to moderate-income households. LendingClub, the largest marketplace lender in the United States, uses technology to better serve small businesses and its customer base includes 4x the representation of women-owned businesses, and 5x the representation of minority-owned businesses, when compared to estimates of conventional small business lending.[13] In these examples, it is clear that with the right tools and approaches, financial institutions are able to reach the small businesses who need them.

We believe the data provided by 1071 would help encourage investment, within banks and in innovators themselves, in "what works" to better serve minority-owned businesses. The historical record of HMDA, the Home Mortgage Disclosure Act, provides one example of how data collection that identifies market gaps has led lenders to pursue those opportunities. In 1989, HMDA was updated to include data collection of the demographics of applicants, much like Section 1071 will. From 1993 through 1995, conventional (non-government insured) mortgage lending to Black and Hispanic people surged 70 percent and 48 percent, respectively.[14] It is worth noting that this increase predates the emergence of the irresponsible mortgage products that contributed to the financial crises in the 2000s.

In addition to facing a challenge accessing capital, small businesses now also contend with the rise of irresponsible lending practices. These practices have led some observers to draw comparisons to the subprime mortgage sector in the leadup to 2008.[15] The specific problems that

[11] Bone, Sterling A., Christensen, Glenn L., Williams, Jerome D., Adams, Stella, Lederer, Anneliese and Lubin, Paul C, "Detecting Discrimination in Small Business Lending," September 12, 2017. Available at SSRN: https://ssrn.com/abstract=3035972. And National Community Reinvestment Coalition comment to CFPB on Small Business Data Collection, September 12, 2017.

[12] As measured by Opportunity Fund portfolio volume

[13] Senate Committee on Small Business and Entrepreneurship, "21st Century Barriers to Women's Entrepreneurship," July 23, 2014, citing Temkin, Kenneth et al, "Competitive and Special Competitive Opportunity Gap Analysis of the 7(a) and 504 Programs," Urban Institute. January 2008. Although this may be the most relevant data available, it is aged. Analysis draws on SSBF data from 2003. The lack of more recent data further illustrates the need for Section 1071.

[14] This exceeds the 12% increase in home lending to Whites during the same period. Source: National Community Reinvestment Coaltion, *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*.

[15] For example, "Why Online Small Business Loans Are Being Compared to Subprime Mortgages," Forbes, Dec 10, 2015.

led the RBLC to come together and produce the Small Business Borrowers' Bill of rights include:

a) Obfuscation of very high financing costs
b) Misaligned incentives between lenders and borrowers
c) Double-charging borrowers when loans are renewed by "double dipping"
d) Mismatch between financial products' purported use and actual use behavior encouraged by the provider
e) Hidden prepayment charges
f) Misaligned broker incentives steering small businesses into expensive products
g) "Stacking" of too much debt
h) Lack of legal protections in collections, and
i) Need for financial inclusion

Transparency into the small business lending sector through Section 1071 can help steer the market towards better practices, and a better outcome than experienced in subprime mortgage lending.

There is a clear need for Congress' expressed purpose for Section 1071 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." Greater understanding of where the gaps exist would enable lenders to be more effective in reaching the underserved small businesses who need them, and would spur further innovations from banks, fintech companies, community groups, advocates, and the public sector.

Recommendations

Implementation of Section 1071 must be designed to avoid undue regulatory burden that may reduce financing to small businesses, discourage new entrants into small business financing, or add unnecessary cost to the small business credit system.

The ease or difficulty that financing providers experience in complying with Section 1071 will vary by the type of organization. Financing providers that utilize technology will generally have an easier time complying than smaller brick-and-mortar lenders, for example. Larger banks, and especially fintech companies, are already accustomed to storing data in structured environments for easy analysis. Sophisticated banks and fintech companies may use systems to "permission" which employees are able to access specific data points, such as personally identifiable information (PII). This same capability could be easily applied to restrict access to demographic information. Many technology companies also are accustomed to automating data transfers. Critically, the CFPB should structure implementation of the 1071 program to make it possible for 1071 data reporting to be completely automated.

On the other hand, smaller firms using paper and manual processes are likely to require greater resources and process changes to comply with Section 1071. Complying with 1071 will require a certain amount of investment for any firm. As discussed below, most firms are not collecting demographic information about applicants, and some are not collecting other data points such as NAICS and census tract. To reduce the adverse impacts of compliance costs for all firms, we offer the following recommendations.

Small Business Definitions (Responsive to Questions 1 and 2)

Defining small businesses using the SBA's NAICS-specific size criteria would be unnecessarily burdensome and complicated for lenders, researchers, and small businesses themselves. A much simpler approach is needed.

We recommend that the CFPB define small business non-equity financing rather than defining what a small business is. This will avoid the complications that produced the SBA's complex NAICS-specific size criteria, as well as some of the complication of addressing multiple-entity relationships identified in Question 2d.

Specifically, we suggest that "small business non-equity financing" be defined as financing below $1 million, exempting financing to larger firms. Larger firms might be described as those with higher annual receipts of perhaps more than $10 million or $20 million.

Loan size of $1 million is an existing threshold used FFIEC in CRA reporting. Moreover, loans of $1 million or less represent the vast majority of loans sought by small businesses, including 96% of loans sought by startup firms according to the Federal Reserve.[16]

Reporting Process and Data Points (Responsive to Questions 3 and 4)

Financing providers that are adept at utilizing technology will have an easier time complying with Section 1071, while organizations less technologically adept will require greater investment and cost to comply. To reduce the compliance burden for all firms, as an overarching principle the CFPB should structure the 1071 program to make it possible for the required data reporting to be completely automated.

The CFPB should standardize data formats to match those used in reporting to the USDA, SBA, and Treasury Department's CDFI Fund. Furthermore, the CFPB should cooperate with these agencies to create a single, central recipient for this information, which will then distribute it to the relevant agencies. (Responsive to Question 3)

Data points not collected (Responsive to Question 4b and 4c)

[16] "2016 Small Business Credit Survey," Federal Reserve.

NAICS Code - Some financing providers do not collect NAICS code. The NAICS system is quite complex, and requires small business owners or lenders to use a detailed and sometimes ambiguous taxonomy to determine their NAICS code. In some cases, financing providers use SIC codes or other more general industry classifications. We believe NAICS code should be an optional field, not required if it unavailable to the reporting organization. (Also responsive to Question 7)

Census Tract - Financing providers often do not collect census tract information. However, census tract information is valuable for determining what geographic communities are being served. The CFPB should provide a tool to enable financing providers to convert the address and zip code information to census tract in a completely automated way. Up-to-date tables converting zip code to census tracts would be one option. Although zip code alone may not always identify a single tract, zip code information is widely held, if not universal, and so would be a lower-burden method of collecting geographic data. Simple software to convert addresses to census tracts is another option. Additionally, when publishing data, the CFPB should consider whether geographic information such as census tract or zip would compromise borrowers' privacy by allowing the public to infer the identities and financial information of individual firms.

Collection of additional pricing data points

APR - As irresponsible business lending has grown since the passage of Dodd-Frank Act Section 1071, it may be important to understand not only whether financing is being provided, but also at what terms. A whitepaper by Opportunity Fund found that the average APR on products provided by alternative lenders to small businesses reaching out to Opportunity Fund was 94%, and ranged as high as 358%.[17] Research by the Woodstock Institute also identifies APRs ranging up to 350%.[18] If the Section 1071 data collection indicates that access to capital is improving, but is blind to whether that capital is at 10% APR or 300% APR, Congress' purpose will not be accomplished.

If the Bureau collects pricing data in addition to the data points specifically noted by Congress, pricing should be collected in the form APR. For products such as cash advances or factoring which may not have a fixed APR, a projected APR should be used until the financing has been repaid and an actual retrospective APR can be determined. Every financing provider has an annualized return that they expect to earn from a financing transaction, whether or not they are disclosing an estimated annualized cost of capital to the borrower. Additionally, reporting a retrospective actual APR may be important in many cases, because actual use behavior including prepayment, loan flipping, and "double dipping" may result in higher APRs as terms are shortened and multiple loans may be "stacked."

[17] Opportunity Fund, "Unaffordable and Unsustainable: The New Business Lending on Main Street." May 2016. https://www.opportunityfund.org/media/blog/unaffordable-and-unsustainable-new-opportunity-fund-report/

[18] Woodstock Institute, "Analysis of Business Loan Terms." http://www.woodstockinst.org/research/analysis-business-loan-terms

If pricing data is collected, it should be prohibited from being published broken out by demographic group at a firm level, or it will risk creating significant confusion and undue regulatory burden. Fair lending analysis requires sophisticated techniques to determine whether differences in pricing result benignly from differences in creditworthiness, or represent unequal outcomes. Unfortunately, collecting data to establish creditworthiness in order to perform this analysis requires many more data points than would be prudent for the Bureau to collect. While HMDA data collection may be able to benchmark consumer creditworthiness with a credit score variable, small businesses are much more heterogeneous than mortgage borrowers and not as easily benchmarked. Standard small business credit scores are not available for a very significant portion of businesses, and are not as effective at classifying risk as standard consumer credit scores for consumers. Additionally, small business creditworthiness is evaluated in different ways. Benchmarking may require different data points for different types of business and financing products.

For these reasons, if pricing data is collected, it should be published in concert with demographic information only in aggregate, such as at an industry or multi-firm level. At an individual firm level, publication of pricing information by demographic groupings risks creating fair lending conflicts that are not based in adequate analysis. In other words, the CFPB may permit the publishing of the APR range and averages of a certain firm, and the demographics of the applicants the firm has served. It should not permit publishing of the APR averages provided to different demographic groups by that firm, or applicant-level information including both pricing and demographic information. If pricing data is restricted from publication in concert with demographic information at a firm level, this unnecessary confusion and undue regulatory burden can be avoided. (Responsive to Question 6)

Outstanding balance or Term length - It may be valuable to know the term length of the financing to understand the volume of capital being provided. A loan is a lease of capital. Just as a 36-month car lease provides more car than a 6-month car lease, in some sense a 36-month loan provides more capital than a 6-month loan. If capital allocation is measured only by the original financing amount, the data will conflate the volume of lending of 6-month and 6-year loans, and so inaccurately portray the degree and manner in which small business are being capitalized. An even more accurate alternative to collecting term length would be to collect the outstanding balance of financing provided.

Collateral – In order to help policymakers, innovators, and others understand small businesses access to capital, the CFPB may consider collecting collateral information in a simple manner. For example, the Bureau could employ a single categorical variable describing whether or not real estate, equipment, cash collateral, or similar "hard" collateral is required.

The availability of collateral is a major constraint on access to capital for small business. Denial for insufficient collateral was the second or third most common reason for credit denial measured in the Small Business Credit Survey of the Federal Reserve banks. Financing shortfalls based on insufficient collateral affected between 27% and 36% of financing-seeking small businesses,

depending on the age and other characteristics of the business.[19] Collateral shortfalls disproportionately affect the credit seeking of minority-owned businesses. For example, while the White homeownership rate in 2015 was 71%, the homeownership rate of Black Americans was 41%.[20] Moreover, the availability of collateral significantly affects the terms at which financing can be offered. A fully collateralized loan may carry low risk of charge-off losses to a lender, while an unsecured loan may carry significant risk of charge-off if the loan is not repaid. Thus including a simple collateral variable could help explain why disparities may exist, or why loan terms differ.

Identifying Minority-Owned and Women-Owned Firms (Responsive to Question 9)

While financing providers often have some of the data points identified by Congress for collection under Section 1071, in most cases they do not have demographic information of the business owner and may avoid collecting this information for compliance reasons or to avoid the potential practice or appearance of discrimination. (CDFIs and Special Purpose Credit Programs focused on serving underserved borrowers are an exception.) We offer the following suggestions to reduce potential regulatory burden in the collection of demographic data.

Collect data only on the owners identified - We recommend that the Bureau accept demographic information on the business owners known to the financing provider, without requiring information on all owners. Financing providers do not always collect information identifying 100% ownership of every small business they serve. In some cases, a financing provider may work with owners representing only a portion of the ownership that is authorized to act on behalf of the business. Collecting information on every owner may inconvenience small business owners that are not actively participating in a business' financing process and cause undue burden. Financing providers should simply report the demographic information provided by all owners identified.

Demographic data optional to small business owners - While financing providers should be required to seek demographic data and report the data they receive, demographic information should of course be optional for business owners to provide. If small business owners feel that they must provide demographic information to financing providers, this may discourage some applicants who are concerned about discrimination. Again, this may disproportionately discourage borrowing by minority-owned businesses. Research has indicated that African Americans are 37% more likely and Hispanic people are 23% more likely than Whites to avoid

[19] "2016 Small Business Credit Survey," Federal Reserve Banks of Atlanta, Boston, Chicago, Cleveland, Dallas, Kansas City, Minneapolis, New York, Philadelphia, Richmond, St. Louis and San Francisco (April 2017). https://www.newyorkfed.org/medialibrary/media/smallbusiness/2016/SBCS-Report-StartupFirms-2016.pdf

[20] Urban Institute Housing Finance Policy Center, as cited in Whitehouse, Mark, "Homeownersihp and the White-Black Wealth Gap," Bloomberg, 2/27/17. https://www.bloomberg.com/view/articles/2017-02-27/home-equity-and-the-white-black-wealth-gap

applying for credit because of fear of rejection.[21] While it is important for this information to be optional for a small business owner to provide, the CFPB should be prepared that this may introduce data gaps that reduce the accuracy of the data.

Permit proxy analysis – In some circumstances it may be appropriate for demographic information to be obtained by the financing provider using proxy analysis as described by the CFPB, such as Bayesian Improved Surname Geocoding (BISG), rather than requesting self-reported information from the small business owner.[22] For example, proxy analysis may be appropriate where small business owners themselves decline to provide demographic information. Proxy analysis may not be sufficient as a general substitution for borrower-collected information, because it can be used only in aggregate and cannot estimate the demographic information of a specific applicant.

Limiting underwriter access to demographic information – Financing providers that are adept at using technology will have an easier time restricting access to demographic information to ensure it will not be used improperly. Many banks and fintech companies use permissioning systems in their databases to limit which employees are able to access certain data points. Additionally, financing providers who operate through online interfaces may be capable of routing information to different functions, so that an underwriter may never see what race an applicant has indicated on their application. However, organizations managing processes in paper may have a difficult time restricting access to data. This is especially true when an underwriter interacts directly with an applicant in person, and is the recipient of the loan application.

Exempting Classes of Financial Institutions (Responsive to Question 10)

While complying with a well-considered implication of Section 1071 may be easier for medium-sized and larger firms, particularly those adept at using technology, it may be relatively more difficult for very small firms. For example, very small traditional lenders operating with paper and manual processes may struggle. New startups entering the small business financing market may have hopes of expanding access to responsible capital, but may need to mature before establishing strong controls. If an exemption granted to certain classes of financial institutions, it should be focused only on very small firms such as these.

Role of Marketplaces, Brokers, and other 3rd Parties (Responsive to Question 11)

In addition to lenders, reporting under 1071 should be required of brokers, marketplaces, and other third-party entities that facilitate the decisions on whether and how small businesses are

[21] Alicia Robb, *Access to Capital among Young Firms, Minority-Owned Firms, Women-Owned Firms, and High-Tech Firms,* Office of Advocacy, U.S. Small Business Administration, Washington, DC (2013); Michael S. Barr, *Minority and Women Entrepreneurs: Building Capital, Networks, and Skills*, Brookings Hamilton Project (March 2015).

[22] CFPB: "Using Publicly Available Information to Proxy for Unidentified Race and Ethnicity: A Methodology and Assessment," Summer 2014. http://files.consumerfinance.gov/f/201409_cfpb_report_proxy-methodology.pdf

offered credit. Collecting data from brokers and facilitators will help policymakers and others understand the growing role these organizations play in providing small business financing, and the effect they may have on access to capital.

The Bureau can avoid double-counting of loans by including an attribute that indicates if the financing was originated by the reporting entity. Facilitators such as marketplaces and brokers would indicate that they did not originate the loans they are reporting, and these loans could be excluded from aggregate information to ensure that each loan is only reflected once. If a bank or nonbank lender provides credit through multiple facilitators, the Bureau could require these different financing programs to be broken out separately in reporting.

Forms of Financing (Responsive to Question 12)

We support the CFPB in collecting data on the wide range of current (and future) financing products used by small businesses, in order to provide accurate information about market activity and to avoid creating unfair advantages for different financing products. For example, credit cards are an increasingly common source of financing from banks, as small business loans have become less of a focus for many traditional financial institutions. Among nonbanks, cash advances are an important type of non-equity financing for policymakers and others to understand. Cash advances have becoming a significant part of nonbank small business financing, and in some cases are associated with irresponsible practices that led this coalition to develop the *Small Business Borrowers' Bill of Rights*, including obfuscation of very high financing costs, misaligned incentives between financing providers and borrowers, double charging borrowers when loans are renewed, hidden prepayment charges, and "stacking" of too much debt.

Definition of Application (Responsive to Question 13)

Section 1071 data on approval rates will produce inaccurate conclusions if the Bureau does not take into account the different stages at which an application may take place in different forms of financing. For products offered online, an application generally represents the first expression of interest by a small business. Many online applications can be completed in a few minutes, and take place before a conversation between the small business and financing provider.

In contrast, applications at more traditional financial institutions often take place after the small business owner has spoken with the financing provider and gathered a range of paperwork required for the application. Those conversations may encourage or dissuade a small business from applying. In some cases, business owners may not apply upon realizing they would not qualify. However, minority-owned firms may be disproportionally discouraged through this process. As described in the National Community Reinvestment Coalition research cited above, bank staff offered to help a white business owner complete the loan application 27% of the time,

and offered to help the black business owner only 12% of the time.[23] In an online lending process, these business owners would already have completed their application. Because approval rates for traditional, offline processes do not include business owners who were discouraged from applying, approval rates of traditional financial institutions are generally inflated when compared to online lending processes.

Small businesses today struggle with access to capital on the one side, and a rise in irresponsible lending on the other. A well-considered implementation of Section 1071, taking into account the recommendations above and other insights gathered through this RFI, will create tremendous benefit for small businesses and spur innovation in the financing providers that serve them. We welcome further discussion of these recommendations, and can be reached at info@responsiblebusinesslending.org.

Sincerely,

The Responsible Business Lending Coalition

Members of the Responsible Business Lending Coalition include:
Accion
Aspen Institute
Community Investment Management
Fundera
Funding Circle
Lending Club
Opportunity Fund
Small Business Majority

Attachments:

- The Small Business Borrowers' Bill of Rights
- List of signatories and endorsers of the Small Business Borrowers' Bill of Rights

[23] Bone, Sterling A., Christensen, Glenn L., Williams, Jerome D., Adams, Stella, Lederer, Anneliese and Lubin, Paul C, "Detecting Discrimination in Small Business Lending," September 12, 2017. Available at SSRN: https://ssrn.com/abstract=3035972. And National Community Reinvestment Coalition comment to CFPB on Small Business Data Collection, September 12, 2017.

SMALL BUSINESS BORROWERS' BILL OF RIGHTS

Small Business Borrowers' Bill of Rights, 2021[1]

The way small businesses borrow money is being transformed. Innovation is creating faster and easier ways to borrow and increasing access to credit in communities that have historically been underserved. However, irresponsible practices have grown as well. The transformation in small business financing that we are experiencing will achieve its potential only if it is built on transparency, fairness, and putting the rights of borrowers at the center of the lending process.[2] This *Small Business Borrowers' Bill of Rights* identifies six fundamental financing rights that we believe all small businesses deserve. These rights are not yet protected by law, in most cases. We encourage the entire small business financing industry to join us in upholding these rights.

1. The Right to Transparent Pricing and Terms

You have a right to see the cost and terms of any financing being offered in writing, in a form that is *clear*, *conspicuous*, *complete*, and *easy to compare* with other options, so that you can make the best decision for your business.

In order to protect your Right to Transparent Pricing and Terms, lenders and brokers must uphold the following practices:

- **Transparent Rate** – Disclose the Annual Percentage Rate ("APR").[3]

[1] The Small Business Borrowers Bill of Rights has been updated in the December of 2020 to incorporate feedback and learnings since the previous revision in 2017. The Small Business Borrowers' Bill of Rights was first launched in August 2015.

[2] The term "loan" and related terms used here, such as "lending," are intended to be interpreted in the broadest sense to refer to all business financing, including loans, lines of credit, merchant cash advances, factoring, and similar products offered and provided to U.S. small businesses. Similarly, the terms "lender" and "borrower" are intended to be interpreted in the broadest sense to include, in the case of lenders, merchant cash advance providers and credit marketplaces that facilitate loans on behalf of lenders.

[3] The annual percentage rate ("APR") is the total cost of financing, including interest, fees, and other required charges, annualized and expressed as a single percentage number. APR is the only established metric that enables informed price comparisons between products of different types, amounts, and term lengths. This is why APR has become the long-standing price metric that people are familiar with, vetted over 50 years of the Truth in Lending Act. An "Estimated APR" should be used for financing such as merchant cash advances, factoring, and similar products with variable term lengths. For a more detailed description of APR calculation, please see the *Small Business Borrowers' Bill of Rights* attestation forms.

- **Clear Comparison** – Present the following seven key terms clearly and prominently, in writing, to the borrower whenever a specific loan offer is presented or summarized for the borrower, such as in a term sheet, offer summary, or equivalent. This complete disclosure should be re-presented if the loan offer changes.

    1. Loan amount, and total amount provided after deducting fees or charges
    2. APR, or Estimated APR in the case of products with variable term lengths
    3. Payment amount and frequency, including the actual or estimated total payment amount per month if payment frequency is other than monthly.
    4. Term or estimated term
    5. All upfront and scheduled charges
    6. Collateral requirements
    7. Any financing charge potentially due at prepayment

    The *Small Business Borrowers' Bill of Rights* does not mandate a standardized form for these disclosures. Where the formatting of these disclosures is not mandated by state law, lenders may use their own designs that are consistent with the *Small Business Borrowers' Bill of Rights*.

- **Plain-English Terms** – Describe all key terms in an easy-to-understand manner. Do not, at any stage of the financing process, use percentages or the term "rate" to describe pricing in metrics that are not the actual interest rate or APR but may be reasonably mistaken for an interest rate or APR. Pricing described as a "factor rate," "simple interest rate," or other novel forms of percentage rates may be easily misunderstood to be interest rates or APRs, but mask that the actual interest rate or APR is much higher.

2. The Right to Non-Abusive Products

You have a right to loan products that will not trap you in an expensive cycle of re-borrowing. Lenders' profitability should come from your success, not from your failure to repay the loan according to its original terms.

In order to protect your Right to Non-Abusive Products, lenders must uphold the following practices:

- **No Debt Traps** – If the borrower is unable to repay an existing loan, extend new credit only if due diligence indicates that the borrower's situation has changed, enabling them to repay the new loan.
- **No "Double Dipping"** – Do not double-charge the borrower. When offering additional financing with a fixed repayment amount to an existing borrower, if requiring their outstanding financing from this same provider to be repaid, forgive any unpaid fixed charges on the borrower's outstanding balance.

- **No Hidden Prepayment Charges –** If, in the event of prepayment, the borrower will be required to pay financing charges other than interest accrued since the last payment, disclose these charges as "prepayment charges." Also disclose any additional charges or fees added in the case of prepayment as "prepayment penalties." Disclose (a) the potential amount of these prepayment charges and penalties in any loan offer summaries, and (b) the actual prepayment charge and penalties at the time of any prepayment. In the case of financing with payments that vary as a percentage of the borrower's sales, a payoff event is considered prepayment if the borrower states the intent to pay off the financing, or in any event of refinancing.
- **Appropriate Product** – Match loan product design and loan product use. If presenting a loan product as designed for one use, do not encourage borrowing behavior contrary to that use. For example, short-term products may be well suited for short term use, but not for ongoing, long-term recurring use. Long-term products with prepayment penalties may be well suited for long-term use, but not for short-term needs.
- **Pressure Free** – Allow borrowers a reasonable time to consider their loan options free from pressure or artificial timelines.
- **Fair Prepayment** – If a borrower requests to prepay or refinance a loan, provide any information required for prepayment within two business days of the borrower's request. To enable small businesses to access the most appropriate financing, the final payoff amount should not vary based on the source of funds used for payoff, funds from a third-party should be considered equivalent to funds from the borrower.
- **Responsive Complaint Management** – If a complaint is submitted requesting action or a response, provide a confirmation of receipt in writing within five days. When possible, research and resolve the complaint in a timely manner.

3. The Right to Responsible Underwriting

You have a right to work with lenders who will set you up for success, not failure. High loss rates should not be accepted by lenders simply as a cost of business to be passed on to you in the form of high rates or fees.

In order to protect your Right to Responsible Underwriting, lenders must uphold the following practices:

- **Believe in the Borrower** – Offer financing only with high confidence that the borrower can repay its *entire* debt burden without defaulting or re-borrowing.
- **Alignment of Interests** – Lenders who receive repayment directly from the borrower's gross sales must also verify, through documents, data from third parties, and/or due diligence, that the borrower can repay all debt and remain profitable, or that it has a credible path to profitability. Lenders should not make loans that the borrower cannot truly afford, even if the lender can find a way to be repaid.

- **Right-sized Financing** – Size loans to meet the borrower's need, rather than to maximize the lender's or broker/lead generator's revenue. Seek to offer the borrower the size of loan that they need, rather than offering the largest amount they could qualify for.
- **Responsible Credit Reporting** – Report loan repayment information to major credit bureaus and consult credit data when underwriting a loan. Such reporting enables other lenders to responsibly underwrite the borrower and helps the borrower build a credit profile that may facilitate access to more affordable loans in the future. Lenders must inform the borrower and any guarantors if they intend to report loan repayment performance to guarantors' credit bureaus only in certain circumstances, such as after a default.

4. The Right to Fair Treatment from Brokers and Lead Generators

You have a right to transparency, honesty, and impartiality in all of your interactions with brokers and lead generators.

In order to protect your Right to Fair Treatment from Brokers, brokers and lead generators must offer:

- **Transparent Loan Options** – Disclose all loan options for which the borrower qualifies through the broker or lead generator's services, indicating the lowest APR option.
- **Transparent Compensation** – Disclose all compensation paid to the broker or lead generator, by either the lender or borrower, in connection with each loan offer presented.
- **Disclosure of Broker Incentives** – Disclose the broker's or lead generator's fee structure and any other financial incentives they have, including whether they receive higher fees for brokering certain loans. Brokers or lead generators who have not legally agreed to act in the best interests of the potential borrower may not state they are acting in the best interest of the potential borrower.
- **No Fees for Failure** – No brokering or related fees can be charged to the potential borrower if the broker or lead generator is unable to find them a loan and if the borrower does not accept a loan secured through their services.
- **Responsive Complaint Management** – If a complaint is submitted requesting action or a response, provide a confirmation of receipt in writing within five days. When possible, research and resolve the complaint in a timely manner.

5. The Right to Inclusive Credit Access

You have a right to fair and equal treatment when seeking a loan.

In order to protect your Right to Inclusive Credit Access, lenders and brokers must uphold:

- **Non-Discrimination** – Uphold the letter and intent of fair lending laws, including the Equal Credit Opportunity Act. Do not discriminate against small business owners on the basis of race, color, religion, national origin, gender identity, marital status, age, or sexual orientation.

6. The Right to Fair Collection Practices

You have a right to be treated fairly and respectfully throughout a collections process. Collections on defaulted loans should not be used by lenders as a primary source of repayment.

In order to protect your Right to Fair Collections Practices, lenders must uphold the following practices:

- **Fair Treatment** – Abide by the intent of the Fair Debt Collection Practices Act and provide borrowers similar protections as described in that Act.
- **Fair Agreements –** Do not utilize confessions of judgement or equivalent legal agreements by which a borrower preemptively agrees to lose disputes with the lender.[4]
- **Responsible Oversight** – Diligently vet and oversee the collections practices of third-party collectors and debt buyers. Do not work with collectors or debt buyers who fail to treat borrowers fairly.
- **Accurate Information** – Transmit accurate, current, and complete information about the loan to third-party collectors and debt buyers.

[4] Lenders currently utilizing confessions of judgement (COJ) are granted 180 days from the date of signing their attestation form to comply with the COJ prohibition. A limited exception to the prohibition is provided for certain Small Business Administration (SBA) loans, for which SBA requires a COJ clause (borrowers based in MD, VA, and PA). The Responsible Business Lending Coalition urges the SBA to remove all COJ requirements, both optional and mandated, from SBA loan documents moving forward.