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National Association of Federally-Insured Credit Unions

December 14, 2020

Comment Intake
Bureau of Consumer Financial Protection
1700 G Street NW
Washington, DC 20552

RE: Small Business Data Collection Rulemaking - Outline of Proposals Under Consideration and Alternatives Considered

Dear Sir or Madam:

On behalf of the National Association of Federally-Insured Credit Unions (NAFCU), I am writing to share our comments regarding implementation of section 1071 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (Dodd-Frank Act). Our comments address the Outline of Proposals Under Consideration (Outline) issued by the Bureau of Consumer Financial Protection (CFPB or Bureau) in furtherance of its obligations under the *Small Business Regulatory Enforcement Fairness Act* (SBREFA). NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 122 million consumers with personal and small business financial service products.

Credit unions support the ultimate objectives of section 1071, which generally seeks to promote access to small business credit on fair and equitable terms. However, there is widespread concern that the complexity of section 1071 data collection and the accompanying burden of adopting new compliance systems will lead to less favorable outcomes for borrowers. In response to a future section 1071 rulemaking, credit unions may need to raise fees and some could exit the small business lending market entirely.

In the context of total regulatory burden created since the passage of the Dodd-Frank Act, the one-time and ongoing cost of future section 1071 implementation could prove unsustainable and reduce the capacity of credit unions to offer affordable small business lending products or remain competitive in the communities they serve. Credit unions often fill a niche role as relationship lenders in communities that lack access to traditional, face-to-face institutions. Many smaller credit unions that engage in small business lending have only a few employees who handle business loan applications. Requiring these and other small, community-based institutions to divert additional resources to data collection duties will likely reduce the efficiency of processing loan applications, and could drive borrowers towards a subset of automated, impersonal lending platforms that have no presence or attachment to America's Main Street communities. Accordingly, the Bureau should consider whether the ultimate beneficiaries of a 1071 rulemaking are small businesses or online lenders not examined by the Bureau.

Given the significant costs associated with section 1071 implementation, and considering credit unions' marginal share of overall small business loan volume, record of fair and responsible lending, and unique statutory constraints, NAFCU urges the Bureau to consider the broadest

possible exemptive relief in any future rulemaking. Additionally, we recommend the Bureau delay issuing any proposal related to section 1071 until the disruptive economic forces created by the COVID-19 pandemic have stabilized, recovery is evident, and the pandemic emergency has ended. Only then can the Bureau properly assess the impact of a future rulemaking, particularly when there is a likelihood that America's "new normal" will entail fundamentally changed economic patterns.[1]

General Comments

Section 1071 amended the *Equal Credit Opportunity Act* (ECOA) to require financial institutions to report information concerning credit applications made by women-owned, minority-owned, and small businesses. The legislative purpose of section 1071 is to facilitate enforcement of fair lending laws and to enable communities, governmental entities, and creditors to identify business and community development needs and opportunities of women-owned, minority-owned, and small businesses. To fulfill that purpose, section 1071 specifies various data points that financial institutions must compile, maintain, and submit annually to the Bureau. The Outline indicates that section 1071 requires financial institutions to report a minimum of sixteen discrete data elements.[2]

Future collection of small business lending data will necessitate significant investments in new compliance systems and training, particularly if the Bureau requires financial institutions to verify any of the required information. NAFCU member credit unions familiar with the Outline regard these costs as significant enough that they would likely consider raising fees on small business credit products to offset compliance burdens. Respondents to NAFCU's October 2020 Economic & CU Monitor Survey ranked what actions they would most likely take if the core ideas in the Outline were finalized. To manage compliance costs, the vast majority of respondents (89 percent) said that they would need to charge higher fees on business products, with a significant number (44 percent) saying that this would also be true for other credit products as well. Additionally, a majority of respondents also indicated that they would expect to change either the set of small business products offered or underwriting practices in response to the implementation of the eventual 1071 rule.

NAFCU surveys also show that credit unions' capacity to absorb additional regulatory compliance burdens is highly limited in the business lending domain. For example, a majority of NAFCU respondents polled in February 2019 reported that staff limitations and insufficient expertise prevented them from retaining a dedicated staff member for SBA lending. Another survey from September 2018, asking questions similar to those presented in the Bureau's 1071 cost survey, found that 54 percent of respondents characterized their overall business lending process as "marginally manual." The same survey revealed that the median number of staff involved in the decision-making and internal reporting process for small business loans was only two. These low-

[1] Testimony of Jerome H. Powell, Chairman, Board of Governors of the Federal Reserve, "Coronavirus Aid, Relief, and Economic Security Act," Before the Committee on Financial Services, U.S. House of Representatives, Washington, D.C. (September 22, 2020), available at https://www.federalreserve.gov/newsevents/testimony/powell20200922a.htm.
[2] See Small Business Data Collection Rulemaking - Outline of Proposals Under Consideration and Alternatives Considered [Outline], Appendix D.

complexity characteristics will place credit unions at a significant disadvantage if section 1071 compliance ultimately translates into longer application processing timeframes.

Opportunity Costs

According to research published by the Federal Reserve regarding the habits of small business owners in relation to nonbank, online lenders, "applicants that chose to seek financing at online lenders reported the most important factors in their choices were the speed at which they expected lenders to approve and/or fund their application."[3] NAFCU anticipates that future implementation of section 1071 will tend to widen the competitive gulf between smaller, community institutions and fintech companies by introducing requirements that act as a speed bump to application approval. Lenders with the economies of scale and the technological sophistication to automate these compliance functions will immediately benefit, while those with minimal staff resources and primarily manual processes will be placed at a significant disadvantage.

The Bureau's Outline omits discussion of the opportunity costs that may be associated with delayed processing of small business loan applications, and how these costs are likely to be borne by institutions of varying complexity. This is particularly concerning given the purpose of the Outline, which is to solicit views on the impact of a future on section 1071 rulemaking on small business entities. The vast majority of credit unions are small businesses based on the SBA size standards (total assets not greater than $600 million), but even within this domain, a majority of credit unions are *very small*—with a median asset size below $40 million. For credit unions in this asset range, fully automated business loan processing that satisfies section 1071 requirements will likely be out of reach. Although many credit unions are eager to adopt new technology and partner with fintech companies to deliver improvements in member service, these investments must correspond with demand. If business loan applicants lose patience with their local credit union because manual systems are relied upon to satisfy data collection requirements, the journey to better technology only grows longer and more challenging. In the long term, this could precipitate credit union departures from the small business lending market as online, nonbank lenders take full advantage of additional opportunities for regulatory arbitrage.

While the Bureau may regard a tilting playing field with ambivalence so long as consumers are served and data is collected, it should not assume too much about the ultimate trajectory of consumer outcomes. Data collected through the Federal Deposit Insurance Corporation's (FDIC) Small Business Data Collection Survey (SBCS) has shown that satisfaction levels with nonbank, online lenders is "far lower than with traditional lenders (net satisfaction of 33 percent at online lenders versus 73 percent at small banks and 55 percent at large banks)."[4] In the Federal Reserve's study of small business borrowers, 63 percent of online lender applicants reported challenges

[3] Board of Governors of the Federal Reserve System, "Uncertain Terms: What Small Business Borrowers Find When Browsing Online Lender Websites," 4 (December 2019), available at https://www.federalreserve.gov/publications/files/what-small-business-borrowers-find-when-browsing-online-lender-websites.pdf.

[4] Id. See also, Small Business Credit Survey, https://www.newyorkfed.org/smallbusiness/small-business-credit-survey-2018.

working with their lender, with more than half saying they experienced high interest rates and almost a third reporting concerns with unfavorable repayment terms.[5]

Statutory Constraints

In addition to opportunity costs, credit unions face unique statutory constraints imposed by the *Federal Credit Union Act* (FCU Act). Field of membership imposes the greatest immediate constraint. For small businesses to secure a loan with a credit union they must be eligible to join the credit union. As a consequence, even if there is greater availability of small business lending data, the strategic marketing efforts of credit unions may not always benefit since the hard boundaries of field of membership (e.g., geographic limits, select employee groups, or other bonds) will remain.

Unlike fintech companies and other institutions that operate nationally, credit unions cannot easily shift their attention to new markets where there might be identifiable gaps in business credit availability. They are limited by the boundaries of their charter. Not surprisingly, this same limitation accounts for credit unions' keen understanding of the credit needs in the communities where they operate. In other words, credit unions do not need section 1071 data to identify new lending opportunities—limited fields of membership already provide sufficient incentive to pursue growth when the chance presents itself.

Credit unions also face limits on the aggregate number of member business loans (MBLs) they can originate. When Congress passed the *Credit Union Membership Access Act* (CUMAA) in 1998, it restricted the ability of credit unions to offer business loans to their members. CUMAA codified the definition of a MBL and limited a credit union's MBLs to the lesser of either 1.75 times the net worth of a well-capitalized credit union or 12.25 percent of total assets. This aggregate cap impairs credit unions' ability to effectively lend to small businesses and was recognized in the Bureau's recent Data Point on "Small Business Lending and the Great Recession."[6] A far more effective mechanism than section 1071 for expanding business credit opportunities in unserved or underserved communities would be for the CFPB to support legislative amendments to the FCU Act that would eliminate or expand the MBL cap.

To the extent that section 1071 data may be disclosed to the public, credit unions who are constrained by the MBL cap may appear superficially as less willing lenders when additional analysis would reveal that is not the case. The MBL cap also limits the economies of scale possible in business lending units that would otherwise help offset the significant compliance costs associated with new data collection requirements.

NAFCU urges the Bureau to recognize the unique disadvantages of credit unions in the small business lending market and to tailor its rule accordingly. Foremost among our recommendations is that the Bureau exercise the broad exemption authority it possesses under both sections 1071 and 1022 of the Dodd-Frank Act to spare credit unions yet another regulatory burden of significant

[5] Id.
[6] See CFPB, Data Point: Small Business Lending and the Great Recession (January 2020), available at https://files.consumerfinance.gov/f/documents/cfpb_data-point_small-business-lending-great-recession.pdf.

magnitude. In the alternative, we offer recommendations to ease specific burdens throughout the remainder of our comments.

Chilling Effect

In conversations with members, NAFCU has observed that anxiety regarding section 1071's future costs may already be having a chilling effect on future plans to expand small business lending operations. After the passage of the *Coronavirus Aid, Recovery and Economic Security* (CARES) *Act*, credit unions expressed optimism that public awareness of Paycheck Protection Program (PPP) funding might enhance general demand for Small Business Administration (SBA) loans. Credit unions who had never previously sought to promote small business loan products also expressed interest in sustaining small business lending even after PPP funds were exhausted. However, after the Bureau's rulemaking efforts were more widely publicized in September 2020, some credit unions expressed hesitancy about pursuing small business lending due to uncertainty about the costs of future section 1071 compliance.

While it is unlikely that section 1071 implementation will prompt a mass exodus of credit unions from small business lending markets, even a modest number of departures could have an outsized impact, particularly if the nation faces a prolonged economic recovery. Historically, credit unions have played a critical role in helping small businesses recover from financial hardship—particularly those that are unable to find credit elsewhere. According to a 2001 study from the SBA, while banks tend to reduce lending during economic stress, credit unions continue to lend to small businesses.[7] For example, during the period of the Great Recession, credit union lending offset a proportional reduction in bank lending.[8] In January 2020, the CFPB published a data point on small business lending before, during, and after the Great Recession. According to the data point, the number of credit unions offering small business lending products doubled since 2004 (10% to 20%). The data point recognized this increase despite consolidation in the credit union industry and restrictions imposed by the FCU Act.

Covered Applicants

As noted by the Bureau, the comprehensive coverage of women-owned and minority-owned businesses within the scope of small businesses supports the notion that data collection and reporting requirements should only apply to applications for credit from small businesses. Collecting information about women-owned and minority-owned businesses that are not small would create additional operational difficulties in exchange for "limited information beyond what would already be collected and reported about women-owned and minority-owned small businesses."[9] NAFCU agrees that financial institutions should not be expected to collect and report 1071 data for women-owned and minority-owned businesses that are not "small."

[7] James A. Wilcox, The Increasing Importance of Credit Unions in Business Lending, SBA Office of Advocacy (Sept. 2011).
[8] NCUA, Member Business Loans; Commercial Lending; Final Rule, 81 Fed. Reg. 13530, 13532 (March 14, 2016).
[9] Outline, 9.

Definition of Small Business

As used in section 1071, the term "small business" references the Small Business Act's definition of "small business concern" in 15 U.S.C. § 632, which itself is general and open to further interpretation. The Outline includes substantial discussion regarding possible interpretations of the term to facilitate compliance and ease regulatory burden and appears to acknowledge the need for simplicity.

NAFCU and its members believe that for the purposes of section 1071, a small business should be defined in terms of gross annual revenue. Based on the underwriting experience of our members, only businesses with revenues of $1 million or less should be considered small for data collection purposes. In addition, a measure of revenue offers a more straightforward assessment of size and avoids unnecessarily complex references to industry type or employee count.

NAFCU strongly opposes any definition of small business that involves use of the North American Industry Classification System (NAICS), which is used by the SBA to determine whether a business concern is small for the purpose of administering many of its specialized lending programs and government contracting rules. NACIS designations are expressed as a five or six-digit code at the most detailed industry level. The first two digits designate the largest business sector and there are 20 possible options. Small businesses might have more than one NAICS code and the total number of NAICS codes is large (over 1,000 identifiable industries).

Relying on NAICS codes to determine whether a business is in fact small would introduce greater complexity into the reporting process and likely slow approvals of applications, particularly if there is any requirement to independently verify the accuracy of the NACIS code reported by the applicant. Furthermore, NAFCU members who participated in the PPP often noted that many small business applicants did not know what a NAICS code was or how to determine what it should be. Such confusion would also contribute to delayed application processing, borrower frustration, and overall costs borne by credit unions.

Covered Institutions

Credit unions have expressed concern about the extent of exemptive relief contemplated in the Outline. While NAFCU has maintained that credit union should not be subject to requirements under section 1071 due to a variety of unique, statutory constraints related to field of membership and caps on aggregate MBLs, we also believe meaningful consideration of transactional or asset-based coverage thresholds must acknowledge current limitations in National Credit Union Administration (NCUA) Call Report Data.

The NCUA Call Report captures data on all loans over $50,000 to members for commercial purposes, regardless of any indicator about the business's size.[10] As a result, the CFPB's modeling of the relief afforded under various exemption thresholds does not take into consideration the

[10] See NCUA, Call Report Form 5300 (June 2020), https://www.ncua.gov/files/publications/ regulations/form-5300-june-2020.pdf.

variance in loans that may be reportable to the CFPB for the purpose of applying 1071 data collection requirements versus what is reported to the NCUA using the 5300 Call Report instructions. As a result, far more credit union offering small business loans under $50,000 might be swept into a 1071 rulemaking with no reasonable means of offsetting significant one-time and ongoing compliance costs.

Congress' decision to exclude member loans under $50,000 from credit unions' business loan cap, as provided in 12 U.S.C. § 1757a, and the NCUA's corresponding decision to exclude such loans from Call Reports reflect a general desire to reduce administrative and capital burdens which would otherwise frustrate credit union members' ability to obtain very small member business loans (MBLs). The CFPB should recognize that credit union lending on this scale serves an important role in terms of addressing Main Street credit needs, particularly among sole proprietorships. Accordingly, as the Bureau considers various methods for providing exemptive relief through transactional thresholds, it should exclude from any total calculation of small business loans those credit union MBLs under $50,000.

In addition to excluding MBLs not reportable to the NCUA from exemptive relief calculations, NAFCU recommends the Bureau adopt both transactional and asset-based coverage thresholds at significantly higher levels than what is currently proposed. Doing so will provide the greatest degree of regulatory relief short of an exemption.

The Outline's proposed options for transactional or asset-based exemptions fall short of what is necessary to provide meaningful relief. Furthermore, it appears that in the process of calculating the percent of depository institutions covered under the various options, the Bureau has relied on total loans held in portfolio as a proxy for originations, which might understate the actual number of originations that would most directly impact coverage under an eventual rule. The Bureau also appears to have calculated the number of depository institutions covered under various exemption scenarios by using varying denominators: one that includes all depository institutions (Option A scenario) and one that includes just "small" depository institutions (Option 1 scenario). Lastly, a complete assessment of what share of small business loans would be covered under each of the proposed exemptions is not available for review, with the Bureau focusing instead on the percentage of small depositories covered.[11] This approach makes it difficult to weigh the costs and benefits of the different options. Accordingly, NAFCU recommends the Bureau not proceed with a rulemaking until it is prepared to present a more transparent methodology that takes into consideration small business loan coverage across a wider range of exemptive thresholds.

The Bureau also appears to approach the design of its exemptive options with the assumption that they will be applied universally to depository institutions and non-depository institutions alike. NAFCU questions whether this approach is sensible given the Bureau's acknowledgment that it has relied upon bank and credit union call reports to assess possible exemptive thresholds absent better information regarding non-depository lending data. To the extent the Bureau worries that a unified exemption standard for depositories and non-depositories might result in underreporting, then it should not punish depository institutions with more conservatively tailored options if the

[11] See Outline, 12-13, 45.

assumption is that fewer non-depository lenders will be covered. Given that depository institutions are regularly examined and closely supervised, the risk of under-reporting presents less of a supervisory concern relative to non-depositories.

Regarding the Bureau's specific institutional coverage options, NAFCU believes the upper limits in all cases must be set higher to provide meaningful relief. At the very least, the Bureau should calibrate any future transactional threshold in a way that is no less generous than what Regulation C accommodates in terms of loan volume coverage. Ultimately, NAFCU supports maximum relief using a combination of asset-based and transactional thresholds to ensure that onerous compliance burdens do not frustrate credit union efforts to support their communities and small businesses, especially during a time of critical economic recovery.

Covered Products

The Outline provides that products that meet the definition of "credit" under ECOA and are not otherwise excluded by regulation from collection and reporting requirements will be covered products under section 1071. The Bureau has proposed that covered products under section 1071 will include term loans, lines of credit, and business credit cards. Consumer-designated credit, leases, factoring, trade credit, and merchant cash advances would not be covered credit products. NAFCU supports this approach and agrees that consumer-designated credit should not be a covered product in an eventual 1071 rule.

The Outline clarifies the exclusion of consumer products by stating "that covered products under section 1071 do not include products designated by the creditor as consumer purpose products." NAFCU recommends the Bureau clarify that it will not challenge a credit union's judgment when designating a consumer or business purpose for credit. NAFCU believes that preserving such discretion is critical to mitigating overall compliance risk given that there is no feasible method for validating a latent business purpose in an application for a consumer credit product.

NAFCU recommends the Bureau consider an additional exception for commercial real estate loans made to investors. NAFCU believes it is unlikely Congress intended to include such loans within the scope of section 1071. Many of the proposed loan purpose categories reflect a desire to collect data regarding credit offered to businesses which offer a product or service. Furthermore, the effort of collecting and reporting information regarding real estate loans made to borrowers as investments would not be worth the added burden given the availability of alternative data sources. Often these types of loans are multifamily loans with five or more units already reported under HMDA, which requires lenders to collect information about the gender and race of the borrower/guarantor. Additionally, commercial real estate loans made to investors are typically made to business entities with complex ownership structures, which would create additional hurdles for lenders seeking to determine the principal owners.

Definition of Application

With respect to covered products, the definition of "application" will trigger data collection and reporting under section 1071. NAFCU recommends the Bureau define "application" under section

1071 by adopting the meaning of a "complete application" as defined in Regulation B.[12] To conserve the resources of credit unions, the Bureau must seek to construe the scope of data collected under 1071 narrowly. Using a complete application definition as the trigger for data collection requirements alleviates the significant burden of having to return to the borrower in the hopes of collecting a data point such as gross annual revenue, which applicants are unlikely to provide if they have no intention of completing an application.

While it may be convenient to have data regarding incomplete applications to explore issues related to borrower discouragement, there is no indication that Congress intended for section 1071 to mirror the requirements found in the *Home Mortgage Disclosure Act* (HMDA) and Regulation C. Furthermore, it is likely that many incomplete actions will not reflect discouragement but rather borrower confusion regarding the need to supply unfamiliar data points, such as gross annual revenue or a potential NAICS code designation. To the extent that borrower discouragement intersects with fair lending concerns, the Bureau will have more than sufficient data, as well as its existing examination authorities to investigate ECOA violations involving business products.

Timing of data collection

Although the definition of "application" triggers a covered FI's duty to collect data, section 1071 does not provide further direction on when during the application process information should be collected. The Bureau is considering not specifying a particular time period during the application process when financial institutions must collect 1071 data from applicants. NAFCU appreciates the flexibility afforded with this approach but cautions that it may be impossible to collect required data if an application is withdrawn, incomplete, or denied before the data is requested. Accordingly, NAFCU emphasizes the importance of the Bureau only requiring data collection to be performed after the receipt of a complete application.

Mandatory Data Points

Although NAFCU maintains that credit unions should be exempt from an eventual section 1071 rulemaking, we also wish to share our recommendations regarding how the Bureau might tailor or clarify mandatory data reporting to ease compliance burdens. The mandatory data elements covered in the Outline are addressed below:

i. Whether the applicant is a women-owned business, a minority-owned business, and/or a small business

NAFCU agrees that collection and reporting of women-owned and minority-owned business status should be based solely on applicant self-reporting. It would be impossible in many cases for a credit union to verify whether an applicant was (or was not), in fact, a women-owned or minority-owned business, and doing so on the basis of visual observation or other factors would create unreasonable fair lending risks.

[12] 12 CFR 1002.2(f). A complete application is an application in which the creditor has received "all the information that the creditor regularly obtains and considers" in evaluating similar products.

ii. Application/loan number

The Outline indicates the Bureau is considering a method of assigning and reporting the application/loan number under section 1071 that is similar to HMDA/Regulation C formatting. The Outline suggests that this may reduce initial software development costs. However, many smaller credit unions, because they are exempt from HMDA reporting, do not have preexisting HMDA software solutions to leverage. The Bureau should consider whether structuring any processes or requirements in the rule to match HMDA reporting systems will in fact add burden for smaller credit unions that do not report HMDA data.

iii. Application date

The Bureau is considering proposing that FIs have a grace period of several days on either side of the application date reported to reduce the compliance burden of pinpointing an exact date on which an application was received. NAFCU agrees with this approach and recommends a window of at least seven business days.

iv. Loan/credit type

The Bureau is considering proposing that FIs report the loan type data point via three sub-components: loan type, type of guarantee, and loan term. Many credit unions do not currently collect information regarding loan or credit type in connection with business applications for credit. Accordingly, NAFCU appreciates the Bureau's inclusion of choices for "Other," "Unknown," or "Other/Unknown," as appropriate, to facilitate compliance.

For reporting when an application requests more than one type of loan, the Bureau is considering two possible approaches. The first permits financial institutions to classify the loan type(s) using a maximum of the three items from the subcomponent lists for the Loan Type data point if there is only one application and multiple products/guarantees/loan terms were requested. The other approach allows a financial institution to report separate applications/originations for each loan type requested or originated. NAFCU believes the first approach will simplify compliance by allowing consolidation of multiple loan types in a single reportable file. However, there may be other instances where credit unions will want to retain separate applications for each loan type. The Bureau should seek to accommodate either approach.

Regarding the limitation of selecting only three items from the subcomponent lists, the Bureau should clarify whether this is a maximum of three items across all lists or for each list (e.g., loan type and guarantee). The Bureau should also consider expanding the number of guarantees that a financial institution can select. NAFCU has learned that some creditors will stack sometimes four or five guarantees on a single loan product, which would make it difficult to report under the proposed structure. NAFCU recommends applying the three-item limit only to the loan type subcomponent.

v. Loan/credit purpose

Some credit unions do collect loan purpose information in connection with business applications. NAFCU has no objection to the proposed loan purpose list but recommends clarification of certain categories. For example, motor vehicle and equipment could be overlapping options for business purchases of vehicles. The Bureau should clarify whether both categories must be selected or otherwise provide a simple distinction. More generally, the Bureau should seek to minimize the potential for overlap and conflict among the choices presented.

NAFCU also recommends clarifying how loans should be reported when they are made directly to the sole proprietor of a business, but not to the business itself. Small credit unions engaged in small business lending to sole proprietors individually may find it confusing to report a loan purpose that implies that the business itself is the recipient.

vi. Credit amount/limit applied for

The Bureau is considering proposing that financial institutions report the initial amount of credit or credit limit requested by the applicant at the application stage, or later in the process but prior to the evaluation of the credit request. NAFCU believes that reporting the first initial credit request could present an incomplete picture of the lending process which disregards how credit union lenders work with applicants to refine the loan amount. Many small businesses will request a much higher loan amount than what is ultimately approved after evaluation of collateral, particularly in transactions involving real estate or equipment, so there are frequently large variances between applied for credit versus approved credit. For startups and sole proprietorships, lack of sophistication can also lead to initial requests being unrealistic.

In these cases, the credit union will work with the applicant to arrive at a more reasonable amount, which could take place over a period of weeks or months. Given that the extent and length of these pre-evaluation interactions can vary by institution and business sector, NAFCU recommends the Bureau grant financial institutions the discretion to report an "applied for amount" that is determined at later stage, and not the first request of the applicant.

vii. Credit amount/limit approved

The Bureau is considering proposing that FIs report (1) the amount of the originated loan for a closed-end origination; (2) the amount approved for a closed-end loan application that is approved but not accepted; and (3) the amount of the credit limit approved for open-end products (regardless of whether the open-end product is originated or approved but not accepted). NAFCU does not object to this approach but asks the Bureau to explain how it will define the terms "closed-end" and "open-end" credit in the context of section 1071 compliance.

viii. Type of action taken

As noted previously, NAFCU recommends that the Bureau require collection of section 1071 data only when a completed application is received. In conjunction with this framework, NAFCU

believes that it would be beneficial for financial institutions to voluntarily supplement reporting of incomplete or denied applications by reporting a denial reason.

NAFCU does not agree with the Bureau's assumption that the availability of credit might be underreported if counteroffers are not separately identified in the 1071 data set. The number of counteroffers could be potentially numerous when lending to certain businesses—particularly those that are inexperienced borrowers—and difficult to report separately in a cost-effective manner. Developing a single counteroffer data flag could simplify the reporting process by minimizing the need to generate separate reports for multiple counteroffers where items such as loan guarantees or loan type has changed. Based on credit unions' experience with HMDA, there is concern that increase the number of separate date elements will make preforming edits and validity checks more time consuming.

ix. Census tract (principal place of business)

The Bureau is considering proposing that financial institutions report a geocoded census tract based on an address collected in the application, or during review or origination of the loan. The Outline suggests several fallback options if the address where the loan proceeds will principally be applied is unknown. These would be the owner's office or headquarters, or another address on the application. A financial institution would also need to explain which option it is using.

The geocoding requirement will be a source of significant burden for many credit unions, the vast majority of which do not collect census tract information for small business loans. Although some Community Financial Development Institution (CDFI) credit unions collect census tract information, many are completely unfamiliar with how to collect this information—particularly those that are exempt from HMDA reporting. If credit unions do not use the Federal Financial Institutions Examination Council's (FFEIC) geocoding tool to collect census-tract information, most will need to acquire a separate software license from a vendor to implement geocoding. There may also be separate costs incurred for upgrades to business loan reporting systems.

For credit unions who cannot justify the expense of a third-party geocoding tool, there will be a substantial opportunity cost in terms of longer, manual processing times. The FFIEC geocoding tool also does not permit batch inputs, which will slow application processing by a significant degree. For credit unions with limited staff, such a bottleneck could mean losing business as members frustrated by longer approval times look elsewhere.

x. Gross annual revenue

The Bureau is considering proposing that financial institutions report the gross annual revenue of the applicant during its last fiscal year. In general, financial institutions would report verified revenue if known or else whatever the applicant provides if there is no process for verifying. NAFCU recommends that the Bureau not require financial institutions to verify gross revenue. Most credit unions do not collect this information and it is unlikely that small businesses, particularly sole proprietorships, will be able to supply this information easily.

xi. Race, sex, and ethnicity of principal owner(s)

Section 1071(e)(2)(G) requires FIs to collect and report "the race, sex, and ethnicity of the principal owners of the business." The Bureau is considering proposing to define the term "principal owner" in a manner that is consistent with the CDD rule. The Bureau is also proposing that collection and reporting of the race, sex, and ethnicity of small businesses' principal owners be based solely on applicant self-reporting, and would not expect financial institutions to guess if an applicant does not choose to report. NAFCU agrees with this approach.

NAFCU supports the Bureau's proposal to develop a sample collection form to facilitate compliance and communicate an applicant's right to refuse to provide such information. NAFCU recommends expanding upon this concept by developing a model form or platform that could be voluntarily used for collecting all 1071 data. Given the Bureau's interest in leveraging technology and automate to reduce compliance burdens, NAFCU encourages the Bureau to explore the use of a Tech Sprint to develop a free, online tool that can guide applicants through the process of submitting section 1071 data. Such a tool could help reduce technological disparities that are likely to put smaller, less sophisticated lenders at a disadvantage relative to large banks and fintech companies—particularly in terms of opportunity cost.

Discretionary Data Points

Section 1071(e)(2)(H) requires financial institutions to collect and report "any additional data that the Bureau determines would aid in fulfilling the purposes of [section 1071]." The Bureau is considering requiring the reporting of the following "discretionary data points": pricing, time in business, NACIS code, and number of employees. NAFCU does not believe the Bureau should include any discretionary data points in a future proposed rule due to the significant burden of collecting the mandatory data points.

In one survey of NAFCU members, respondents were asked how the addition of new data elements would affect the overall cost of 1071 compliance. The vast majority predicted a moderate (69 percent) or significant (23 percent) increase. The Bureau has even suggested that it may be desirable to have financial institutions verify certain data points, but acknowledged that this could make ongoing reporting 125 percent more costly—an assessment that almost all (92 percent) NAFCU respondents agreed with, with some suggesting that costs would be even higher.

With respect to more detailed NAICS code information, for the reasons already described, NAFCU disagrees that such information will be easily obtained or materially useful in terms of fulfilling the ultimate objectives of section 1071. One statutory purpose of section 1071 is to facilitate enforcement of fair lending—a goal that is not sector dependent. The identification of business and credit needs can be accomplished without explicit reference to NAICS codes, such as by leveraging already existing data sources and voluntary surveys of business owners. Furthermore, sector-specific analysis of business credit supply and demand is best left to the SBA which already collects NAICS information through its lending programs.

Bureau Assumptions Regarding Ongoing Compliance Costs

NAFCU disagrees with certain assumptions the Bureau has made regarding the magnitude of ongoing costs small financial institutions are likely to face when implementation section 1071 requirements. For example, NAFCU is concerned that the Bureau has significantly underestimated the external audit costs that credit unions would likely incur. NAFCU's members have indicated that this cost is likely several multiples higher than the amount listed in Table 7 of the Outline.

Likewise, there is concern that training costs have also been severely underestimated. Some credit unions have suggested that the Bureau's figures in Table 7 would tend to reflect a scenario where the only staff that are trained are those who directly perform section 1071 data reporting functions, and essentially perform the training autonomously. For a very small credit union where only one or two employees handle every aspect of the business lending pipeline, this may be an acceptable assumption. But for credits unions with larger headcounts, or a dedicated commercial lending unit, there is generally an expectation that all employees involved in business lending will receive training on section 1071 compliance given a desire to promote cross-functional expertise. For those credit unions, training costs are likely to be higher, particularly given that training programs may involve the separate input and resources of Human Resources departments. Some credit unions may also choose to contract with third parties to train a large group of employees. Initial impressions of the Bureau's measurements of ongoing costs suggest that such expenses have not been fully considered.

Lastly, the Bureau is potentially overlooking an entire category of opportunity costs. As discussed previously, slowdowns in application processing could result in the loss of business, the cumulative toll of which could ultimately threaten the entire viability of business credit products. The Bureau has not attempted to measure this risk despite its awareness that small institutions will not be operating in a vacuum and will be competing with large banks and fintech companies with access to superior technology who can minimize the impact of opportunity costs through application tools that might, for example, auto-populate NAICs code fields and efficiently identify the principal place of business, census tract, and gross revenue data elements. Although the Bureau may perceive a single standard of compliance as an equitable method of implementing section 1071, credit unions will be placed at a disadvantage due to technological limitations. At the same time, efforts to reduce opportunity costs in small business markets will correspond with implicit investments in new technology to preserve competitive vitality, which the Bureau has also not considered explicitly.

Underwriting Firewall

Section 1071 generally contemplates the existence of a firewall between employees handling inquiries about the applicant's status as a women-owned, minority-owned, or small business and those who perform underwriting, subject to certain exceptions. Under section 1071(d)(2), if a financial institution discovers that an underwriter or others involved in making a determination regarding an application "should have access" to such information (i.e., the type of covered applicant), it must provide the applicant a notice of "the access of the underwriter to such information, along with notice that the financial institution may not discriminate on the basis of

such information." The Bureau is considering proposing that financial institutions need only limit the access of a loan underwriter or other person to an applicant's responses to inquiries regarding women-owned and minority-owned business status under section 1071(b), as well as the race, sex, and ethnicity of principal owners. NAFCU agrees with this approach as information that solely pertains to small business status is not protected under ECOA.

Additionally, the Bureau is proposing to interpret section 1071(d)(2) to permit financial institutions to give underwriters, employees, and officers access to firewall information when the financial institution determines that such access is needed for the underwriter, employee, or officer to perform his or her "usual and regularly assigned job duties." However, the institution would still be required to send notice to the applicant. NAFCU believes that the Bureau should interpret the feasibility standard in section (d)(1) more broadly to limit the need for case by case notice and disclosure. The Bureau should also recognize that instituting an underwriting firewall may be impossible for smaller credit unions with only a handful of employees performing every duty within the business lending pipeline.

Credit unions with limited staff may not be able to guarantee that every employee will have usual and regularly assigned duties, particularly when industry culture has traditionally emphasized on all-hands-on-deck approach. Accordingly, there may be circumstances where employees assume irregular duties which are nonetheless essential for lending operations (such as when credit unions made extraordinary efforts to train staff to facilitate access to PPP loans). To spare credit unions the requirement to send numerous firewall notices on a case by case basis, the Bureau should develop short form language that can be appended to all applications. Institutions with relatively few employees engaged in business lending functions should benefit from an inference that their use of the notice is necessary and appropriate.

Borrower Privacy and Future Balancing Test

As NAFCU has noted in prior comment letters, the publication of small business data from credit unions risks presenting a misleading portrait of overall credit availability due to variables such as field of membership and aggregate MBL limits. As a result of these unique statutory restrictions, credit union lending patterns may not translate easily when compared to other institutions. Accordingly, it is imperative that the Bureau supply a transparent description of the methods and analysis it will apply when evaluating section 1071 data for supervisory purposes.

The Bureau should also recognize that some credit unions may respond to perceived reputational risks associated with data publicization by eliminating certain product offerings or modifying underwriting practices in a way that reduces the overall diversity of small business products. In such a scenario, small businesses could ultimately find it more difficult to acquire credit on favorable terms if financial institutions seek to flatten pricing artificially because they are concerned by the outward appearance of such discrepancies, even when more "fulsome analysis" (as the Bureau suggests) would "conclude that the disparities do not support a finding of discrimination on a prohibited basis."[13] Credit unions may also need to allocate additional

[13] See Outline, 62.

resources responding to examiner inquiries about section 1071 data from NCUA examiners, who will be entering uncharted territory as far as performing fair lending analysis of section 1071 data.

To help credit unions better assess possible reputational concerns, the Bureau must also provide a full and complete explanation of any balancing test it intends to use to limit public disclosure of section 1071 data. Specifically, the full policy of a future balancing test must be included with any initial notice and comment rulemaking. Merely referencing a conceptual framework, and then articulating the full policy later (as the Bureau did when it implemented HMDA) will not suffice. For credit unions to accurately assess the full range of privacy and reputational impacts that might be associated with any proposal, there must be a complete understanding of how the balancing test will be applied. For example, credit unions might approach their assessment of the costs of collecting certain data items by consider how it might be used to reidentify a borrower. The risk of reidentification cannot be fully known unless the Bureau provides a complete description of how a balancing test or other methodology for limiting public disclosure.

NAFCU believes the best approach for protecting small business applicants' privacy is to adopt an alternative to the balancing test. The Outline indicates that the Bureau considered an approach in which it would modify data if an identified privacy risk crosses some significance threshold, without weighing that risk against the benefit of disclosure. Such test may be better suited for protecting the interests of business customers given that the consequences of borrower re-identification can be more severe than in the consumer context. Small businesses generally do not want to broadcast to their competitors their expansionary ambitions, which might be revealed inadvertently through the public disclosure of section 1071 data. Furthermore, the risk of re-identification could be very high in regions where only one or two businesses occupy a census tract or other statistical area, and each operates in a distinct business sectors. A significance test would offer a more versatile and efficient approach to balancing privacy interests given these specific considerations and would be practically essential should the Bureau choose to report NAICS data.

The Outline also explores the idea that credit unions could satisfy the requirement to make section 1071 data available to the public upon request by referring the public to the Bureau's website where section 1071 data would be available. The alternative to this approach, which would be highly undesirable for credit unions, requires financial institutions to make their own data available to the public directly, upon request. NAFCU strongly opposes this proposal due to its implicit operational complexity and data security risks. As the Bureau rightly assumes, direct access through financial institutions will involve greater burden and be less efficient overall.

Implementation Period

NAFCU urges the Bureau to delay for at least one year any formal proposal implementing section 1071. Doing so will afford the Bureau additional time to collect information from a larger sample of credit unions regarding the expected one-time and ongoing costs of small business data collection. Furthermore, the additional time will permit the Bureau to revisit assumptions about the operation of small business credit markets in a stable, post-recovery environment. The social and economic disruption created by the pandemic is still ongoing, and its impact on small

businesses lending has the potential to distort the Bureau's current assumptions regarding the ultimate cost of section 1071 implementation.

For example, the Outline notes that the Bureau relied on established correlations between loan application volume and financial institution complexity in the context of HMDA to derive the classification scheme used to estimate compliance impacts relative to small business loan volume. Reliance on past correlations may fail to capture future changes in small business lending patterns, which could, in turn, influence estimates of ongoing compliance costs. Some credit unions that would be deemed "low-complexity" under the Outline have expanded small business lending operations in response to the pandemic. In most cases, the increase in small business lending volume has not coincided with any meaningful change in the credit union's overall complexity or capacity to absorb compliance costs, but could possibly jeopardize the applicability of any transaction-based exemptive relief in the future. Likewise, NAFCU members who report entering the small business lending market for the first time through the SBA's PPP to help local businesses have done so by leveraging existing resources. The fact that some credit unions may now provide a more diverse range of products does not necessarily equate to greater sophistication or less reliance on manual systems.

To minimize any potential underestimation of compliance costs, or overestimation of expected small business lending profitability going forward, the Bureau should revisit the contents of the Outline through an additional request for information in 2021 before proceeding with a notice of proposed rulemaking. If the Bureau does proceed with a formal rulemaking, it should also seek to address practical implementation concerns in advance of any mandatory compliance date. For example, the CFPB should include alongside any proposal the input it has received from other FFIEC agencies regarding a model framework for extending fair lending supervision using newly available 1071 data.

Unlike mortgages, which are largely homogenous consumer products, business loans can vary widely in design and purpose. Accordingly, applying the same analytical techniques and examination approaches applicable to HMDA enforcement to small business data may yield erroneous results. Absent a clear description of the methodologies that might be employed to perform fair lending analysis using 1071 data suggests, there will likely be a period where examiner expectations are in flux and perhaps inconsistent immediately following implementation. To the extent that credit unions are subject to 1071 reporting, the Bureau must coordinate with other FFIEC agencies, including the NCUA, to develop model examination procedures that are presented alongside any proposal.

Lastly, NAFCU generally agrees with the Bureau's assessment that financial institutions should be given ample time to prepare for compliance following the issuance of any final rule. The Bureau is considering proposing a period of approximately two calendar years to facilitate implementation. NAFCU believes this period should be extended to three years to better account for the magnitude of costs that will likely be incurred and to give vendors ample time to upgrade systems and services to facilitate future reporting. Past experience with HMDA implementation has shown that the Bureau is prone to underestimating the time required for vendors to adapt their products to the requirements of major rulemakings. A three-year post-rule implementation period will better

ensure that smaller credit unions, who are often last in line to receive core system upgrades, are prepared for compliance.

NAFCU's proposed timeframe also avoids any possibility that section 1071 implementation might overlap with adoption of CECL, which becomes effective for credit unions in 2023. Given the current status of the Bureau's litigation in California regarding section 1071, it would be prudent for the Bureau to anticipate the possibility that the U.S. District Court for the Northern District of California might, at the request of plaintiffs, compel the Bureau to issue a final rule before the end of 2021. In this scenario, credit unions would have to prepare for eventual compliance with CECL, the NCUA's new risk based capital rule, and section 1071 all within the same timeframe, creating tremendous operational strains that would likely coincide with greatly increased one-time costs. Adopting a longer implementation period would reduce this hazard, even if the possibility of a 2021 rulemaking is remote.

Conclusion

NAFCU believes the costs associated with instituting a major small business data collection rule will tend to overshadow any hypothesized improvements in supervisory efficiency or market transparency. ECOA already permits the Bureau to detect and remediate discrimination in commercial products and services. The Bureau has never sought to explain how its supervisory toolset suffers from lack of section 1071 data or quantified what tangible benefits would accrue to borrowers if such data were available today. Instead the Bureau has characterized the ambitions of its current rulemaking as fulfilling a Congressional mandate. Yet Congress also enacted section 1022 of the Dodd-Frank Act, and even included a specific exemption provision with section 1071 itself. Section 1071(g)(2) empowers the Bureau to exempt credit unions from the entirety or any aspect of a future small business data collection rulemaking.

The Bureau should exercise the authority granted by Congress to exempt credit unions from a future section 1071 rulemaking. The alternative is to impose yet another data collection regime that is certain to exacerbate the cumulative toll of regulatory burden endured since the last financial crisis, particularly for smaller community financial institutions like credit unions that have experienced significant and ongoing consolidation. Section 1071, like many Bureau rulemakings, will likely drive further consolidation, reduced choice, and potentially result in small businesses losing access to trusted, responsible and affordable community lenders.

NAFCU also urges the Bureau to delay its section1071 rulemaking to ensure that a robust cost-benefit analysis can be performed at the appropriate time—namely, when there is greater confidence regarding how the economy has changed in response to the pandemic. NAFCU appreciates the opportunity to share comments in response to the Outline. Should you have any questions or require additional information, please do not hesitate to contact me at (703) 842-2266 or amorris@nafcu.org.

Sincerely,

Andrew Morris
Senior Counsel for Research and Policy