
Subcommittee on Consumer Protection and Financial Institutions

US House Committee on Financial Services

February 17th, 2022

Submitted by:

The Center for Responsible Lending (CRL), the National Coalition for Asian Pacific American Community Development (“National CAPACD”) and National Association for Latino Community Asset Builders (“NALCAB”).

Dear Members of the Committee:

Working across multiple states and localities and serving different populations, we all have seen and heard first-hand the challenges that minority-owned businesses – and especially those in Latino and Asian American and Pacific Island communities – face in securing the capital needed to start or scale a business. Many of those stories reek of blatant disparate treatment or of policies that have a profound disparate effect on communities of color. It has been well documented that Black and Hispanic loan applicants are required to produce more documentation to support their loan application and received less information about fees, and less friendly service when visiting a small business lender.1 Others bespeak of gaps in small business financing which lead to unmet business and community development needs within the communities we serve and consequently restrict economic mobility and limit the availability of goods and services to our communities.

The consequences of these inequities played out during the pandemic. For example, researchers found that during the first four months of the pandemic, the number of active Black business owners dropped by 19% and the number of Latino and Asian business owners dropped by 10% compared to only a 5% drop for white business owners. Even among those businesses that survived, entrepreneurs of color report experiencing more severe revenue loss as a result of the pandemic than white entrepreneurs; indeed, 79% of Asian-owned firms, 75% of Black-owned firms and 67% of Latino-owned firms report that their businesses are in fair or poor financial condition compared to just over half of white-owned firms.

To better understand the challenges faced by business owners of color seeking access to capital, NALCAB and National CAPACD conducted a survey, asking their members questions about how the businesses they serve acquire small business credit in November 2021. Across the 43 organizations surveyed, respondents reported that 70 percent of the small businesses they serve are underbanked, meaning that although they have access to mainstream banking institutions, they may be unable to utilize many of the financial products offered by banks.2 Entrepreneurs of color shut out from mainstream small business credit products are more likely to rely on family and

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1 Disinvestment, Discouragement and Inequity in Small Business Lending (ncrc.org)
friends or personal lines of credit to fund their businesses. With limited access to small business loans from traditional lenders, one survey respondent noted how in her experience “most lending for marginalized communities is predatory.” Equally troubling, the same respondent noted that many of the businesses owners she serves do not speak English as their primary language and loan documents are seldom translated, making many immigrant borrowers especially vulnerable to predatory practices.³

In addition, among those surveyed, they reported that their clients are most likely to rely on either family and friends/equity partners (60%) or personal credit cards (58%) as sources of credit for their businesses. When asked to identify what financial products their clients are using, survey respondents indicated that among their clients 28% use leasing arrangements, 21% take out traditional business loans from an FI, and 20% use Merchant Cash Advances (MCAs). These survey findings indicate a reliance on personal and non-traditional sources of spending, which is becoming an increasingly common inequity for entrepreneurs and communities of color.

Still, even within the collected survey responses there were noticeable differences between the financial lending experiences of NALCAB and National CAPACD clients. For example, a higher proportion of clients served by NALCAB member organizations, which are disproportionately Latino-owned businesses, take out loans under $50,000. Another key difference between the two survey groups is that clients served by National CAPACD member organizations are more likely to utilize mainstream banks whereas clients of Latino serving organizations are more likely to utilize nonprofit lenders.

Evident within the survey responses is how the impact of COVID-19 on small businesses was exacerbated for small businesses owned by people of color. Relaying their personal experiences, serving small businesses in Latino and AAPI communities, survey respondents noted how pandemic-induced temporary closures, limited access to affordable, non-predatory credit, and a lack of in-language support from lenders offering PPP loans, were the biggest challenges facing their clients. One survey respondent described how “requests for technical assistance for both accessing relief resources and starting new businesses” tripled. Multiple survey respondents discussed the challenges limited English speakers face when seeking in-language support from their lender. In relaying these challenges, a respondent shared how one of her clients, a Vietnamese business owner, sought assistance applying for PPP loan forgiveness. This client was unsure how to find their PPP loan number, required information for a loan forgiveness application, and their lender did not offer any in-language support. One of the many reasons that small businesses are likely to feel “intimidated by banks and prefer smaller, more relationship-based lenders” is because traditional lenders do not provide inclusive customer service, e.g. translated loan documents, to English-limited borrowers.

As previously noted, many survey respondents are increasingly turning to personal and non-traditional sources of funding and assistance, such as friends and financial services outside of mainstream banking institutions. This represents a growing unreached population whose data cannot be officially collected, exacerbating existing inequities. For example, one grocer from Akron, OH, shared in her survey response that as newly-arrived refugees in the U.S.

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Malaysia, “The freedom of being an entrepreneur is what makes me happy. I like being able to work for myself and set my own schedule.” She added that she “...always wanted to open a restaurant and own my business but it was scary when we first came over.” Undeterred, she took English as a Second Language (ESOL), U.S. citizenship, and sewing classes for a year and was eventually introduced by a friend to ASIA Inc., a linguistically and culturally-competent social service programming organization. ASIA Inc. provided the grocer with technical assistance, translation, and interpretation services necessary to successfully navigate application, loan, licensing, and transactional processes.

This story is echoed by many immigrants; according to the U.S. Current Population Survey, 5.1% of immigrants had their own businesses in comparison to 3.7% of U.S.-born individuals between 2010-2011. As a respondent noted, “A trait of entrepreneurs and immigrants alike is persistence. From navigating taxes to visas, permits and deposits, immigrants develop the resilience necessary to navigate the obstacles of entrepreneurship, where courage and perseverance are often prerequisites for success. Similarly, setbacks when starting a business or selling a product are par for the course for entrepreneurs who must have grit to try again.”

It is in light of these experiences that we are submitting this comment which also reflects the information we sent to the Consumer Financial Protection Bureau (CFPB) last month during its public comment period on implementing Section 1071. We have seen the value that the sunlight of disclosure through the Home Mortgage Disclosure Act has provided within the context of residential mortgage lending, and we are confident that Section 1071, if faithfully implemented, can produce similar benefits for the communities we serve. Indeed, those of us that are CDFIs expect to be able to use Section 1071 data to enhance our own ability to provide capital effectively within our communities, while those of us that are community-based organizations expect to be able to use these data to identify those financial institutions which are failing to serve our communities and to take appropriate actions.

In order for Section 1071 to accomplish these vital objectives, the rule the Bureau promulgates must do all of the following:

**Require data collection and reporting across the full range of the small business lending marketplace** – It goes without saying that the rule can act to identify discriminatory practices and unmet business and community development needs only if it covers the small business lender marketplace writ large. In this regard, we support the Bureau’s decision to require lenders with 25 or more originations to report data. Although that may require some of the CDFIs joining in this comment to report data, we are prepared to assume that responsibility and are confident that we can do so without burdening our business operations. We likewise support the Bureau’s decision to require financial institutions offering Merchant Cash Advances (MCAs) to collect and report data under Section 1071 as those products are the most predatory products being offered to those we serve.

**Require reporting of the key data elements that are generally relied upon in underwriting applications for small business credit** – For the rule to achieved its intended purposes, the data collected and reported under Section 1071 must be sufficient to allow data users to understand the characteristics of applicants that are denied credit so as to identify areas of unmet need and also to
be able to compare declined applicants with those who are approved for credit to look for evidence of discrimination. We therefore support the Bureau’s decision to use its discretionary authority to require reporting of such data elements as the NAICS code, number of employees, and time in business. We urge the Bureau to add to the proposed data fields a requirement that lenders that rely on an individual or composite credit score of business owners to report that score, and the scoring model used, just as is currently required under HMDA.

Require reporting of the key data elements that define the price of credit that is offered to applicants for small business credit – Pricing information is every bit as important as underwriting information to identify potential discrimination as well as unmet business needs. Accordingly, we support the Bureau’s decision to use its discretionary authority to require reporting of the interest rate, origination charges, and prepayment penalties. We urge the Bureau to require reporting not only of annual charges during the first year of a loan but also of annual charges in succeeding years to capture the true cost and avoid potential evasion.

Require reporting of disaggregated national origin data – Neither the Latino nor the Asian American and Pacific Islander community that we serve is a monolith and at least in the residential mortgage context experience has shown that different sub-groups of Latino or Asian American borrowers fare quite differently when seeking credit. Thus, we support the Bureau’s decision to require lenders to collect and report data for sub-group among Latinos, Asian Americans and Pacific Islanders (as well as for Black or African Americans).

Provide for robust public disclosure of 1071 data – The value of Section 1071 in shedding sunlight on discriminatory practices and in illuminated unmet business and community needs is, of course, entirely dependent upon those data being made available to the public. We agree with the Bureau that the interest in public disclosure must be balanced against the interest in protecting the privacy of small business owners who apply for credit. However, we urge the Bureau to create a strong presumption in favor of disclosure and to permit modification or deletions only with respect to data fields that are highly sensitive and where the risk of reidentification is clear.

In addition to the above recommendations around data collection, we have attached a summary of survey findings to better inform policies aimed at improving access to credit among microentrepreneurs of color.

We thank the committee for the opportunity to submit our comment.
In 2021, the partners surveyed their networks of community-based organizations, CDFIs, and other SBA lenders about how the businesses they serve acquire small business credit. Across the 43 organizations surveyed, respondents reported that 70 percent of the small businesses they serve are underbanked, meaning that although they have access to mainstream banking institutions, they may be unable to utilize many of the financial products offered by banks.

**Figure 1 shows the distribution of Average Size of Loan/Financing** - Showing a disproportionate number of businesses owned by people of color answer use microloans. The responses show that 68% of clients served by CAPACD and NALCAB member organizations have loans under $50,000. Utilizing 2018 Federal Reserve data on employer firms, ValuePenguin puts the average small business loan amount in the U.S. at $663,000.

The financial sources of assistance for clients of surveyed organizations differ from the average American business, relying on personal and non-traditional sources of funding more often. These funding sources could have severe repercussions for individuals and households of color in the event the business fails. It is important that the CFPB collects information on data on a broad set of products and financial institutions that captures the reality and experiences of these businesses.
Figure 2 shows Products and sources of credit in response to the question “What type of products are entrepreneurs in your community most commonly using to meet their business financing needs?”

The survey results show that the most common funding sources are “Family and friends/equity partners” (60%) and “Personal credit card for business” (58%). These percentages are slightly higher than findings from the 2019 Federal Reserve Banks’ small business credit survey on employer firms. According to the Federal Reserve Banks, 56% of small businesses used “personal savings or funds from friends or family” and 53% “credit cards” on a regular basis.

This comparison shows the business clients of surveyed organizations disproportionately use less traditional sources of finance. For example, according to surveyed organizations, 22% of their clients rely on “traditional business loans from a financial institution to fund their business”. In comparison, information on all small businesses from the Federal Reserve Banks show that 44% used a “bank” for funding.

However, clients of surveyed organizations are more likely to use alternative sources of funding such as “Nonprofit Lenders” (24%) and “Community Pool Funds (kitty)/Lending Circle” (19%) and. This compares to 5% for all small businesses using “Nonprofit/community based funding source” as reported by the Federal Reserves.

Figure 2. Most Common Financial Products and Sources of Credit

Note: Respondents could select multiple options
Figure 3 shows the type of institutions clients of surveyed organizations utilize for their business needs.

The surveyed organizations estimate that about 83% of their clients primarily utilize a mainstream bank. The second most commonly used institutions are “community banks” and “credit unions”. The clients of surveyed organizations are more likely to use “credit unions” when compared to the small businesses reported by the Federal Reserve Banks in 2019 (49% compared to 6% respectively).

Figure 3. Types of Financial Institutions for “Banked” Entrepreneurs

For this part of the analysis, we grouped organizations by their membership in CAPACD or NALCAB. This serves as a rough proxy for racial and ethnic differences in their clients. We recognize that each organization serves a racially and ethnically diverse set of clients, but overall each organization serves a disproportionate number of clients who are AAPI (CAPACD) or Latinx (NALCAB).
There are noticeable differences between the financial practices of clients of surveyed organizations National CAPACD and NALCAB. To ensure equitable lending practices, CFPB must ensure data and information on small business lending that make it possible to disaggregate by race and ethnicity.

The results of the survey conducted by National CAPACD and NALCAB shows that there are noticeable differences in the financial practices of the clients served by their member organizations. For example, a higher proportion of clients served by NALCAB member organizations, which are disproportionately Latinx, take out loans under $50,000 (79% compared to 70% for CAPACD, See Figure 4).

Furthermore, as presented in Figure 5, the survey results also find differences in financial products and sources of credit. Clients of National CAPACD member organizations, which are disproportionately, are much more likely than clients of NALCAB to utilize “Community Pool Funds (kitty)/Lending Circle” to fund their businesses.

**Figure 5. Financial Products and Sources of Credit of Entrepreneurs Served by National CAPACD and NALCAB Member Organizations**

![Financial Products and Sources of Credit Chart]

Finally, we also see differences in the type of institution used by the two racial groups as shown in Figure 6. Clients served by CAPACD member organizations are more likely to utilize mainstream banks; whereas clients of Latinx serving organizations are more likely to utilize nonprofit lenders.
Figure 6. Type of Financial Institutions Utilized by Entrepreneurs Served by CAPACD and NALCAB Member Organizations