**Written Statement**
**CFPB Symposium on Section 1071 Rulemaking - Washington D.C.**
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Thank you for the opportunity to participate on this panel. My name is William Phelan and I have over 30 years in small business lending and credit. I am honored to speak with you about Section 1071 of the Dodd-Frank Act (Act) and appreciate the Consumer Financial Protection Bureau's (CFPB) careful consideration of the implementation of this provision.

I am the co-founder, SVP and GM of PayNet, an Equifax Company. PayNet helps commercial lenders make better decisions through expert credit assessments and market insights. PayNet's database includes more than 25 million and growing small and private business contracts—representing more than $1.6 trillion in obligations.

Equifax is a global data, analytics, and technology company and believes knowledge drives progress. The Company blends unique data, analytics, and technology with a passion for serving customers globally, to create insights that power decisions to move people forward. Headquartered in Atlanta, Equifax operates or has investments in 24 countries in North America, Central and South America, Europe and the Asia Pacific region. Equifax employs approximately 11,000 employees worldwide.

## MINIMIZE COSTS AND BURDENS

A time-series analysis of the commercial credit process shows that a manual underwriting process can consume significant man-hours (up to 100 hours in some cases) and cost approximately $5,000 per application. These high costs have resulted in a well-documented credit gap, especially for certain groups of business owners such as low-income, women-owned, and rural small businesses. Furthermore, given the time and schedule commitments and the number of inter-departmental handoffs, it is not uncommon for the duration of the entire process—from application to adjudication—to take 30 days or longer. With this construct in place, the typical institution can handle a volume of just 10 loan applications per analyst, per month; and at an average booking rate of 50%, this means the underwriting cost per loan equals $10,000. This existing process puts an unfair burden on the lender as well as the borrower, exacerbating the credit gap and keeping much-needed capital away from businesses that need it most.

In addition to the underwriting process, financial institutions conduct periodic reviews of the loans in portfolio in order to assess overall credit quality and revise risk ratings which enables the lender to take timely steps to minimize credit losses. The loan review process involves 15 separate steps in the lending, credit and audit departments. These tasks are essentially a re-iteration of the initially outlined underwriting process that comprise collecting and spreading financial statements, conducting cash flow analysis, and adjusting risk ratings. A review of this process shows a lender takes up to two days of work and at a cost of over $1,000 for a single loan review. The volume of loan reviews means that a typical institution can review 120 loans per analyst per year.

The elevated costs of credit underwriting needed to meet 1071 requirements, combined with the expense of portfolio reviews, requires more efficiencies or we risk a lending pull-back that could worsen the growing credit gap.

## DATA REPORTING

A Reporting File format can be configured to provide automated data feeds of data to fulfill 1071 requirements from their system to be included in the 1071 Repository/Database. This information is combined with information provided by other lenders and information provided by additional information sources. This 1071 repository is available to provide data extracts to meet the reporting needs specified by Congress.

The format and contents of the Reporting File will be used to create and send information to the 1071 repository. The types and definitions of data elements remain critical to achieving Congress's intent. Several data elements possess nuanced definitions that can materially limit analytical results. For example, credit amount applied may or may not include total payment amount, taxes, fees or late payments. Application status contains several nuances that can impact the results of analysis on the fair allocation of credit. Business ownership remains another area of nuances that could significantly impact analyses. Fields that impact the cost of credit are likely to be relevant to the analysis.

Software vendors will likely develop and provide services to create the Reporting File Format to reduce the cost and burden of reporting to the CFPB Repository. Data privacy can be provided through data transmission via secure data encryption. Standard file formats and packaged software programs remain key tools to minimize added costs and burden of implementing 1071. A careful consideration of data elements is necessary to ensure reporting.

## SMALL BUSINESS LENDERS

Small business lenders include banks, online lenders, equipment finance lenders, commercial credit card providers and business to business trade finance. Research shows over 95% of all banks maintain some form of loans to small businesses. However, bank consolidation and branch closures are taking critical lending resources away from local communities. Rural, less populated, and lower income communities often bear the burden of these decisions. There were nearly 10 percent fewer branches in operation in 2017— for all sizes of banks—than there had been in 2008, according to the FDIC 2018 Small Business Lending Survey. A 2017 PayNet study showed that major banks garner the bulk of small business relationships. Almost three-quarters (71%) of all small businesses consider a Top 6 bank to be their primary financial institution, compared to 39% of all U.S. consumers. When banks leave communities, small businesses can be left behind. While community banks may strive to fill the void, they usually only serve less than 50 local businesses. These local financial institutions often struggle with the high costs, additional hours, and advanced technology needed to scale small business lending and reach a broader pool of diverse and less affluent business borrowers. Meanwhile, hundreds of financial institutions provide credit to small businesses via the equipment finance industry. Fintech represents a new form of credit for small businesses through a relatively small number of lenders and a majority of businesses provided credit to customers in the form of trade financing receivables that are payable in some defined period of time such as 30 days.

## CREDIT FACILITIES COVERED BY THE ACT

Of the $28.4 trillion owed by all non-financial businesses, the liabilities comprising the non-financial private credit market account for $5.7 - $6.4 trillion. Estimate Breakdown consists of Depository Institutions accounting for $2.0 - $2.2 trillion in loans. Trade Payables account for $1.9 - $2.5 trillion in liabilities. Other loans and advances make up the remaining at $1.5 - $1.6 trillion in loans among financial and non-financial companies.

The Act clearly designates financial institutions and loans to small businesses for reporting requirements. The Act defines Financial Institution as "any partnership, company, corporation, association, trust, estate, cooperative or other entity that engages in any financial activity." The Act also defines Small Business Loan as a "loan made to a small business." – defining trade credit as a source of credit under 1071. Trade credit is the credit extended by one trader to another when the goods and services are bought on credit. Trade credit facilitates the purchase of supplies without immediate payment. Trade credit is commonly used by business organizations as a source of short-term financing. It is granted to those customers who have a reasonable amount of financial standing and goodwill. Financial and non-financial companies providing $3.5 - $3.8 trillion in Loans fall under the reporting requirements of the Act.

## DEVELOPMENT NEEDS AND OPPORTUNITIES

The Act requires that sufficient data is available to enable communities, government entities and creditors to identify business and community development needs and opportunities of women-owned, minority-owned and small businesses.

The Agency is required to provide compiled information made available to any member of the public upon request in the form required under regulations prescribed by the CFPB. The Agency is also required to make compiled information available to the public generally. Compiled information presumably means tables showing lending total by various metrics including amount of credit made available to minority-owned, women-owned, and small businesses. Other aggregated metrics will likely include amount of credit arrayed by industry, geographies, and business size, among others. Aggregating data that provides the basis for meaningful comparisons will require reporting standardization by data fields and formats. This also needs to be benchmarked against local, regional and national comparatives.

Communities, government agencies, academics, and policy makers will likely analyze the data to determine access to capital. Analyses will likely seek to determine the impact of access to credit on local communities as a source of economic growth. Programs to enable access to credit such as the lending programs offered by the Small Business Administration and others will likely be encouraged. Statistical analytics will be applied to determine whether-or-not access to credit is available in local communities and to compare access to credit against other communities and against the national averages. Likely the CFPB will seek to conduct such analyses. Having data organized in tables with clearly defined fields to create comparisons will be key to accurate analyses.

To create meaningful analyses across 3,142 counties and numerous Census Tracts means data sufficiency techniques and statistical analyses methods must be deployed. Benchmarks against local, regional and national comparatives will be one method of determining the availability of certain types of credit or cost of credit in local markets.

In many counties and census tracts, one financial institution serves as the primary source of credit for local businesses. In certain cases, the local community bank may only serve less than 50 local businesses. Insufficient data will likely result in the inability to determine the "development needs and opportunities" of local businesses. In these cases, borrowing data from adjacent counties or census tracks will be required. In addition, inferences will need to be made to determine local needs and opportunities. Quantitative methodology such as the model credibility theory must be used to arrive at statistically sound results by establishing measures of credibility and standards of full credibility.
Compiling data into statistical measures to prepare data sets for analysis will be a non-trivial activity. Conducting statistical analysis to determine if Fair Lending Laws are met will require time series data that must be groomed and standardized across multiple lenders and across millions of small businesses. The broader objective of setting standards for the reporting of 1071 data remains a non-trivial amount of work. Standards are needed for the data fields' definitions in the data dictionary of 1071 data. Report templates for providing 1071 Information in varying forms suitable for public use must be established that provide the needed information for determining the credit needs of small business, but also to maintain the privacy of individual small businesses, particularly in areas of the country where thinner populations of businesses exist; for example, the sole car wash or doctor's office in a small town. Standards for creating and storing archive data sets is needed to provide the time series data snap shots that can show the changing access to credit as market providers exit and enter new markets. As mentioned above, the 1071 data set will become a prime target for cyber criminals. CFPB can mitigate the risk of a breach of this data once inside CFPB's firewalls by limiting their data collection to aggregated, de-identified borrower data sets, rather than data sets which identify specific borrowers.

**REPORTING PROCESSES**

Two collection processes are available to meet requirements of 1071. PayNet categorizes them into "hubs" reflecting the central focal point for the collection of data. The hubs are CFPB Hub and Financial Institution Hub, outlined as follows.

The Financial Institution Hub meets the intent and is within technological requirements for data collection. Technology needed for small business to report 1071 data can be captured at the point of credit application. This will require changes by implementing a new credit application, training staff, and software modifications. We estimate the data collection cost for a small financial institution to be approximately $100,000, for a medium sized financial institution to be $250,000 to $300,000, and for a large financial institution to be in excess of $1,000,000 per year with the key cost driver based on the number of credit applications processed. One major element of these costs is the requirement to separate underwriting from access to data; if access is provided to underwriting, a notice must be sent to the borrower. Many smaller financial institutions will likely be required to add administrative costs to create a separate data collection department, which will likely raise their costs or reduce their competitiveness at providing small business loans.

**1071 INFORMATION**

It is clear from 1071 SMALL BUSINESS DATA COLLECTION that Congress intends financial institutions to collect and report small business loan data. SEC. 1071 also clearly provides the bureau the right to compile and aggregate data and the duty to make it available to the public. Finally, SEC. 1071 provides rights to the small business to report data or refuse to report as a means of protecting its privacy rights. A viable option for CFPB to meet their requirements as outlined in SEC. 1071 lies in the sourcing of standardized data sets that can fulfill the mandate.

Section 1071 presents added administrative requirements for financial institutions that will likely raise the cost of granting credit to small businesses at a time when they face a credit gap. To ease this cost burden, data warehouse technology that is used today to collect and report data for business and regulatory purposes could be purposed for 1071 data collection into a CFPB Repository. Cross sharing through independent third-parties of 1071 data could lower some of these costs. For example, a third-party provider can match two separate credit applications to different lenders at different times from the same business to validate gross revenues. This approach also provides the benefit of separation of 1071 Data from underwriting for the financial institution and it utilizes currently available technology to collect 1071 data and create 1071 information. We recommend the bureau carefully consider these issues in its decision to implement 1071.