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ECOA Loan Data Collection Background

Section 1071 of Title 10 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111- 203) amends the Equal Credit Opportunity Act (ECOA), adding extensive data collection requirements to the credit application process. These requirements subject all businesses who extend credit to the jurisdiction of the Consumer Financial Protection Bureau (CFPB). This section will come into force upon the issuance of regulations by the CFPB, which has placed this rulemaking on its formal agenda for 2016.

Section 1071 represents a sea change in the area of data collection in commercial transactions. The provision will obligate lenders to overhaul their credit application, information gathering, underwriting, and record-keeping processes, resulting in significant additional costs through added resources and personnel without commensurate benefits beyond the strong protections and safeguards that are currently provided to borrowers under the ECOA. Moreover, such additional costs will undoubtedly lead to the unintended consequence of a reduction in the availability of credit to those who need it most and increased borrowing costs for borrowers, again without commensurate benefits to the small business borrowing community. For these reasons, in recent years, ELFA has advocated for the repeal of Section 1071, and continues to believe that repeal of this provision is the best long-term policy outcome. However, with the possibility of the CFPB beginning its rulemaking process this year, ELFA is asking Members of Congress to weigh-in with the CFPB on this rule-making process.

Section 1071 requires any financial institution, defined to include any business that provides financing options to its customers, to inquire during the credit application process whether any commercial credit applicant is a woman-owned, minority-owned, or small-business enterprise. Inasmuch as the term "financial institution" is defined broadly, this will, as drafted, affect not just traditional financial institutions, but any business that extends credit. The affected universe would include businesses ranging from the expected large financial institutions to the unexpected small "main street" businesses, such as a small hardware store who opens a line of credit for local contractors.

This inquiry is currently prohibited by Section 1002.5 of Regulation B promulgated under the ECOA, which provides, "[a] creditor shall not inquire about the race, color, religion, national origin, or sex of an applicant or any other person in connection with a credit transaction..." These prohibitions were enacted for good public policy reasons that remain valid today; they protect privacy and help insulate the credit process from any potential discrimination, whether real or perceived. Section 1071 is fundamentally at odds with those prohibitions. While the new law did provide for an exemption to 1002.5 for inquiries made under Section 1071, how this

conflict is resolved from a practical standpoint is critical to avoiding legal uncertainty for affected businesses.

Under Section 1071, after a lender inquires whether an applicant for a commercial loan is a small business, minority-owned business, or woman-owned business, if feasible, no one involved in the credit decision may have access to that information. The language does not define "feasible" and will require extensive and expensive modifications to credit application processes and systems by creditors.

The information must be maintained and submitted annually to the CFPB where it may be accessed by the public. Upon request, businesses subject to Section 1071 must also make the information available directly to members of the general public. The creation of a publically available national database of loan terms for credit approved and credit denied will have a significantly adverse impact on competition in the commercial credit market. The ultimate magnitude of this impact is difficult to predict, partially because the CFPB has been given broad latitude in the information required to be collected, but also because the creation of this database is unprecedented in nature and scope.

Ultimately, these new data collection mandates, unprecedented in commercial lending transactions, will have an adverse effect on access to affordable credit (particularly on the small business community who can least afford it) and will impose a costly administrative burden on any businesses that offer financing to their customers. The provision will force those who provide credit to make drastic and expensive changes to their application processes, systems, and technology. ELFA believes that, for each impacted business, it will take many months, and hundreds of thousands of dollars, in many cases, to develop the systems to collect and store data in a manner that complies with the requirements of the law, the costs and burdens of which will be very difficult, if not impossible, for smaller lenders to absorb. By making inquiries as to race and gender, prohibited under current law, this new data collection law inserts intrusive questioning into the business-customer relationship. It also exposes lenders to liability based on what is in many cases very unreliable statistical analysis of data, such as census tracts, which are often heavily correlated to the purely financial factors that credit decisions are and should be based upon. No matter how well intentioned the analysis is, in situations where there is a significant amount of heavily correlated data, it is extremely difficult to conduct an analysis that shows definitively whether actual discrimination is occurring, especially when credit applicants have the option of not providing the data, thereby exacerbating the problem by creating an incomplete data set.

In short, Section 1071 will have the unintended consequence of increasing the borrowing costs of, and restricting the availability of credit to, the small businesses the amendment is designed to benefit, without providing commensurate benefits beyond the robust protections already afforded to borrowers under the ECOA. Lastly, this additional data collection, storage, and reporting will have the unintended consequence of forcing some companies out of the commercial credit business, again limiting the availability of much needed affordable credit to the small business community.

For these reasons, and as other Members of Congress have already noted, ELFA believes that it is critical that this rule-making process takes into account the breadth of the commercial credit market, recognizing that there is unlikely to be a one-size-fits-all solution to enacting Section 1071. Additionally, it is vital that the publicly available database be created in a form that does not do irreparable harm to competition in the commercial credit markets. For these reasons, ELFA believes that it is essential that the CFPB utilize the Advance Notice of Proposed Rulemaking (ANPRM) process in order to gather information about the scope of the industry subject to this regulation. Similar information could and should be gathered through significant public outreach to trade associations similar to ELFA and the holding of public hearings; however, we believe these actions should be viewed as complementary to the ANPRM process rather than as a replacement. The ANPRM process was created exactly for rules like this and **ELFA urges Members of Congress to encourage the CFPB to utilize the ANPRM process.**

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Key Points

- The new data collection requirements under Section 1071 of Dodd-Frank will impose an unnecessary and costly burden on businesses that provide customers financing options.

- This provision will require businesses to overhaul their credit approval processes, thereby resulting in significant additional costs through added resources and personnel. Most, if not all, of these costs will be passed on to the consumer in the form of higher rates, or alternatively force smaller lenders out of business, thereby further restricting access to credit to the small business borrowing community.

- The requirement that businesses inquire whether a commercial credit applicant is a woman-owned, minority-owned, or small-business enterprise is fundamentally at odds with current law that prohibits inquiring about the "race, color, religion, national origin, or sex" of an applicant during the credit process. Current law protects the privacy of the credit applicant, and insulates the credit process from the potential for perceived or real discrimination. While Dodd-Frank did provide for an exemption to these existing prohibitions in order to allow for the collection of this information, it is not entirely clear how this conflict will, from a practical standpoint, be resolved in a way that does not create significant legal uncertainty for affected businesses.

- The creation of a publicly available national database of loan terms for credit approved and credit denied will significantly and adversely impact competition in the commercial credit market and has unknown, but potentially significant adverse impacts on small business owners' privacy.

- Section 1071 would add very little, if any, value beyond the protections currently provided to borrowers under the ECOA. The myriad of issues and costs, as well as the adverse impact to be felt by the small business borrowing community, associated with the requirements of Section 1071 will drastically outweigh any potential benefits.

- ELFA encourages Members of Congress to urge the CFPB to utilize the ANPRM process when they proceed with rulemaking under Section 1071.