January 6, 2023

Via Electronic Mail

Dianna Seaborn
Director, Office of Financial Assistance
Office of Capital Access
Small Business Administration
409 3rd St., SW
Washington, DC 20416

Re: ***Small Business Lending Company (SBLC) Moratorium Rescission and Removal of the Requirement for a Loan Authorization*, RIN 3245-AH92**

Dear Director Seaborn:

The Consumer Bankers Association (CBA)[1] appreciates the opportunity to submit this letter in response to the U.S. Small Business Administration's (SBA or Agency) request for comments on the SBA's proposal to lift the moratorium on licensing new Small Business Lending Companies (SBLCs) and add a new type of entity called a Mission-Based SBLC (Proposed Rule).[2]

In the Proposed Rule, SBA proposes to lift the longstanding moratorium on the number of non-federally regulated institutions that can make loans under the 7(a) program and to create a new type of SBLC called "Mission-Based SBLCs." Accordingly, the Proposed Rule intends to open SBA's flagship 7(a) program to a potentially unlimited number of SBLC lenders, including non-bank financial technology companies, or "FinTechs," that would be regulated solely by SBA. SBA claims that the purpose of removing the moratorium for all types of SBLCs is to fill a capital market gap for underserved markets identified by SBA.

CBA represents many of the country's largest lenders participating in the SBA's 7(a) loan program and we welcome competition from any lender as long as those lenders operate by equal standards and under adequate scrutiny. While the SBA's stated intention for the

[1] The Consumer Bankers Association is the only national financial trade group focused exclusively on retail banking and personal financial services—banking services geared toward consumers and small businesses. As the recognized voice on retail banking issues, CBA provides leadership, education, research, and federal representation for its members. CBA members include the nation's largest bank holding companies as well as regional and super-community banks that collectively hold two-thirds of the total assets of depository institutions.

[2] 87 FR 66963.

proposed changes is to aid traditionally underserved borrowers, a goal which CBA members fully support, we believe the changes, as proposed, will not actually help minority and underserved communities, and could unintentionally harm the very borrowers that SBA is trying to aid. The SBA would be better served to work with Congress to adjust overburdensome lending requirements and low guarantee levels to existing programs (e.g., 7(a) Express), ensuring more low-dollar loans to those small business borrowers in need.

Specifically, our concerns include:

- The proposed rule will not actually promote mission lending. As proposed, the new SBLCs, like the existing SBLCs, would <u>not be subject to any</u> requirements to serve underserved borrowers.
- We believe that SBA's Office of Credit Risk Management (OCRM) lacks the resources to take on additional supervisory responsibility.
- We are concerned that SBA failed to propose any regulatory requirements that would attempt to mirror, for the new SBLCs, the federal regulatory and compliance requirements imposed on depository institutions that are supervised by a federal banking agency or the National Credit Union Administration.
- The SBA states it intends to approve only three new "regular" SBLCs at the current time, however, the actual proposed regulatory language *does not limit* SBA's ability to add an unlimited number of SBLC licenses at any time.
- The SBA is acting hastily by proposing to expand the number of SBLCs before the numerous investigations relating to fraud in PPP and other SBA programs have been concluded by Congress, the IG community, and the Department of Justice.

<u>Discussion</u>

<u>Mission Lending</u>

CBA is concerned that the proposed rules will not actually promote mission lending. As proposed, the new SBLCs, like the existing SBLCs, would <u>not be subject to any</u> requirements to serve underserved borrowers. And while the proposed rule creates a new category of Mission-Based SBLCs to focus on mission lending, it fails to present any clear set of defined or consistent mission-lending requirements for these entities. Instead, the proposed rule states that SBA political appointees will establish participation parameters on a lender-by-lender basis without any minimum requirements and without clearly describing how these Mission-Based SBLCs would fill market gaps.

In addition, the requirements that Mission-Based SBLCs form separate non-profit corporations could present such financial and legal barriers that it may be difficult for the intended non-profit mission entities to participate as envisioned. It would also appear that SBA has provided no details or pathway regarding how new entities not already participating in SBA's Community Advantage (CA) pilot program, such as non-profit CDFIs, would be permitted to apply for a license.

SBA Supervision of SBLCs

The importance of innovation in financial service offerings and products to meet the needs of borrowers and to maintain America's financial competitiveness cannot be overstated. But neither can the importance of transparency, market stability, and borrower protections. CBA has long called on policymakers to recognize and respond to the risks associated with the rapid growth of fintech and other large non-bank providers, which are not held to the same broad federal oversight requirements as traditional banks and credit unions.

In proposing to lift the moratorium, the SBA's assumption of supervisory responsibilities over the new non-federally regulated lenders gives great cause for concern as we believe OCRM lacks the resources to take on additional supervisory responsibility. Under the Proposed Rule, OCRM would serve as the primary regulator for every new SBLC, and SBA states that it has adequate staffing and funding to supervise three additional "regular" SBLCs, or non-mission lending entities, at this time. However, SBA's belief in its supervisory capacity is not in line with SBA lenders' experience that OCRM is operating at its maximum capacity, given its existing responsibilities, low staffing, and limited resources.

Regulatory Guidelines of SBLCs

Banks and credit unions are subject to prudential obligations that include requirements for minimum capital and liquidity, constraints on large exposures, and specific rules on governance arrangements. Prudential requirements for banks consider all activities that an institution performs. Prudent lending standards – including compliance with Bank Secrecy Act and Anti-Money Laundering requirements, concentration caps, safety and soundness parameters, stress test parameters, and other regulatory criteria to promote prudent lending – apply to every 7(a) lending decision made by a federally-regulated bank or credit union. Capital requirements are based on an assessment of the credit, market, and operational risk of the institution as a whole. The focus of prudential requirements is on a financial institution's consolidated balance sheet.

Following the emergence of FinTechs, few adjustments have been made to the perimeters of financial regulations to accommodate their activities as providers of financial services. Accordingly, we are concerned that SBA has failed to propose any regulatory requirements that would attempt to mirror, for the new SBLCs, the federal regulatory and compliance requirements imposed on depository institutions that are supervised by a federal banking agency or the NCUA. Given that SBA proposes to serve as primary regulator to an unlimited number of additional non-federally regulated lenders, we are deeply worried about the potential for imprudent lending behavior that could jeopardize both borrowers and the performance of SBA's 7(a) portfolio.

SBA states that a lender should follow its federal regulator's requirements. While SBA does review and monitor lenders' SBA loan practices and performance, it does not attempt to replicate the extensive supervisory framework that the federal banking agencies and NCUA have in place which governs all federally regulated lender behavior, *including* a federally regulated lender's SBA lending behavior. A complete absence of any federal regulatory standards for new unregulated entities is deeply worrisome and out of line with prudent lending safeguards.

Limits on SBLCs

While the proposed rule includes supplementary information indicating that SBA intends to approve only three new "regular" SBLCs *right now*, the actual proposed regulatory language *does not limit* SBA from adding any number of additional SBLC licenses at any time that the agency sees fit. The unlimited scope of licenses and lack of any cap on the number of loans that could be generated by these new SBLCs is far different from testing a new concept in a gradual and prudent fashion.

Fraud, FinTechs, and SBA Lending

We are concerned that the SBA is acting hastily by proposing to expand the number of SBLCs before Congress, the IG community, the Department of Justice, and law enforcement conclude their investigations related to fraud in the Paycheck Protection Program (PPP). have been concluded by. While these investigations are ongoing, several early findings indicate a direct correlation between PPP fraud and non-bank Fintech participation in PPP. By way of example, the House Select Subcommittee on the Coronavirus Crisis noted that "Recent reports have found that FinTechs and their bank partners handled 75 percent of the approved PPP loans that have been connected to fraud by DOJ, despite facilitating just 15 percent of PPP loans overall."[3] While investigations into potential criminal behavior by FinTech companies in one federal government program (PPP) is still underway, SBA should not invite FinTech entities into another federal government program.

In addition, the Department of Treasury report, *Assessing the Impact of New Entrant Non-bank Firms on Competition in Consumer Finance Markets*, was released on November 16, 2022. The report concludes that while non-bank firms can increase competition and innovation, they have also increased market risk. As a result, Treasury has called for enhanced oversight of non-bank firms. It is hard to reconcile the recent Treasury report raising alarms over the same exact institutions to which SBA is proposing to open the 7(a) program.

Perhaps the most illustrative example of the need to press pause on bringing FinTech into the 7(a) program is the report released by the House Select Subcommittee on the Coronavirus Crisis on December 1, 2022. This report identifies how FinTech participation in SBA's PPP resulted in wide-scale fraud.[4] It also illuminates in detail the ways in which FinTech utilized "inexcusable

[3] https://coronavirus.house.gov/news/press-releases/select-subcommittee-launches-investigation-role-fintech-industry-ppp-fraud

[4] *New Select Subcommittee Report Reveals How Fintech Companies Facilitated Fraud In The Paycheck Protection Program*,
https://coronavirus.house.gov/news/press-releases/clyburn-fintech-fraud-ppp-doj-sba

misconduct" amounting to tens of billions of fraudulent loans, significant harm to the taxpayer, and in many cases, the prioritization of only large loans.[5] This is not what anyone should want to replicate in SBA's 7(a) loan program. The report concludes that "any plans by the SBA to again open 7(a) participation to Fintechs and other unregulated, non-depository institutions must be accompanied by a well-defined, more rigorous, and better-resourced initial review process, and such entities should be subject to continuous monitoring to confirm their adherence to SBA rules and industry best practices."[6]

We would argue that given these recent findings, pressing pause on allowing these types of entities into the SBA's flagship loan program is more than reasonable. This deferment would allow Congress and SBA to better understand the impact of these criminal investigations and reports on FinTechs' damaging and concerning behavior.

* * * * *

We support SBA's continued adoption of efforts to reach borrowers who traditionally do not have long-standing banking or credit union relationships. We understand that automation and other improvements to lending processes may help the traditionally underserved markets. We welcome further discussions with SBA and other policymakers as to how such advancements and simplifications can be incorporated into the SBA loan programs.

Should you need further information, please do not hesitate to contact the undersigned directly at 202-552-6368 or dpommerehn@consumerbankers.com.

Sincerely,

D. P

David Pommerehn
SVP, General Counsel
Consumer Bankers Association

[5] id.
[6] id.