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SECURED FINANCE NETWORK



December 10, 2020

Ms. Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street, NW
Washington, DC 20552

**Re: Comments on Outline of Proposals Under Consideration and
Alternatives Considered for Section 1071 of the Dodd-Frank
Act governing small business lending data collection and reporting**

Dear Ms. Jackson:

This letter provides comments from the Secured Finance Network to the Consumer Financial Protection Bureau's ("CFPB") "Outline of Proposals Under Consideration and Alternatives Considered," (the "Outline of Proposals") in association with the Small Business Advisory Review Panel for the CFPB's small business lending data collection rulemaking under Section 1071 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

WHO IS SFNET?

The Secured Finance Network (formerly known as the Commercial Finance Association) ("SFNet") is the international trade organization founded in 1944 representing the \$4.1T secured finance industry comprised of firms providing asset-based lending, factoring, trade and supply chain finance, leasing and other forms of secured lending, through 280 member organizations in the United States, Canada and around the world. Our network of secured lenders, finance companies, service providers and others do the essential work of providing capital that fuels our nation's economy.

The \$4.1T secured finance industry underpins, either directly or indirectly, about one-fifth of the transaction volume that makes up the \$20 trillion US gross domestic product. We estimate the number of those directly employed in either providing or supporting secured financing activity is approximately 60,000 individuals at over 5,000 commercial banks and another approximately 1,500 non-depository lenders across the US.

Secured transactions provide financing to over 1 million US commercial entities, ranging from single-employee firms to large corporate and public enterprises. Roughly one-third of the approximately 4.6 million firms in the US with at least two employees directly feel the impact of secured finance. And the benefits affect not only the enterprises, but also more broadly their employees, customers, communities and the economy as a whole.

While SFNet appreciates and supports the CFPB's interest in implementing public policy to ensure that all small U.S. businesses have equal access to capital, we request that asset based lenders, factors, purchase order financing and smaller lenders be exempted from the Outline of Proposals.

WHY DO SPECIALIZED LENDERS DESERVE AN EXEMPTION?

Simply put factors, asset-based lenders and purchase order finance entities base their extensions of credit almost entirely on the value of the collateral that supports these disciplines and not upon the identity of the ownership of the businesses they finance. It is SFNet's recommendation that the reporting required under the Outline of Proposals focus on general commercial and industrial credit and not specialized lenders who do not determine credit based upon the race, sex or ethnicity of the borrowers' ownership but rather upon the value of the business' collateral.

Specifically, SFNet suggests that the following categories of specialized lenders be exempted from Section 1071 data collection requirements:

1. Asset-Based Financing.

Asset-based lending is a large class of commercial finance that is notably distinct from cash flow lending and operating lines of credit. Rather than serving as a general line of credit, asset-based lending is a type of financing arrangement that is largely based on the nature, quality and quantity of collateral, specifically a near constantly monitored borrowing base of accounts receivable, inventory (and/or similarly quantifiable collateral). Specifically, so long as the borrower has no record of bad conduct or integrity issues an asset-based lender does not base its approval decision, in any material way on the borrower's principals. Therefore, because asset-based lending is strictly collateral - and not borrower - driven, it should be exempt from Section 1071.

As such, SFNet is recommending that the CFPB provide an exemption from the Section 1071 reporting requirements for financing that is primarily based upon and/or driven by the value borrower's collateral at any given time.

2. Factoring.

As already suggested by the CFPB in its Outline of Proposals, factoring is a financing arrangement that warrants exemption from Section 1071. Pursuant to Regulation B, factoring refers to a purchase of accounts receivable whereby a business sells its unpaid invoices at a discount to a factor. Because factoring arrangements are generally not considered subject to ECOA or Regulation B, it should be exempt from Section 1071 coverage.

Factoring should be exempt from Section 1071 for the additional reason that, because it is exclusively collateral-based, it is separate and distinct from commercial lending. Factoring

companies do not lend money but, rather, engage in a purchase and sale of accounts that meet certain criteria set by the factor.

As such, based on the foregoing, SFNet respectfully submits that factoring should be exempt from the Section 1071 reporting requirements.

3. Purchase Order Financing (“PO Financing”).

Similar to factoring, PO Financing is not a loan but, rather, a purchaser of inventory (or other assets) on behalf of a client. As PO Financing falls outside of the scope of the legislative intent of Section 1071, SFNet suggests that PO Financing be exempt from the Section 1071 reporting requirements

WHY DO SMALL LENDERS ALSO DESERVE AN EXEMPTION UNDER SECTION 1071?

Small lenders engaged commercial credit should also be exempt from the data collection requirements of Section 1071. On the one hand the majority of these providers are the primary financing source for minority owned business given the loan size being requested and the risk profile of these smaller business and at the same time these same providers are least able to absorb the additional regulatory costs associated with the Outline of Proposals.

Specifically:

- a. Section 1071 requires that, “where feasible, no loan underwriter or other officer or employee of a financial institution, or any affiliate of a financial institution, involved in making any determination concerning an application for credit should have access to any information provided by the applicant pursuant to a request under subsection (b)[.]” Although this proposed regulation would pose less of a challenge for federally chartered banks to comply with, it would be a threshold that would be both difficult and unduly burdensome for small financial institutions to meet.
- b. Small financial institutions have limited resources to create a firewall between its loan officers and credit underwriters, which would likely require, among other things, hiring additional staff. Small businesses simply do not have, nor can they afford, the division of labor required to comply with the legislative intent of Section 1071.
- c. Small businesses largely lack the automation to track and report the contemplated data and information for the proposed regulation. Indeed, the finite resources to which small businesses have access must be deployed to generate and service new clients in order to adequately compete and survive in the marketplace.
- d. Even if financial institutions have the necessary means to do so, requiring those institutions to be responsible for collecting the data, verifying ownership structures, minority status and gender, and other information of the principals of the borrowing entities, would be very costly to such businesses and would

significantly raise the borrowing costs for small businesses. It may also lead to the inevitable exit of many financial institutions from the small business lending market because maintaining that portion of their portfolios would simply become impractical.

As such, we support the recommendation that small lending companies with either less than \$500 million in annual new business volume, or fewer than 500 transactions per year, be exempt from the collection.

Each of these proposed exemptions could effectively limit the burden of Section 1071 and limit marketplace disruption, including, but not limited to, the resulting injury to small businesses that the proposed Section 1071 regulation would otherwise create. While there may well be other forms of credit equally suited for exemption (e.g., trade credit and leasing), we are aware that other market constituents have weighed in on such category's requirements under Section 1071.

SFNet wishes to thank the CFPB for the opportunity to provide commentary and insight on the proposed Section 1071 regulation and its potential effects on the small business lending market. SFNet looks forward to working with the CFPB on these important issues.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'R. Gumbrecht', with a horizontal line extending to the right.

Richard Gumbrecht
Chief Executive Officer
Secured Finance Network