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National Association of Federally-Insured Credit Unions

March 22, 2023

The Honorable Roger Williams
Chairman
Committee on Small Business
U.S. House of Representatives
Washington, DC 20515

The Honorable Nydia Velázquez
Ranking Member
Committee on Small Business
U.S. House of Representatives
Washington, DC 20515

Re: Tomorrow's Hearing: "Oversight of the Small Business Administration"

Dear Chairman Williams and Ranking Member Velázquez:

I write to you today on behalf of the National Association of Federally-Insured Credit Unions (NAFCU) to share our thoughts on issues of importance to credit unions ahead of tomorrow's hearing, "Oversight of the Small Business Administration (SBA)," with SBA Administrator Isabella Guzman. NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 135 million consumers with personal and small business financial service products. We are pleased to see the continuing support for the SBA in the President's budget proposal. We would also like to thank you for this opportunity to provide input on other matters relating to oversight of the SBA.

As champions of financial inclusion, credit unions have been at the forefront of efforts to increase access to personal and small business financial services for underserved communities. Credit unions have grown their overall business lending portfolio by more than 20 percent this past year, which is nearly identical to the growth rate over the past five years. At the same time, NAFCU has worked tirelessly to ensure that non-depository financial institutions such as fintechs operate on a level playing field with credit unions to protect consumers and small businesses by instituting appropriate financial safeguards and compliance processes. Unfortunately, we are concerned that two recent actions by the SBA may end up running counter to both of these efforts by opening the programs to more underregulated competition.

On October 26, 2022, the SBA published the Affiliation Proposed Rule that would loosen affiliation standards, lending criteria, and loan conditions in the SBA's 7(a) Loan Program and 504 Loan Program. Shortly thereafter, on November 7, 2022, the SBA issued a proposed rule that would rescind the agency's decades-long moratorium on the licensing of new Small Business Lending Companies (SBLCs), in effect allowing fintech lenders that are only supervised by the SBA's Office of Credit Risk Management to participate in the 7(a) Loan Program (SBLC Proposed Rule). While these two proposals were issued separately, they would have the combined effect of loosening 7(a) lending standards at the same time as opening that program to entities already proven to be more susceptible to fraud than traditional depository institutions overseen by federal prudential regulators. It may be appropriate to reduce 7(a) lending standards for institutions already bound to follow underwriting requirements set by their prudential regulator, but any newly licensed SBLCs would have no such processes to fall back on. Fintechs

would then be participating in an unfamiliar-to-them lending program with few established standards to follow, and subject only to oversight from the SBA that does not include supervision for 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.

Allowing fintechs to participate in 7(a) lending on those grounds would place credit unions and other traditional lenders at a severe competitive disadvantage. Non-depository SBLC lenders implementing less stringent underwriting requirements, and with significantly less regulatory compliance cost, would expend fewer resources to offer SBA loans and would therefore be able to offer these loans at more favorable terms. Small businesses would gravitate toward these riskier lenders, reducing demand for SBA loans from depository institutions and gradually reducing the number of depository institutions participating in SBA lending. With a greater reliance on fintech lenders, SBA lending programs would be at increased risk of fraud, credit losses, and reputational risk. This risk was clearly demonstrated in the early stages of the pandemic when fintechs participating in the Paycheck Protection Program experienced much higher levels of fraud compared to regulated financial institutions.

The economics of smaller dollar business lending are challenging and a lack of comprehensive regulation and supervision over fintechs makes them prone to fraud. Fintechs streamline processes and increase efficiencies by assessing creditworthiness with business credit scoring models and leveraging AI and big data analytics to speed up loan approval processes. This faster, less costly approach to lending may appear to be beneficial; however, there are reasons behind many of the regulations governing traditional financial institutions and every new approach to lending has trade-offs. As the Committee conducts its oversight over the SBA, we urge you to call on the agency to reconsider these proposals and the impacts that they may have on community lenders.

We thank you for the opportunity to share our thoughts and look forward to continuing to work with you on improving the SBA's lending programs. Should you have any questions or require any additional information, please contact me or Lewis Plush, NAFCU's Senior Associate Director of Legislative Affairs, at (703) 258-4981 or lplush@nafcu.org.

Sincerely,

Brad Thaler
Vice President of Legislative Affairs

cc: Members of the U.S. House Committee on Small Business