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Before the Subcommittee on Investigations, Oversight, and Regulations  
Committee on Small Business  
United States House of Representatives  
Thursday, July 28, 2011

## **Introduction**

Thank you, Chairman Coffman, Ranking Member Altmire, and members of the Subcommittee for inviting me to testify today on the subject of small business and the Consumer Financial Protection Bureau. It is my privilege to serve as Deputy Associate Director for Research, Markets & Regulations at the Consumer Financial Protection Bureau (CFPB).

Small businesses are a critical issue. Half of all American workers are employed by companies with fewer than 500 employees, and small businesses create two-thirds of all private sector jobs. Many small businesses today report having difficulty obtaining credit. These difficulties originated in the most severe financial crisis since the Great Depression and in the recession and credit contraction that the crisis produced.

Failures of the regulatory system were a major cause of the financial crisis. One of the system's most profound failures was the fragmented, unaccountable, and ineffective oversight of consumer financial markets.

To address this failure Congress created the CFPB. We are already hard at work to fulfill the objectives Congress set out for us, including: making sure that consumers have better information for making financial decisions; reducing unwarranted regulatory burdens; leveling the playing field for community banks and credit unions and their competitors; promoting transparent and efficient markets that facilitate access and innovation; and preventing discriminatory practices.

Our statutory objectives and authorities focus on financial products and services for consumers. The Bureau does not have jurisdiction over small business credit except in limited cases where Congress has explicitly and affirmatively granted the Bureau such jurisdiction. The main exception is the Bureau's authority to prevent discrimination in business lending. We may also be able to help many potential small business borrowers with better lending data and more accurate consumer credit histories. In addition, we are already working to reduce burdens on small lenders, and we will continue this work.

## **The CFPB is open for business**

The CFPB opened for business last Thursday, July 21. We are already focused on our mission of making consumer financial markets work better. We are working to make rules for these markets more effective, to enforce them fairly and consistently, and to strengthen consumers' ability to

make the decisions that are best for them. Our vision is a market where consumers can see prices and risks and compare products, and firms do not feel pressure to lower their standards to compete.

We are moving in a focused and deliberate way to bring the market closer to this vision. As the Dodd-Frank Act requires, we have begun work on regulations to strengthen mortgage markets. With substantial input from consumers and mortgage lenders, we are working to make federal mortgage disclosures easier to understand and less burdensome. Standards for mortgage servicing and rules requiring mortgage lenders to evaluate borrowers' repayment ability are also key priorities.

We are launching our program for supervising the largest depository institutions and their affiliates. Roughly one-half of our staff will work on supervision and enforcement. Our examiners, many of them with extensive experience with other financial regulators, are beginning their work of ensuring that institutions in our purview comply with consumer financial laws. Rules and procedures are in place to address violations of federal consumer financial laws, and an enforcement team is ready to operate. We are taking consumer complaints about credit cards, with other products to follow. And we are connecting distressed homeowners who contact us with HUD-approved housing counselors.

The expertise and diversity of the team carrying out the CFPB's work will be a tremendous resource. Our leaders and staff come from both the private and public sectors. Some worked for financial institutions in the traditional banking sector, some outside it. Many are seasoned veterans of other federal or state financial services regulators. Some come from nonprofits, others from academia. No viewpoint dominates our staff or leadership other than a commitment to strengthening consumer financial markets. Our expertise and diversity will help keep our actions smart, effective, and balanced.

The Inspectors General of the Treasury Department and Federal Reserve Board have just reported on our effectiveness so far in standing up the CFPB. According to their recent joint report:

“[W]e found that CFPB identified and documented implementation activities critical to standing up the agency's functions and necessary to address certain Dodd-Frank Act requirements. Furthermore, CFPB developed and is implementing appropriate plans that support ongoing operations as well as the transfer of employees and functions . . . .”

And we are working diligently to execute these plans effectively.

### **The CFPB is focused on credit for consumers**

Our focus is on financial products meant for consumers. Our enabling legislation mandates that focus. With narrow exceptions discussed below, the Bureau does not regulate small business credit.

Since 1969 the Truth in Lending Act (TILA), the flagship federal consumer credit law, generally has covered credit only to natural persons, not business entities. And its coverage generally is limited to credit primarily for personal, family, or household purposes, which do not include business purposes. The Dodd-Frank Act applies the same limitation to the scope of the CFPB's new authorities.

Consumers who own small businesses sometimes use consumer credit for a business purpose, but available evidence does not suggest that, as a group, owners borrow heavily for their businesses on credit instruments intended for personal use. For example, a sizable share of small business owners uses personal credit cards to make payments – but only a small share actually borrows (carries a balance) on these cards (12 percent in 2009 according to one survey). A still smaller share borrows significant amounts (6 percent carried a balance larger than \$5,000 according to the same survey).<sup>1</sup> The volume of borrowing on personal cards was as small as one percent of total small business borrowing in 2003, the most recent year for which the figure is available.<sup>2</sup> Similarly, there is some evidence showing a subset of small businesses using proceeds from a first or second mortgage to provide capital for their businesses.<sup>3</sup> Some small businesses use personal credit for some periods in their firms' lives; however, available data do not support a conclusion that small business owners as a group rely substantially on personal credit.

Exceptions to the consumer laws' focus on consumer financial services are few, explicit, and well-defined; they also provide significant benefits to small businesses. The Equal Credit Opportunity Act (ECOA) prohibits lenders from discriminating in the provision of business (as well as consumer) credit on the basis of race, national origin, sex, or other protected bases. The Bureau implements ECOA by regulation and supervises compliance with ECOA for certain lenders. In addition, Congress has applied to business cards two credit card protections of TILA – limiting the liability of cardholders for unauthorized use of the card and restricting unsolicited issuance of new cards. Thus, with few exceptions, the Bureau does not have authority over small business credit.

### **How the CFPB may help small business borrowers**

Although the CFPB's jurisdiction over small business lending is very limited, we hope to be able to help small business borrowers in several ways. First, our efforts to prevent unlawful discrimination should promote a fairer marketplace and thereby promote credit availability. Second, we will provide the market with better data on small business lending. Third, we may be able to help consumers who rely on their personal credit histories when they apply for a business loan.

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<sup>1</sup> Board of Governors of the Federal Reserve System, Report to the Congress on the Use of Credit Cards by Small Businesses and the Credit Card Market for Small Businesses, May 2010, at pp. 1-2.

<sup>2</sup> Id. at p. 2.

<sup>3</sup> William J. Dennis, Jr., National Federation of Independent Business, Small Business Credit in a Deep Recession, February 2010.

The Dodd-Frank Act helps small businesses by filling a major gap in knowledge about the market for small business credit. Section 1071 of the Dodd-Frank Act amends the Equal Credit Opportunity Act to require that financial institutions collect and report information concerning credit applications made by small businesses and women- or minority-owned businesses. One stated purpose of Section 1071 is to strengthen fair lending oversight. The CFPB and other authorities will be able to use these data to improve the effectiveness and efficiency of fair lending enforcement efforts.

New business lending data will also improve understanding of both demand conditions and supply conditions. Reporting these data publicly, as the Act requires, may tend to make the small business credit market more transparent and efficient.

We will move deliberately and with substantial public input to maximize the benefit of these loan data for small businesses and to minimize the cost for their lenders. To develop implementing regulations we will engage the small business community, business lenders, and civil rights and community development groups.

In addition, the CFPB's efforts to help consumers may in particular help those consumers who decide to start up small businesses using their personal credit histories. Business lenders making loans to new small business owners frequently depend on the personal credit histories of the owners to make a credit decision and set the interest rate and other credit terms. The CFPB will strengthen oversight of the credit reporting system, which should both reduce errors in and increase the accuracy of consumers' credit histories. More accurate personal credit histories should improve the market for small business credit, potentially benefitting both start-ups applying for business credit and the lenders that serve this market.

### **How the CFPB may help small business lenders**

Small financial institutions, which frequently make both consumer loans and business loans, are often burdened disproportionately by compliance requirements, as compared to larger institutions. We are working to reduce existing regulatory burdens where feasible and to avoid imposing unwarranted new regulatory burdens. Small financial institutions have also had to compete on a playing field that has tilted too often toward less closely regulated nonbank competitors. We are working to level that playing field.

Our work to make federal mortgage disclosures clearer for consumers and less burdensome for lenders shows our commitment to improving regulation. We understand the deep frustration of lenders that current mortgage forms required by TILA and the Real Estate Settlement Procedures Act (RESPA) are complicated, duplicative, and costly to fill out. We are striving to make the disclosures easier to complete and use. We are interviewing lenders and brokers in our disclosure testing sessions, and thousands of industry participants have submitted comments on prototype forms we have posted on our web site.

Simplifying federal mortgage disclosures is just one example of how we are working to reduce or avoid unnecessary regulatory burdens for small banks. There are many other ways in which we will continue these efforts.

First, we have a large variety of tools besides regulations to fulfill our mandates – including supervision, guidance, enforcement, consumer education, research, and reporting. We expect to conclude in many cases that one or more of these tools would better address a problem, with fewer burdens, than would a new regulation.

Second, we will consider the potential benefits and costs of proposed rules to consumers and covered persons, including small lenders. We will consider specifically impacts on banks and credit unions with assets of \$10 billion or less described in Section 1026 of the Act.

Third, under the Regulatory Flexibility Act (RFA), we must generally conduct a regulatory flexibility analysis unless we certify that a proposed regulation will not have a significant economic impact on a substantial number of small entities. In these analyses we will consider the effectiveness and compliance burdens of a proposal versus less burdensome alternatives. Section 1100G of the Dodd-Frank Act amends the RFA to provide that the analysis must describe any projected increase in the cost of credit for small businesses, and significant alternatives in that light, and we will act accordingly.

Fourth, as appropriate we will seek public input on benefits and costs even before we propose a rule. In our project to reform mortgage disclosures we have engaged and continue to engage extensively with lenders about how to reduce compliance burdens – well before our proposing a regulation. We will also follow the requirements of the Small Business Regulatory Enforcement Fairness Act (SBREFA). Generally, unless we can certify a proposed rule will not have a significant economic impact on a substantial number of small entities, before we propose the rule we will seek input directly from small entities about potential costs and potentially less-burdensome alternatives. We plan to use the SBREFA process to supplement our outreach to small mortgage originators in connection with our development of a combined TILA-RESPA disclosure.

Fifth, as required by the Dodd-Frank Act, we will review the effectiveness of a significant rule we adopt within five years of its effective date.

## **Conclusion**

Thank you again for the opportunity to discuss the CFPB and small business with the Subcommittee. We look forward to carrying out our responsibilities under the Dodd-Frank Act to strengthen the market for consumer financial services. While the Bureau's statutory role with respect to the market for small business credit is very limited, we will work within that role to strengthen that market, too.