January 22, 2019

Robert E. Feldman, Executive Secretary
Attention: Comments, Federal Deposition Insurance Corporation
550 17th Street NW
Washington, DC 20429

SUBJECT: Comments on Request for Information on Small-Dollar Lending (RIN 3064-ZA04)

To Whom It May Concern:

The Local Initiatives Support Corporation (LISC) is pleased to offer comments in response to the Request for Information on Small-Dollar Lending.

LISC is a non-profit housing and community development organization and certified Community Development Financial Institution (CDFI) with offices in 33 cities throughout the country and a rural network encompassing 86 partners serving 44 different states. LISC's work supports a wide range of activities, including affordable housing, economic development, building family wealth and incomes, education, community safety, and community health. LISC mobilizes corporate, government and philanthropic support to provide local community development organizations with loans, grants and equity investments; technical assistance; and policy support.

As part of its efforts to improve low-income families' financial well-being, LISC provides community organizations financial support and technical assistance to operate Financial Opportunity Centers (FOCs). Through LISC's FOCs, clients receive three bundled services -- financial counseling, employment services and benefits counseling – frequently enhanced with low-cost financial products that help build credit, savings and assets. FOCs' mutually reinforcing program components have proven to help people stay motivated, as evidenced by improved job retention; and to improve their economic prospects, as evidenced by improvements in credit scores and in credit building behavior.

**Unmet Consumer Demand**

Without access to affordable credit, residents face hurdles finding jobs, encounter higher costs for everything from automobiles to cell phone service, and have problems finding housing in the private market. The FDIC's 2017 survey of unbanked and underbanked households found that approximately 8.4 million households are unbanked and an additional 24.2 million are underbanked.[1] The lack of bank

[1] FDIC. (2018, October 22). 2017 FDIC National Survey of Unbanked and Underbanked Households. Retrieved December 10, 2018, from https://www.fdic.gov/householdsurvey/

presence in low-income communities hinders the use of financial services. Individuals attempting to access credit products through banks are also dissuaded by a lack of an existing bank account.

Nonbank options, including payday loans with interest rates well in excess of 100%, are often the most readily available options for many low- to moderate-income Americans. The Consumer Financial Protection Bureau (CFPB) reported that 84 percent of payday loan borrowers had a reported annual income of less than $40,000; and that 43 percent of borrowers had a reported income of less than $20,000 annually.[2]

Since the recession, credit access has tightened significantly, thus leaving individuals and families with limited options. In 2016, underserved consumers spent $57.9 billion on fees and interest for short-term loan products that function on an installment basis with terms from several months to 2 years or as a line of revolving credit.[3]

**The Consumer Lending Environment**

The Government Accountability Office (GAO) analyzed the "2015 National Survey of Unbanked and Underbanked Households" data and found that approximately 20 percent of households reported using alternative financial service (AFS) providers for transactions in the past year, and about 8 percent reported using nonbank or AFS providers for credit.[4] Their analysis suggests that lower-income households may have greater demand for small-dollar loans than their higher-income counterparts, but are more likely to obtain them from alternative financial services. These low-income households are less likely to have had consumer credit from a bank because they were discouraged from applying for credit or are not approved. The lack of savings for unexpected expenses and lack of access to credit leaves consumers more likely to fall behind on bills.

The Federal Reserve's "Survey of Household Economics and Decisionmaking" measures the economic well-being of U.S. households and identifies potential risks to their finances. Jonathan Morduch, author of The Financial Diaries: How American Families Cope in a World of Uncertainty, references the annual study to illustrate how a family's income volatility can lead to unconventional spending and/or saving habits. Among households earning less than $25,000 for the year, almost 20 percent experience extreme income volatility. Morduch argues that public support for the poor is designed to pay for specific expenses such as food or medical care, but what families need is a flexible bridge to assist them during parts of the year when they dip below the poverty line. In the Diaries study, informal loans – those with no institutional involvement – were more common than payday, pawn, and auto title loans.

[2] CFPB. (2013, April 24). Payday Loans and Deposit Advance Products. Retrieved December 10, 2018, from https://files.consumerfinance.gov/f/201304_cfpb_payday-dap-whitepaper.pdf

[3] Wilson, E., & Wolkowitz, E. (2017, December). 2017 Financially Underserved Market Size Study. Retrieved December 10, 2018, from https://s3.amazonaws.com/cfsi-innovation-files-2018/wp-content/uploads/2017/04/27001546/2017-Market-Size-Report_FINAL_4.pdf

[4] GAO. (2018, February). Community Reinvestment Act: Options for Treasury to Consider to Encourage Services and Small-Dollar Loans When Reviewing Framework. Retrieved from https://www.gao.gov/assets/700/690050.pdf

Over the course of the last few years, there have been more affordable and responsible alternatives. For example, responsible loan programs that can be accessed through employers, non-profits, and utility and telecommunications companies are viable options to payday alternative loan programs.

Employer-based small-dollar loans have been offered through participating CDFIs and partner experts (e.g., the Center for Financial Services Innovation and the National Federation of Community Development Credit Unions). Through 2016, Opportunity Finance Network's (OFN) Knowledge Network participants had cumulatively lent more than $24 million in more than 25,000 loans to employee borrowers through these programs.[5] In terms of individual products, Community Loan Center of the Rio Grande Valley is a CDFI with a small-dollar loan product that has a loan maximum of $1,000, 18% interest, $20 origination fee, relaxed underwriting standards and features reporting to credit bureaus.

Financial Technology, or "FinTech," has also entered the lending marketplace, but their promises of "efficiency and speed" must be viewed with caution. There is an uncertainty around the industry, and we are wary of automated algorithms that quickly assess creditworthiness without the risk of disparate impact. Focus must be paid on the end user in order to ensure transparent pricing and terms, non-abusive products, fair treatment from brokers, and inclusive credit access. As of 2018, there have been a few advancements in FinTech and CDFI relationships. INSIKT, a fintech company that lends to low income people in California, Illinois, Texas and Arizona, was awarded with CDFI certification in 2018. On the business lending side, Opportunity Fund and LendingClub developed the first CDFI-Fintech partnership to target underserved entrepreneurs. LISC is also working closely with the Financial Solutions Lab (FinLab), managed by CFSI and JP Morgan Chase Co., to assess non-profits relationship with FinTech providers on how to meet the needs of low-income communities.

**How LISC is Serving Low- and Moderate-Income Populations**

LISC's FOCs, which are operated at nonprofit partner organizations, are implementing innovative programming initiatives for residents in our communities who are hard to employ and have limited economic mobility. The FOC's integrated services delivery model makes our approach different and more successful in improving longer term outcomes for clients we serve. The integrated service components are:

1) Access to income supports

2) Financial coaching, and

3) Job placement.

Incorporated in this bundled service delivery model is a data system that tracks detailed budgets, including a client's income and expenses, as well as credit score updates every six months. This data is used to guide their work with individual clients.

The research shows a direct relationship between the number and type of services accessed and the FOC clients' ability to grow their earnings and secure their finances. For instance, those who spent the

[5] Opportunity Finance Network. (n.d.). Expanding Employer-Based Small Dollar Loan Programs and the CDFI Industry: Learnings from the Knowledge Network. Retrieved December 6, 2018, from https://ofn.org/sites/default/files/EBSDL White Paper-final.pdf

most time on all three bundled services offered by the FOCs had the highest job placement rates and the highest job retention rates—a 74 percent placement rate and a 78 percent six-month retention rate.[6] The goal of our FOCs is not just to place individuals in jobs but to help them keep those jobs so that they have more financial control of their futures.

**LISC's Twin Accounts Initiatve**

After recognizing a dearth in financial credit building products tailored for low- to moderate income individuals, LISC created the Twin Accounts program. Building off of the Financial Opportunity Center program, which combines workforce services with financial coaching and access to income supports to promote financial stability for largely low-income participants, Twin Accounts is available around the country.

LISC Twin Accounts combines the incentives provided in an Individual Development Account (IDA) with credit building to achieve a high level of impact on an individual's financial bottom line. Participants are issued a 12-month, $300 loan which is transferred into a "locked" savings account, where it remains until the loan is paid off. By the end of the twelve month program, participants have not only saved $300, but they have also earned a match on every on time payment, doubling their savings to $600, and their payments are reported to the major credit bureaus.

By participating in this program, individuals not only build their savings, they also begin to build their credit. For many, the LISC Twin Accounts is the first connection point to traditional banking. Over one thousand clients have participated – with over 80% completing successfully. Most clients pay off the loan in full within 12 months, and to help them continue building credit beyond the term of the loan, they must use their matched funds to open a secured credit card. On average, clients with a positive impact on their credit score saw a 40 point increase. For those who are scored, median score at entry is 582 and at exit is over 610.

Participants must work with a LISC-supported financial counselor who is also a certified credit-building counselor at a participating FOC. For the Twin Accounts product to be available to clients, they must have at least one counseling session with the financial counselor in which a detailed budget is completed with the client.

Ongoing counseling with clients is important to prevent negative marks. LISC's Twin Accounts program is designed to follow financial coaches and Twin Accounts managers to work with clients to close their loans early if the participant is unable to keep up with payments, with the goal of avoiding a negative hit to the participant's credit. Usually an external issue causes clients to miss payments such as a job loss or other financial strain, and coaches can work with the client to address the root cause and decide if Twin Accounts is still a good fit.

Credit cards trigger the creation of consumer credit reports more frequently than other products such as auto loans or student loans. The Bureau has found that consumers in lower-income neighborhoods are more likely than consumers in higher-income neighborhoods to acquire a credit record from non-loan

[6] Rankin, S. (2015, April). Building Sustainable Communities: Integrated Services and Improved Financial Outcomes for Low-Income Households. Retrieved December, 2018, from http://www.lisc.org/media/filer_public/8d/d0/8dd0ddcd-e6b4-443a-bf47-a0c67096e212/041415_srankin_foc_report.pdf

items, such as third-party collection accounts or public records.[7] We support bank small-dollar loan repayment be tracked to help build stronger credit histories, which in turn could help consumers qualify for lower-rate financial products.[8]

Participants in LISC's credit builder loan had higher six- and twelve-month employment retention rates, perhaps indicating a greater ability to weather financial crises or stronger connection to all FOC services including employment counseling. The findings of this analysis provide support for the continuation and expansion of the Twin Accounts program.[9] While we believe that increased access to capital is a benefit for the population we serve, an important part of clients' success results from the high touch client interaction and integrated service delivery model.

**Why Work with Community Based Organizations**

There are various factors that may discourage consumers from seeking responsible, prudently underwritten small-dollar credit products. According to the FDIC, 30% of unbanked households cited their mistrust of banks as a reason for not having an account, the second-most commonly cited reason.[10] LISC, as well as other asset building organizations[11], helps move people out of poverty by providing counseling/coaching support and a bridge to appropriate services. We operate as a responsible and relationship based lender throughout low-income communities nationwide. Our relationships with deeply engrained community based organizations allows us to reach populations not served by mainstream financial institutions.

Experience from the FDIC's Small-Dollar Loan Pilot Program has proven that banks can offer reasonably priced alternatives to high-cost, short-term credit. The pilot defined small-dollar loans as low or no-fee loans of $2,500 or less, with a term of 90 days or more, an APR or 36 percent or less, and a streamlined underwriting system enabling financial institutions to issue a loan discussion within 24 hours of a loan application.[12] We would like to improve the pilot by suggesting that banks seek out stronger community-based relationships.

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[7] CFPB. (2017, June). CFPB Data Point: Becoming Credit Visible. Retrieved December, 2018, from https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/BecomingCreditVisible_Data_Point_Final.pdf

[8] The Pew Charitable Trusts. (2018, February 15). Standards Needed for Safe Small Installment Loans From Banks, Credit Unions. Retrieved December, 2018, from https://www.pewtrusts.org/en/research-and-analysis/issue-briefs/2018/02/standards-needed-for-safe-small-installment-loans-from-banks-credit-unions

[9] Rankin, S. (2017, February). Loan Products for Credit-Building: An Impact Analysis of Twin Accounts. Retrieved December, 2018, from http://www.lisc.org/our-resources/resource/loan-products-credit-building

[10] FDIC. (2018, October 22). 2017 FDIC National Survey of Unbanked and Underbanked Households.

[11] Credit Builders Alliance General Membership. (2018, December 19). Retrieved from https://www.creditbuildersalliance.org/download/3911/

[12] Burnhouse, S., Miller, R., & Sampson, A. (2009). The FDIC's Small-Dollar Loan Pilot Program: A Case Study after One Year. FDIC Quarterly, 3(2), 29-38. Retrieved December 10, 2018, from https://www.fdic.gov/bank/analytical/quarterly/2009-vol3-2/smalldollar.pdf.

As an outcome of the FDIC's Small-Dollar Loan Pilot Program, banks recognized partnerships with community groups were crucial to the success of their programs.[13] With LISC's integrated service model, clients are encouraged to return to the FOC. The median enrollment time was 527 days.[14] We understand that physical locations may be an issue for banks to reach consumers. We encourage banks to work closely with community-based organizations and perhaps co-locating like credit unions have with our FOCs.

The FDIC's Small-Dollar Loan Pilot addressed some of the concerns of banks in offering these types of products, but below we will discuss additional potential benefits and risks with bank offered small-dollar credit products.

A benefit for consumers is their ability to build credit. Taking on debt is the only way to build a credit score, and borrowing is the easiest way to manage illiquidity challenges in the short term. Participants in Twin Accounts had double the credit score gain of non-participants in Twin Accounts and were more than twice as likely to gain a score and keep it (98 percent versus 36 percent in the comparison group). On average, Twin Accounts participants increased their credit score by 35 points, compared to a 10 point increase for non-borrowers.[15]

There are also benefits for banks and consumers when small-dollar loans are made to consumers who have historically been left out. For example, consumers are able to build trust and a relationship with mainstream banking. Several stakeholders, including the Center for Financial Service Innovation, have suggested that lenders should prioritize long-term relationships to small-dollar loan borrowers, suggesting that these borrowers may return for additional products and services over time.[16]

That is not to say that risks do not exists for banks to provide small dollar loans to consumers. Due to the limited profitability of these loans, banks are not incentivized to offer this products.  There are also concerns about possible failure to repay. Consumers and advocacy groups may be concerned with developing negative credit history due to job loss and trouble managing finances. But we are encouraged that there are best practices available for banks to address the short-term capital access needs of low- and moderate-income communities.

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[13] Miller, R., Burnhouse, S., Reynolds, L., & Sampson, A. (2010). A Template for Success: The FDIC's Small-Dollar Loan Pilot Program. FDIC Quarterly, 4(2), 28-41. Retrieved December 12, 2018, from https://www.fdic.gov/bank/analytical/quarterly/2010-vol4-2/fdic-quarterly-vol4no2-smalldollar.pdf.

[14] Rankin, S. (2015, April). Building Sustainable Communities: Integrated Services and Improved Financial Outcomes for Low-Income Households.

[15] Rankin, S. (2017, February). Loan Products for Credit-Building: An Impact Analysis of Twin Accounts.

[16] Garon, T., & Brockland, B. (2017). Designing High-Quality, Small-Dollar Credit: Insights from CFSI's Test & Learn Working Group. Retrieved December, 2018, from https://s3.amazonaws.com/cfsi-innovation-files/wp-content/uploads/2017/01/26043219/CFSI-Small-Dollar-Credit-Test-and-Learn.pdf

We hope that the FDIC and other regulatory agencies take into consideration LISC's experience with the Twin Accounts Program to provide a flexible tool for families to address income volatility, build the financial stability of individuals and protect consumers from predatory financial alternatives.

We thank you for considering these comments, and look forward to working on implementation going forward.

Sincerely,

[redacted]

Matt Josephs
Senior Vice President for Policy