

National Community Reinvestment Coalition's Written Testimony for the U.S House Committee on Financial Services Field Hearing in Houston Texas September 4, 2019

Good Morning. Thank you for inviting me here to speak to you about the research the National Community Reinvestment Coalition (NCRC) has done on matched pair testing in the small business arena.

NCRC is a national non-profit organization that has been in existence for over 25 years. The National Community Reinvestment Coalition and its grassroots member organizations create opportunities for people to build wealth. We work with community leaders, policymakers and financial institutions to champion fairness in banking, housing and business.

NCRC was formed in 1990 by national, regional and local organizations to increase the flow of private capital into traditionally underserved communities. NCRC has grown into an association of more than 600 community-based organizations that promote access to basic banking services, affordable housing, entrepreneurship, job creation and vibrant communities for America's working families.

Our members include community reinvestment organizations, community development corporations, local and state government agencies, faith-based institutions, community organizing and civil rights groups, minority and women-owned business associations, as well as local and social service providers from across the nation.

My name is Dedrick Asante-Muhammad and I am the Chief of Race, Wealth and Community at the National Community Reinvestment Coalition. I oversee our work on fair lending, fair housing, entrepreneurship and developing practices to address the racial wealth divide.

For over 20 years NCRC has been involved in civil rights matched-pair testing in the housing discrimination arena. NCRC has received and continues to receive funding from the U.S. Department of Housing and Urban Development (HUD) Fair Housing and Equal Opportunity division to perform rental, sales, insurance, and lending testing under the Fair Housing Act. Matched-pair testing is routinely performed not only by advocates but also by financial institutions to mitigate fair lending risks. Currently, the majority of this mystery shopping occur in the mortgage lending arena.

Chairman Green has introduced two bills (H.R. 149 and H.R. 166) during this Congressional session. Both bills would strengthen fair housing and fair lending laws by increasing the support for testing at both HUD and the Consumer Financial Protection Bureau (CFPB). Testing provides a snap shot in time of an interaction between a tester and a housing provider. It provides information that is not always possible to be collected by other methods. More specifically, testing highlights a difference in how two people are treated based solely on a protected status, such as race, national origin, or disability.

In 2017, NCRC partnered with three university professors: Dr. Jerome Williams at Rutgers North, Dr. Glenn Christensen at Brigham Young University, and Dr. Sterling Bone at Utah

State University. These three professors first published work in this area in 2010 “Rejected, Shackled, and Alone: The Impact of Systemic Restricted Choice on Minority Consumers’ Construction of Self” in *Journal of Consumer Research* the top academic journal in their field. See attachment A. This collaboration with the university professors resulted in the publishing of the academic paper “Shaping Small Business Lending Policy Through Matched-Pair Mystery Shopping” in the *Journal of Public Policy & Marketing*. See attachment B.

The “Shaping Small Business Lending Policy Through Matched-Pair Mystery Shopping” paper looked at the experience that black and white men had when they inquired about a small business loan. The paper highlights that the testing “show[s] that African American testers were asked to provide more information about their businesses and personal financials than Caucasian testers. Specifically, compared with Caucasian testers, African American testers were more frequently requested to provide information from their business financial statements, personal financial statements, the amount of their accounts receivable, and their personal W2 forms”. The service that the black tester received was poorer than the service received by the white tester.

Today, NCRC released a white paper “Disinvestment, Discouragement and Disparity in Small Business Lending”. See attachment C. To evaluate differences in small business ownership and lending opportunities, NCRC and our academic partners conducted a two-part study. First, NCRC analyzed small business ownership and lending at the national and metropolitan level in seven cities using data from the federal government. This analysis revealed that the recovery of small business lending activity in the wake of the 2008 recession has been uneven. Black and Hispanic entrepreneurs experienced almost no improvement since the crisis ended.

The areas that we examined are: Atlanta, Houston, Los Angeles, Milwaukee, the five boroughs of New York City, Philadelphia and Washington, D.C.

The data shows the following:

- There were steep declines in SBA 7(a) lending to black small business owners. This resulted in a reduction from about 8% to 3% of loans during the Great Recession, a decline that has yet to recover. There was an initial decline of lending for whites and then it recovered. For Hispanic borrowers it was stagnant.
- Business owners in wealthier areas received the largest share of loans - 85% in Milwaukee. In fact, in six of seven metro areas analyzed, more than 70% of loans went to middle- and upper-income neighborhoods.
- The number of bank branch locations declined 10% since 2009, likely affecting small businesses that are highly dependent on local-level banking relationships.
- Banks have not reinvested the increased capital accumulated after the end of the Great Recession back into small businesses. The most significant difference between deposits and loans occurred in New York, where deposits increased by 100%, but lending decreased by nearly 40%.
- There are tremendous gaps in black and Hispanic business ownership relative to their population size. Although 12.6% of the U.S. population is black, only 2.1% of small businesses with employees are black-owned. Ownership for Hispanic entrepreneurs is

slightly better at 5.6% of businesses, while they represent 16.9% of the population; White businesses are 81.6% of the total, with 62.8% of the total population.

Next, NCRC and our partners conducted a series of “mystery shopping” tests of banks in the pre-application arena to evaluate the customer service experience of prospective borrowers of different races and ethnicities in the Los Angeles metropolitan area. The data shows the following:

- Overall the customer service experience for all of the testers was poor regardless of race or national origin. However, the black and Hispanic testers experienced worse treatment compared to the white tester. A few examples are:
 - Bank personnel introduced themselves to white prospective customers 18% more frequently than they did to black prospective customers. White testers received friendlier service overall.
 - Black and Hispanic testers were requested to provide more information than their white counterparts, particularly personal income tax statements. Hispanic testers were asked to provide them nearly 32% then counterparts and black testers were asked 28% frequently than their white counterparts.
 - White testers were given significantly better information about business loan products, particularly information regarding loan fees. White testers were told about what to expect 44% more frequently than Hispanic testers and 35% more frequently than black testers.
- One area of customer service was significantly better for black and Hispanic prospective customers – they received an offer to schedule an appointment to take their application more often, which happened 18% more frequently for black testers and 12% more often for Hispanic testers.

Our results show a pattern of disinvestment and discouragement that contributes to the wide disparities in small business ownership for blacks and Hispanics in the U.S. The Federal Reserve Bank of New York in their annual small business study highlighted that 27% of Black and 21% of Hispanic business owners, with employees, reported feeling discouraged from applying for credit. This means that Black and Hispanic business owners would not apply for financing because they believed they would be turned down. This concept of discouragement is vague because it's based on subjective feelings rather than objective observations. The research that NCRC and its partners engage in provides objective measures to behaviors that, taken as a whole, discourage potential customers from applying for bank loans. When business owners don't apply for credit they stall business growth affecting all of us.

Thank you again to Chairman Green for the opportunity to highlight the NCRC's research in the small business arena and for recognizing the importance that testing has in highlighting the barriers that black and Hispanic small business owners face when trying to access credit to grow their businesses.