Testimony of Bill Himpler
for the
American Financial Services Association

Before The Subcommittee on Oversight and Investigations of
The House of Representatives Financial Services Committee

Fair Lending – Race and Gender Data in Nonmortgage Lending

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Good morning, Chairman Watt, Ranking Member Miller and Members of the Subcommittee. My name is Bill Himpler and I am Executive Vice President for Federal Affairs at the American Financial Services Association. AFSA's 350 members include consumer and commercial finance companies, auto finance companies, card issuers, mortgage lenders, industrial banks and other firms that lend to consumers and small businesses.

Mr. Chairman, I commend you and your colleagues for holding this hearing. We recognize the importance of ensuring that all persons have equal access to credit and are committed to eliminating discrimination in lending. We believe that the Equal Credit Opportunity Act and Regulation B contain the necessary restrictions and enforcement tools to end discrimination, and we do not believe that access to affordable credit will be enhanced by requiring non-mortgage creditors to collect race and gender data. To the contrary, imposing data collection obligations may decrease the credit options available or increase the cost of credit for consumers. While both the government and the industry have strived to make the credit application process as colorblind as possible, we believe the proposed requirement being discussed today goes against this goal.

## Current Obligations

Regulation B currently prohibits creditors from collecting information about an applicant's personal characteristics, including race and gender, in connection with non-mortgage credit. This prohibition ensures that the decisions in non face-to-face transactions are race neutral. For example, in the indirect finance situation, an auto finance company makes a decision about whether or not to purchase a retail installment sales contract based upon the applicant's creditworthiness, not race. The decision is race neutral because the finance company does not typically have contact with the applicant and, therefore, does not have race information. Similarly, when an applicant applies for a credit card over the telephone, online, or by mail, the creditor will not know the applicant's race or gender. These scenarios differ from the concerns that gave rise to the mandatory collection of race information in the mortgage context, where historically many applications were made in face-to-face transactions.

## Little Evidence to Suggest Discrimination

There is scant statistical evidence to demonstrate that race or gender plays a role in access to or the cost of non-mortgage credit. Rather, studies suggest credit scores and related risk factors determine access to and the cost of credit. The Federal Reserve Board conducted a study to determine the relationship between credit scores and actual credit losses and how these relationships vary for groups protected under the Equal Credit Opportunity Act.[1] The Federal Reserve Board concluded that credit scores accurately predict credit risk for the population as a whole and for all major demographic groups. The study revealed that, on average, blacks and Hispanics have lower credit scores than non-Hispanic whites and Asians.[2] This study suggests that if creditors collect data on race, the results would demonstrate a disparity in access to or pricing of credit that would be consistent with credit risk factors and not necessarily any discriminatory conduct by creditors.

Some have raised concerns about discrimination in small business lending. Small business lending presents even more complexities than consumer lending because the credit decision may be based on a multitude of factors. In assessing the risks associated with small business credit, the creditor will consider the size and type of business, as well as the business experience of the owners. In addition, the creditor will often consider each owner's credit history. There may be a mix of ownership that crosses race and gender lines. There is a very real difficulty in classifying the "race" of a small business. Given the various factors at play in small business lending, the collection of race and gender data will not explain access to and cost of credit.

## Negative Effects of Data Collection

The findings in the Federal Reserve Board's 2007 study on credit scores lead to the very important question about the value of requiring creditors to collect race and gender data. We believe that there is little value to be gained, especially in light of the significant change in the law that would be required and the massive data collection that would follow.

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[1] Report to Congress on Credit Scoring and Its Effects on the Availability and Affordability of Credit, August 2007, p. S-1.
[2] *Id* at S-2.

The Federal Reserve Board has already concluded that the benefits of voluntary collection and reporting of race and gender data would not outweigh the potential harm. In 2003, after an extensive review of approximately 600 comment letters on the issue of whether or not to lift the prohibition on collection of race and gender data on credit applications, the Federal Reserve Board decided to retain the prohibition for two primary reasons. First, collection of data that was not available before could create a risk of discrimination if it was made available. Second, the data, at least voluntarily provided data, would be of questionable reliability.[3]

If voluntary collection is unreliable, then the alternative would be mandatory data collection. From experience with HMDA reporting requirements, we know that collection and reporting requirements require tremendous time and resources. Lenders must collect, compile, organize and clean the data. They must then analyze the data to explain how any perceived discriminatory result relates to creditworthiness factors. Based on the 2007 credit score study, we would expect the data to reveal that minorities, on average, pay more for credit. Thus, there may be little additional information gained. From our experience with HMDA reporting, we also know that a mere correlation between race and pricing, without consideration of detailed creditworthiness factors, cannot tell us whether illegal discrimination has occurred.

Although collecting the data will provide little information, it will cause creditors to incur massive costs. Those costs will inevitably be passed along, at least in part, to consumers at a time when consumers and creditors alike cannot afford increases in credit costs.

Imposing a mandatory data collection requirement should be driven by evidence that there is a lack of access to credit or fairness in pricing based upon discriminatory factors. In the more than thirty years since the enactment of the Equal Credit Opportunity Act, creditors' systems for underwriting and pricing non-mortgage credit has undergone tremendous change. Today, most non-mortgage credit is underwritten and priced by creditors using objective, risk-based credit criteria, without face-to-face interaction or any information regarding the applicant's race or

[3] *See* Supplementary Information on Final Rule amending Regulation B, 68 Fed.Reg. 13144, 13148 (March 18, 2003).

other prohibited characteristics.  These race-blind decisioning systems provide the very best assurance that consumers receive credit based on objective, nondiscriminatory criteria.  It is hard to imagine that mandatory collection of racial information will improve this system.

Collection and reporting race and gender information also raises serious privacy concerns.  Both consumers and their creditors have a vital interest in protecting the privacy of consumers' personal information.  Our experience with HMDA reporting has shown that it is sometimes possible, with the addition of other public data, to identify consumers in HMDA loan registers. The collection and reporting of data for non-mortgage credit transactions significantly increases the risk that a consumer's sensitive personal information will enter the public domain.   Also, it may be that consumers will object to being asked information about their race and see this as a violation of their privacy.

**Recommendations**

We believe that the Equal Credit Opportunity Act and Regulation B protect consumers from discriminatory lending practices, and the current prohibition on data collection should be retained.  Any possible benefits to collecting these data are outweighed the potential harms and costs.  In the current financial market, there would be no substantial benefits to consumers who would share the costs incurred by creditors in such a compliance effort.  What's more, we must be careful not to undo the progress that has been made in creating a credit granting system that's race and gender neutral.

Mr. Chairman, we stand ready to work with you as needed.  I want to thank you again for inviting me to participate in this important hearing.  That concludes my statement and I would be happy to answer any questions.