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 **Deep Dive into the Section 1071 Final Rule Manual**

**Preliminary**

On March 30, 2023, the Consumer Financial Protection Bureau (CFPB) issued the small business lending rule (final rule), which implements the small business lending data collection requirements set forth in section 1071 of the Dodd-Frank Act (Section 1071).

**Background**

Section 1071 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) amends the Equal Credit Opportunity Act (ECOA) to require financial institutions to report information to the CFPB certain information about credit applications from women-owned, minority-owned, and small businesses.

In September 2020, the Bureau released an outline of proposals under consideration and alternatives considered in advance of convening a panel under the Small Business Regulatory Enforcement Fairness Act (SBREFA), in conjunction with the Office of Management and Budget and the Small Business Administration. The SBREFA panel was convened in October 2020 and received feedback from representatives of small entities on the impacts the rules the Bureau was considering to implement, Section 1071, would have on small entities likely to be directly affected by the rulemaking.

The panel’s report was completed and released in December 2020.  On October 8, 2021, a Notice of Rulemaking (NPRM) was published in the Federal Register.  The Bureau’s next action for section 1071 was the issuance of a final rule March 30, 2023.

The stated purpose of Section 1071 is to facilitate enforcement of fair lending laws and to enable communities, governmental entities, and creditors to identify the following: Business Needs and Opportunities and Community Development Needs of women owned businesses, minority owned businesses and small businesses. The CFPB has finalized this proposed rulemaking and issued the final rule, which is available at: <https://www.consumerfinance.gov/rules-policy/final-rules/small-business-lending-under-the-equal-credit-opportunity-act-regulation-b/>.

**Summary**

Section 1071 specifies several required data points and provides authority for the CFPB to require additional data points if the CFPB determines that the collection of the additional data would aid in fulfilling Section 1071’s purpose. Section 1071 also contains a number of other safeguards regarding information required to be collected, including that financial institutions restrict certain persons’ access to collected information, requirements for maintaining information, and requirements regarding publication of data.

The rule identifies who will be subject to the rule and defines those as “covered financial institutions.” The rule also defines “covered applications,” “covered credit transactions,” and “small businesses.” The result of these identifications and definitions are that essentially any entity that engages in financial activity that originated at least 100 covered originations in each of the two preceding calendar years to a business that had $5 million or less in gross annual revenue for the previous year are required to collect and report small business lending data.

**Timing**

By issuing the Final Rule on March 30, 2023, the CFPB met its March 31, 2023 deadline for issuing a final rule to implement the small business data requirements of Section 1071 of the Dodd-Frank Act. The Bureau had previously issued a Notice of Rulemaking in August 2021 and the comment period ended on January 6, 2022. The deadline date above was part of a stipulation that the CFPB agreed that which resolved litigation in a California federal district court. That lawsuit sought to force the Bureau to move forward with Section 1071 rulemaking.  The stipulation and agreement resolved the lawsuit.

**Covered Financial Institutions**

The Section 1071 requirements apply to “covered financial institutions.” A “covered financial institution” is any partnership, company, corporation, association, trust, estate, cooperative organization, or other entity that engages in any financial activity that originated at least 100 covered credit transactions to small businesses in each of the two preceding calendar years. Thus, United States banks that make loans to small businesses will be impacted by this new rule. Small businesses are those having gross annual revenues of $5 million or less during the preceding fiscal year.

There is no asset-based exemption threshold for depository institutions or any other general exemptions for particular categories of financial institutions. Institutions will need to determine annually if it is a covered institution. Non-financial institution creditors may collect and report data voluntarily in certain circumstances. Debts related to factoring, leases, consumer-designated credit cards used for business purposes, and credit secured by certain investment properties are not covered.

**Covered Originations**

For purposes of determining institutional coverage (i.e., whether a financial institution is a covered financial institution) and compliance date tier, financial institutions count covered originations. A covered origination is a covered credit transaction that the financial institution originated to a small business. Refinancings can be covered originations. However, extensions, renewals, and other amendments of existing transactions are not considered covered originations even if they increase the credit line or credit amount of the existing transaction

**Reportable Applications**

Covered financial institutions are required to collect and report data regarding covered applications from small businesses. A Covered Application is an oral or written request for a covered credit transaction that is made in accordance with the procedures and process typically used by the financial institution for the type of credit requested. This “application” definition is similar to the definition in Regulation B. However, exceptions include: (1) inquiries and prequalification requests, (2) reevaluations, extensions, or renewal requests on existing credit accounts, unless the requests seek additional credit amounts; (3) Solicitations, firm offers of credit and other evaluations initiated by the financial institution unless the small business responds to an credit offer extended by the institution. A request from a small business for refinancing is a reportable application regardless of additional amounts requested or a line increase if the request is for an extension of business credit, not otherwise excluded from coverage under the rule and is made in accordance with the procedures the financial institution uses for the type of credit requested.

**Covered Credit Transactions**

Covered Credit Transactions are an extension of credit to a small business under Regulation B. These include loans, lines of credit, credit cards, merchant cash advances and credit products used for agricultural products. Exclusions include: (1) Trade credit – a financing arrangement where a business acquires a good or service from another business without making immediate payment (2) HMDA reportable transactions (3) Insurance premium financing (typically a repayment arrangement for proceeds advanced on an insurance contract (4) Public utilities credit (3) Securities credit (4) Incidental credit but without regard to whether the credit is consumer credit, is extended by a creditor or is extended to a consumer. Additionally, certain other transactions are not included, such as factoring, leases, consumer-designated credit used for business purposes, purchases of a credit transaction, purchases of an interest in a pool of credit transactions purchases of a partial interest in a credit transaction (i.e.. loan participation agreement).

**Small Businesses**

Small business parallels, partly, the definition of the Small Business Administration’s (SBA) with regard to “small business concern.” The difference is that the 1071 rule defines a small business as a business that had $5 million or less in gross annual revenue for its preceding fiscal year as opposed to using the SBA’s existing size standards. Conversely, businesses with more than 5 million in revenue in the preceding year are not considered small businesses under the rule. Also, non-profit organizations and governmental entities are not considered small businesses under the rule. Transactions with these entities are not covered originations which negates reporting requirements from these businesses and entities.

Financial institutions are allowed to rely on applicant representations regarding gross annual revenue when determining if an entity qualifies as a small business. In cases where a financial institution verifies provided information or if an applicant provides updated information, the institution is required to use that information.

**Requirements to Collect and Report Data**

Collecting data under Section 1071 requires the collection of many additional data points on reportable applications (i.e. from small businesses). Financial institutions must collect data on a calendar-year basis and report it by June 1. Section 1071 allows financial institutions to reuse previously collected data as long as it was procured within the same calendar year as the current application. This allowance assumes the lender believes the previously collected data is accurate.

**Data Points Generated by the Financial Institution**

Data Collection and Reporting Covered financial institutions are required to compile and maintain the following data that the financial institution generates:

(1) Unique identifier – an alphanumeric identifier, starting with a unique legal entity identifier of the financial institution.

(2) Application date – the date the covered application was received by the financial institution.

(3) Application method – the means by which the applicant submitted the covered application to the financial institution (online, in-person, etc.).

(4) Application recipient – whether the applicant submitted the covered application directly or indirectly to the financial institution (or affiliate) or whether the applicant submitted the covered application indirectly to the financial institution via a third party.

(5) Action taken by the covered financial institution on the application; and

(6) Action taken date

**Date Points for Denied Reportable Applications**

There is a data point for denied reportable applications – the institution states the principal reason(s) the financial institution denied the covered application.

**Data Points for Reportable Applications Approved but not Accepted or that Result in an origination**

There are additional data points for the amount approved or originated and for pricing information. The pricing information includes, as applicable, information regarding the interest rate, total origination charges, broker fees, initial annual charges, additional cost for merchant cash advances or other sales-based financing, and prepayment penalties.

**Data Points Collected from Applicant or Third-Party Source**

This is information about the applied for credit and information about the customer’s business

* Credit type;
* Credit purpose;
* The amount applied for;
* A census tract based on an address or location provided by the applicant;
* Gross annual revenue for the applicant’s preceding fiscal year;
* A three-digit North American Industry Classification System (NAICS) code for the applicant;
* The number of people working for the applicant;
* The applicant’s time in business; and
* The number of the applicant’s principal owners.

**Data Points Collected on Demographic Information**

* The applicant’s minority-owned business status, women-owned business status, and LGBTQI+-owned business status; and
* The applicant’s principal owners’ ethnicity, race, and sex.

A covered financial institution is required to ask an applicant to provide this demographic information, and to report the demographic information solely based on the responses that the applicant provides for purposes of the final rule. However, a covered financial institution **cannot require an applicant or other person to provide this demographic information**. If the applicant fails or declines to provide the demographic information necessary to report a data point, the financial institution reports the failure or refusal to provide the information. Financial institutions are not required or permitted to report these data points based on visual observation, surname, or any other basis (including demographic information provided for other purposes).

**Discrimination Notice**

The institution must inform an applicant that the financial institution is not permitted to discriminate:

* on the basis of an applicant’s responses about its minority-owned, women-owned, or LGBTQI+-owned business status,
* on the basis of responses about any principal owner’s ethnicity, race, or sex, or
* on the basis of whether the applicant provides this information.

Covered financial institutions also must inform an applicant that the applicant is not required to answer the financial institution’s inquiry about the applicant’s minority-owned, women-owned, and LGBTQI+-owned business statuses, or the inquiries about the principal owners’ ethnicity, race, or sex.

**Sample Data Collection Form**

The final rule includes a sample data collection form that covered financial institutions can use to collect this demographic information from applicants and to provide these required notices. As illustrated in this form, covered financial institutions, generally, must collect principal owners’ ethnicity and race using aggregate categories and disaggregated subcategories. Covered financial institutions must allow applicants autonomy to describe a principal owner’s sex through free-form text or a verbal self-description.

**Discouragement**

Covered financial institutions cannot discourage applicants from responding to requests for applicant-provided data and must maintain procedures to collect applicant-provided data at a time and in a manner that are reasonably designed to obtain a response. With regard to data collected directly from an applicant, these procedures must, at a minimum, have provisions to ensure that:

* The initial request for applicant-provided data occurs prior to notifying an applicant of the final action taken on an application;
* The request for applicant-provided data is prominently displayed and presented;
* Applicants are not discouraged from responding to such requests; and
* Applicants can easily respond to such requests.

Additionally, covered financial institutions must maintain procedures to identify and respond to signs of potential discouragement, including low response rates for applicant-provided data. The final rule notes that low response rates may indicate discouragement or another failure by a covered financial institution to maintain procedures to collect applicant-provided data at a time and in a manner that are reasonably designed to obtain a response. The final rule also addresses how a covered financial institution should report certain data if, despite having such procedures in place, it is unable to obtain the data from an applicant.

**Reliance and Reuse of Data**

Covered financial institutions are permitted to rely on information provided by an applicant or appropriate third-party source, where applicable, but a covered financial institution is required to report verified information if it chooses to verify applicant-provided information.

The final rule permits the reuse of certain previously collected applicant-provided data in certain circumstances. Generally, a covered financial institution is permitted, but not required, to reuse certain previously collected applicant-provided data to satisfy the requirement to collect and report certain data points if:

* The data were collected within thirty-six months of the current covered application (except that gross annual revenue must have been collected within the same calendar year as the current covered application); and
* The financial institution has no reason to believe the data are inaccurate.

A covered financial institution that decides to reuse previously collected data to report the time in business data point must update the previously collected data to reflect the passage of time since that data was collected. A covered financial institution may only reuse previously collected demographic information—data regarding the applicant’s minority-owned, women-owned, and LGBTQI+-owned business statuses or data regarding the principal owners’ ethnicity, race, or sex—if the data were previously collected pursuant to the final rule.

**Requirements to Report Data to the CFPB and Provisions Regarding Availability and Publication of Data**

Data will be collected on a calendar year basis and reported to the Bureau by June 1 of the following year. Only one report should be submitted per origination. If more than one financial institution is involved in the origination of a covered credit transaction, the financial institution that makes the final credit decision approving the application shall report the loan as an origination. Covered financial institutions submitting data to the CFPB must provide certain identifying information about themselves as part of their submissions. The CFPB has provided a Filing Instructions Guide, which contains additional information regarding the submission of data. It is available at <https://www.consumerfinance.gov/data-research/small-business-lending/filing-instructions-guide/>.

Subject to certain modifications or deletions that the CFPB determines would advance a privacy interest, data that financial institutions submit to the CFPB will be made available to the public on an annual basis. The CFPB will determine what, if any, modifications and deletions are appropriate after it obtains a full year of data. The CFPB will announce the specific timing and method for issuing these determinations at a later date. Additionally, the CFPB anticipates that it will release higher-level, aggregate data before releasing application-level data. Any publication of aggregate data will be dependent on multiple factors, including privacy considerations, the volume of data received, and trends in the data received.

The CFPB’s publication of data will satisfy covered financial institutions’ statutory obligation to make data available to the public upon request. More specifically, the final rule provides that a covered financial institution is required to make available to the public on its website, or otherwise upon request, a statement that the covered financial institution’s small business lending application register, as modified by the CFPB, is or will be available from the CFPB. The final rule includes language that a covered financial institution could use for this statement.

**Requirements to Limit Certain Persons’ Access to Certain Data (“Firewall” provision)**

Referred to as a “firewall,” the rule restricts the access of certain individuals (underwriters, employees making a determination relating to an application, etc.) at a financial institution or its affiliates to certain race or demographic information provided by an applicant. If a bank determines that an employee “should have access” to covered information, it must provide a notice to the applicant of the underwriter’s access to such information, along with notice that the financial institution may not discriminate on the basis of such information. Alternatively, a covered financial institution can provide the notice to a broader group of applicants, up to and including all applicants.

The rule implements certain limitations on employees’ and officers’ access to certain data. The CFPB refers to this as the “firewall.” Any employee or officer of a covered financial institution or affiliate that is involved in the determination of applications are prohibited from accessing information regarding whether the applicant is a minority-owned business or a women-owned business and regarding the ethnicity, race, and sex of the applicant’s principal owners. In addition, the final rule prohibits a covered financial institution or third party from disclosing this demographic information (i.e., minority-owned, women-owned, and LGBTQI+-owned business statuses and ethnicity, race, and sex information collected pursuant to the final rule) to other parties, except in limited circumstances.

**Recordkeeping Requirements**

The rule requires financial institutions to retain evidence of compliance with this rule, including a copy of their small business lending application register and other evidence of compliance for at least three years after they are required to be submitted. Financial institutions are required to maintain, separately from the rest of the application and accompanying information, an applicant’s responses to the financial institution’s inquiries regarding whether an applicant is a minority-owned or a women-owned business, and the ethnicity, race, and sex of the applicant’s principal owners. Information should not include any name, specific address, telephone number, email address, or any personally identifiable information (PII) concerning any individual who is, or is connected with, an applicant.

**Effective and Compliance Dates**

The final rule is effective 90 days after its publication in the Federal Register. However, compliance with the final rule is not required at that time. In order to determine when it must begin complying with the final rule, a financial institution must determine which compliance date tier applies to it.

Generally, the compliance date tiers in the final rule differ depending on the number of covered originations that a financial institution originated in 2022 and 2023. Additionally, in order to be required to comply with the final rule in a given year, a financial institution must be a covered financial institution (as discussed above) for that year. Taken together, these two provisions in the final rule mean that:

* Tier 1 financial institutions must begin collecting data and otherwise complying with the final rule on October 1, 2024 if it originated at least 2,500 covered originations in both 2022 and 2023.
* Tier 2 financial institutions must begin collecting data and otherwise complying with the final rule on April 1, 2025 if it:
	+ Originated at least 500 covered originations in both 2022 and 2023;
	+ Did not originate 2,500 or more covered originations in both 2022 and 2023; and
* Tier 3 financial institutions must begin collecting data and otherwise complying with the final rule on January 1, 2026 with at least 100 covered originations in both 2022 and 2023 but not 500 or more covered originations in both 2022 and 2023.
* Also, even if it originated fewer than 100 covered originations in 2022 or 2023, a financial institution that originates at least 100 covered originations in 2024 and 2025 must collect data and comply with the final rule beginning January 1, 2026.

**Transitional Period**

Some financial institutions may not be able to readily determine if transactions originated in 2022 or early 2023 are covered originations because they don’t know if a borrower is a small business as defined in the final rule. Thus, the final rule includes a transitional provision that financial institutions may use to determine the number of covered originations they originated in 2022 and 2023. A financial institution may rely on the transitional provision to determine the number of its covered originations for 2022 and/or 2023 if it did not collect sufficient information to determine if some or all borrowers were small businesses pursuant to the final rule or if such information is not readily accessible. Such institutions may count covered originations for the last quarter of calendar year 2023 (October 1 through December 31), and then annualize the number of its covered originations based on this information. The financial institution could use this annualized number to determine its covered originations for 2022, 2023, or both years.

Financial institutions are also permitted to assume that all covered credit transactions originated during a calendar year were made to a small business for purposes of determining institutional coverage and compliance date tier pursuant to the final rule. Alternatively, the financial institution could assume that all of the covered credit transactions that it originated in 2022 and 2023 were made to a small business and, thus, are covered originations. For example, if the same financial institution originated 370 covered credit transactions in 2022, it is not required to begin collecting data or otherwise complying with the final rule before January 1, 2026.

**Safe Harbor**

The final rule also includes provisions regarding enforcement, bona fide errors, and safe harbors. It has safe harbors for certain incorrect entries of census tracts, NAICS codes, and application dates. It also has a safe harbor regarding incorrect determinations of small business status, covered credit transactions, and covered applications. For example, if a covered financial institution initially determines that an applicant for a covered credit transaction is a small business, but then later concludes the applicant is not a small business, the covered financial institution would not be in violation of ECOA or the final rule if, at the time it collected the demographic data required by the final rule, it had a reasonable basis for believing that the application was from a small business. In this situation, the covered financial institution is not required to report the application but is nonetheless required to comply with certain other provisions of the final rule in order to avail itself of this safe harbor.



Deep Dive into the Section 1071 Final Rule

FAQ: Questions

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**Question 1:**

How will Section 1071 be enforced?

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**Question 2:**

When is the final rule effective?

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**Question 3:**

Are there any retention requirements besides keeping copies of small business lending application registers and other evidence of compliance for at least three years?

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**Question 4:**

What time period of data must be reported by June 1 of each year?

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**Question 5:**

May banks use third party vendors and service provides to comply?

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Deep Dive into the Section 1071 Final Rule

FAQ: Answers

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**Answer 1:**

It appears through enforcement of existing Fair Lending and other federal laws that govern this area. The guidance states that in passing section 1071, Congress articulated two purposes for requiring the Bureau to collect data on small business credit applications and loans, one of which is to “facilitate enforcement of fair lending laws”. Although the Dodd-Frank Act does not further explain this, other Federal laws shed light on both purposes. That is, a set of existing Federal laws form the backdrop for the use of small business lending data collected and reported pursuant to section 1071 to facilitate the enforcement of fair lending laws, and to identify business and community development needs and opportunities across the United States.

**Answer 2:**

The final rule is effective 90 days after its publication in the Federal Register. However, compliance with the final rule is not required at that time. In order to determine when it must begin complying with the final rule, a financial institution must determine which compliance date tier applies to it. Generally, the compliance date tiers in the final rule differ depending on the number of covered originations that a financial institution originated in 2022 and 2023.

**Answer 3:**

Yes. The rule includes a requirement to maintain an applicant’s responses to the final rule’s required inquiries regarding an applicant’s minority-owned, women-owned, and LGBTQI+-owned business statuses and regarding principal owners’ ethnicity, race, and sex separate from the rest of the application and accompanying information.

Answer 4:

Data must be reported to the CFPB by June 1 of the year following the calendar year in which the financial institution collected the data (e.g., data collected for 2024 must be reported by June 1, 2025). Reporting banks must provide certain identifying information about themselves as part of their submissions. A Filing Instructions Guide is available here: <https://www.consumerfinance.gov/data-research/small-business-lending/filing-instructions-guide/>.

**Answer 5:**

As long as the obligations stated in the rule are met, including collecting data in a manner that does not discourage small businesses from providing it, financial institutions are free to work with third parties to assist them with their compliance obligations, whether that is with respect to data collection, maintenance or reporting