MIRADOR **Technology for Smarter Small Business Lending**

Mirador Financial ("Mirador")[1] appreciates the opportunity to respond to the OCC's paper "Supporting Responsible Innovation in the Federal Banking System: An OCC Perspective." Mirador is a Portland, Oregon based technology company who provides proprietary software to regulated banks, credit unions and CDFI's to improve the speed at which they are able to underwrite small business loans.

There is much made of small business being the backbone of the economy. The contention is one of the most frequently repeated facts about U.S. economic performance and job creation. In the case of the importance of small business to U.S. growth and job creation, the contention has the added benefit of being true. Small businesses (500 employees or less) make up 99.7 percent of U.S. employer firms and 49.2 percent of private sector employment.[2]

Mirador is dedicated to the proposition that regulated financial services companies want to serve small businesses in their communities. However, due to a confluence of occurrences and competition from those who do not have to contend with federal regulation, loans below a certain dollar amount have become unprofitable. According to the Joint Small Business Credit Survey Report of 2014, it takes an average of 24 hours to ***apply*** for credit, and only 33% of applications resulted in full funding.[3] The results are plain to see: in 2014, one out of five small business applicants applied first with an online lender[4], and it is reasonable to expect that number to grow. Mirador's product enables our customers to make smaller loans profitable once again, increase profitability for larger loans, improve the customer experience for borrowers, and utilize supplemental underwriting techniques and data sources to help more lenders "get to yes" for qualified small businesses.

On April 7, 2016 Comptroller Curry delivered an important speech in Las Vegas, Nevada. His speech was really the first by any financial services regulator to address the emerging challenges for regulators, examiners, bankers and customers posed by financial services innovation. He asserted "…regulated banks aren't the only game in town when it comes to financial services and your competitors are taking advantage of every opportunity to get a leg up on you." Certainly, the Comptroller's point that unregulated entities can and do use the lack of regulatory requirements and regulatory cost to effectively compete against banks – and there is no shortage of options for borrowers – is a new reality. But the Comptroller also went on to

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[1] https://www.miradorlending.com/about-us

[2] *U.S. Census Bureau, SUSB, CPS; International Trade Administration; Bureau of Labor Statistics, BED; Advocacy-funded research,* Small Business GDP: Update 2002- 2010, **www.sba.gov/advocacy/7540/42371**

[3] "Joint Small Business Credit Survey Report, 2014. Federal Reserve Banks of New York, Atlanta, Cleveland and Philadelphia. Respondent Demographics section.

[4] IBID. Executive Summary.

remind the audience that customers can and should “take comfort” in buying their financial products and services from the regulated community. So the central question is how banks, operating under a comprehensive regulatory regime, can compete with a host of emerging marketplace lenders who are either lightly regulated or unregulated all together, and who have found out over time that many small business borrowers are willing to pay higher rates in exchange for increased “speed to funding” and decreased onerous paperwork requirements. In other words, how can bank regulators like the OCC meet their safety and soundness mandate while fostering the types of innovation that will allow banks to compete with non-bank financials not just on rate, but also on speed and process?

We are pleased that the OCC is taking a lead role in examining how innovation is driving evolution in the market place and we look forward to being part of an ongoing dialog with the OCC and all functional regulators as you examine these issues.

1. What challenges do community banks face with regard to emerging technology and financial innovation?

Community banks choose to work with Mirador because we offer a cost-effective technology solution that can sharply reduce underwriting costs with no degradation in underwriting accuracy. Our community bank customers are not satisfied that small businesses in and around their reach are finding it easier to work with marketplace lenders who can fund loans quickly even at the expense of lower rates. We partner with community banks and other regulated lenders of all sizes to bring traditional, safe and sound products to small business in a way that takes many of the best elements of marketplace lending (speed, paperwork reduction, and ease of use) and applies them to banking.

It is unlikely that most community banks would have the expertise or funding to develop their own software solution and to create the seamless digital experience consumers are coming to expect, so working with third party service providers to enhance core business functions makes sense.

2. How can the OCC facilitate responsible innovation by institutions of all sizes?

A top concerns for most innovators and partnering institutions is regulatory uncertainty. For any institution to invest in new products and services, they need to know that these new technologies will not create regulatory vulnerabilities.

The OCC should consider creating an office, task force, working group or advisory committee which exists not as a “one-off” forum, but an ongoing venue for dialog about developments in technology. Just as information security is dynamic and changing, so too are other areas of technological innovation. Indeed, the one thing that seems certain is that customer will continue to demand innovation in the ways they obtain and execute financial products and services.

It is clear from the white paper and Comptroller Curry’s recent remarks that the OCC is well aware of the pace of innovation and we expect that a continuous two-way discussion will supplement important guidance like that governing policies and procedures around third party vendors.

Finally, providing third party providers with reliable "no action" letters would go a long way in encouraging community banks, especially very small banks, to accept new technology and processes. As a third party provider, removing the question of how the examiners will react to the use of products will save a lot of time and money, allowing the technology and innovation to be offered at lower prices, expanding access to smaller institutions.

In May, the Financial Conduct Authority (FCA) in the United Kingdom initiated their "Innovation Sandbox." An essential component of this effort is no-action/no-enforcement letters. The UK example is not a perfect blueprint as it applies mostly to non-tested innovation. However, it does recognize that limiting a bank's exposure to regulatory enforcement that is the result of responsible and considered efforts to innovate can be an important tool fostering innovation and driving bank adoption.

In our view, in order for a NAL program to be valuable, the application process should not be needlessly burdensome, and the no-action protections should be meaningful and certain as opposed to limited in scope and subject to modification at any time by the issuing authority.

Finally, we suggest the OCC (and other prudential regulators) consider updating the Community Reinvestment Act to encourage further lending to small businesses. Specifically, the OCC should consider providing (partial) CRA credit to institutions that refer small business customers they are not able to lend to directly to another responsible lending institution (such as a CDFI) that can successfully fund a loan application.

In our experience, because of their technical assistance and business model, many CDFI's have been able to say "yes" to prospective borrowers that could not meet the requirements of a community banks. In addition, we know that CDFI's are able to save borrowers a substantial amount in interest and fees over many of the on-line products. For this reason, banks that refer would-be customers to CDFIs or other regulated institutions should be eligible to receive some CRA credit when that referral results in a funded loan. There is precedent for this action; in 2007, the prudential regulators jointly published examples of various arrangements for low and moderate income borrowers to help the transition from high-interest mortgages to more affordable products. The various workout arrangements would be eligible for favorable CRA consideration.[5]

3. How can the OCC enhance its process for monitoring and assessing innovation within the federal banking system?

OCC employees – including field examiners – should be encouraged to engage with technology companies that are interacting with banks in a way that fosters dialog and education. If the OCC creates the structure to provide this education, the agency will have more control over what innovative products and procedures are in use at your regulated facilities. We have participated in symposiums organized by the FDIC's Western Region and found them to be extremely useful. In the absence of a more comprehensive consultative process (which could take some time to stand up), we strongly encourage the OCC to continue outreach through regional offices to

[5] Board of Governors of the Federal Reserve System, U.S. Department of Housing and Urban Development, FDIC, NCUA, OCC, OTS, "Federal Regulators Encourage Institutions to Work with Mortgage Borrowers Who are Unable to Make Their Payments," press release, April 17, 2007.

learn about available technology and become familiar with various technology providers outside of an examination context.

4. How would establishing a centralized office of innovation within the OCC facilitate more open, timely, and ongoing dialogue regarding opportunities for responsible innovation?

If the office is constructed in a way that facilitates dialog, we believe it can have a profound effect on the application(s) of innovation on traditional banking. While formal guidance like OCC Bulletin 2013-29 (Third-Party Relationships) is both comprehensive and helpful for banks and technology companies, it is not reasonable to expect that a static guidance document can keep pace with innovation. Some forum for open dialog would be helpful. When institutions know someone is available as a resource and an office exists to answer questions, they are more likely to engage. Without a centralized office of innovation, it is not clear who is involved in the conversations and institutions are more likely to engage in the activity without seeking guidance from the beginning.

5. How could the OCC provide guidance to nonbank innovators regarding its expectations for banks' interactions and partnerships with such companies?

OCC Bulletin 2013-29 is a useful document and it is unclear that any additional formal guidance is needed. We stress that what would be more useful is the creation of a process and venue for an ongoing dialog. Perhaps the venue would be an Office of Innovation; and the process could be regular (quarterly) meetings or listening sessions set to a particular agency-directed agenda.

Third-party providers want to offer innovation that the bank regulators are comfortable seeing their regulated institutions adopt, and most providers would be more than happy to make changes and adjustments in their products and processes to ensure this comfort level. However, those discussions need to take place on a regular basis outside of the normal bank examination process.

6. What additional tools and resources would help community bankers incorporate innovation into their strategic planning processes?

While we are not prepared to offer concrete suggestions on specific regulatory tools, it is clear that innovation is occurring on multiple fronts. Some questions posed by bankers and regulators are directly tied to operational risk associated with innovation (i.e. due diligence, security, redundancy) while others explore more esoteric questions around innovation (i.e. the use of "alternative" data for underwriting and policies and procedures around lead generation and referrals). While the exiting guidance will continue to stand on it's own as a way to consider operational risk, strategic planning is an iterative, living process and so too should be the evaluation of new technologies. It is difficult to imagine a single static guidance keeping up with the pace of innovation.

Additionally, we suggest the OCC provide semi-regular bulletins that describe the behavior, needs and challenges of small business borrowers. The Federal Reserve Banks regularly publish information on SME lending and the SBA has obvious insights into he marketplace. The OCC should consider publishing a summary of the ecosystem in which SMEs and lenders interact. Doing so could spur innovation with government inadvertently acting in ways that pick winners and losers.

7. What additional guidance could support responsible innovation? How could the OCC revise existing guidance to promote responsible innovation?

We suggest the OCC engage in a dynamic fact-finding process based on a dialog with willing innovators to ascertain if and the extent to which existing guidance should be updated or additional guidance is needed.

8. What forms of outreach and information sharing venues are the most effective?

Because we are not an OCC regulated institution, we cannot speak to venues most effective for communication directly to the banks. However, as a third-party provider creating working groups and publishing reports based on the groups' work could be very effective.

9. What should the OCC consider with respect to innovation?

Innovation can come in many different forms and not all innovation may be in the long-term best interest of banks or bank customers. However it is clear that many banks are unable to deliver loans at a suitable speed to many in the market. Our technology is focused on that particular problem.

Whatever market events led to the credit crunch and put traditional bank loans outside of the reach of small business are slowly thawing. And the market place has proven beyond any doubt that if banks cannot deliver loans to small businesses at competitive rates and speeds, that consumer will exercise their options with a myriad other market participants.

We believe in bank lending and we believe that technology can be leveraged to keep it a viable source of small business funding. We would note, however, that if a regulatory pendulum swings to far, too fast in a particular direction, borrowers will vote with their feet and the hope that borrowers will "take comfort" in borrowing from a regulated bank will be reduced to a quaint notion. Regulatory efforts focused on financial services innovation – particularly as it applies to lending – should be the product of clearly identified goals and a stakeholder process that involves the full array of interested parties. We stand ready to participate fully in any process the OCC creates.

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