TESTIMONY OF EVERETT K. SANDS, CEO OF LENDISTRY
TO THE HOUSE SMALL BUSINESS COMMITTEE

"Unleashing Main Street's Potential: Examining Avenues to Capital Access"

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I. Executive Summary

It is a truth universally acknowledged that small businesses are the powerhouses of their local communities. When small businesses grow and thrive, they elevate the people who live and work around them. When they fail, the number one reason is lack of capital. Specifically, the Main Street businesses that power our economy need small-dollar loans to grow to the next level.

My message today is that, right now, there is an army of lenders who stand ready to deploy the capital needed to unleash Main Street. These lenders have proven themselves to be the most effective capital deployers for underserved communities, yet they work with one hand tied behind their backs due to hurdles that made sense when they were first enacted, but no longer fit today's finance landscape. The lenders I'm talking about are Community Development Financial Institutions (CDFIs). Disparity in access to capital on responsible terms is a critical hurdle for small businesses, both in powering the nation's economic and jobs recovery, and in narrowing the racial wealth gap. In order to do our part to unleash Main Street, we need you to unleash us.

To summarize the specific recommendations that I discuss in greater detail below, I propose that policymakers:

1. Fix the state-by-state licensing model that prevents CDFIs from efficiently serving small businesses on a nationwide footprint
2. Increase access to the Federal Reserve Bank and Federal Home Loans Bank to facilitate more small-dollar loans that Main Street businesses need in their growth stages and cannot access from traditional banks
3. Form a task force to analyze programs in an ongoing basis to make sure they remain catalytic and responsive

II. Introduction

Committee Chairman Williams, Ranking Member Velasquez, Vice Chairman Luetkemeyer, Vice Ranking Member Phillips and distinguished members of the Committee, thank you for calling a hearing on Unleashing Main Street's Potential, and for your interest in my perspectives and insights on this topic.

My name is Everett K. Sands, and I am honored to be invited back to offer testimony before this committee. I have more than 20 years of experience in lending at community banks, one of the largest national banks, and at the only fintech Community Development Financial Institution, Lendistry. As founder and CEO of Lendistry, I have focused on innovating and executing alternatives to traditional financing to support the underserved small businesses that frequently fall through the gaps, particularly those owned by minorities, women, veterans, and people in rural areas.

To date, our grant and loan programs have provided over 630,000 small businesses with nearly $10 billion in capital. More than 60% of Lendistry's outstanding principal loan balance is with minority and women-owned borrowers, more than 70% is with underserved small businesses, and 60% is with low- or moderate-income borrowers. Lendistry was the #8 PPP lender in the country in 2021, ranked above large banks like Wells Fargo. All this is to assure you that, while my team and I never claim to have found the final solution, we have made significant progress in reaching the communities that need capital and lack experience with the application process.

Lendistry is a minority-led fintech CDFI and Community Development Entity (CDE), and a member of the Federal Home Loan Bank of San Francisco. Women and minorities comprise a significant majority of Lendistry's management team. Lendistry is a proud signatory of the Small Business Borrowers' Bill of Rights, guidelines set by The Responsible Business Lending Coalition.

Since launching in 2015, Lendistry has sought to use fintech—and partnerships with financial institutions, non-profits, and government organizations—to help solve the problem of disparities in access to capital, to open doors that were previously closed to small businesses owned by minorities, women, and veterans, businesses located in rural areas, or businesses whose financing needs to take the next step in their development are just too small for traditional banks.

As a hybrid of a fintech lender and community bank with roots in traditional banking, Lendistry combines the best of fintech—efficiency, scalability, and seamless user experience—with the best of traditional lending—low cost of acquisition, low cost of funds, and strong risk management—and all with an unwavering commitment to responsible credit culture and expanding access to small business funding.

Our proprietary technology and online application portal enable a faster and more widely accessible lending process for small business borrowers. Since I last addressed this committee, we have improved our processes to provide conventional loans in as little as five days, and SBA 7(a) loans in as little as 14 days. I'll pause there a moment—as an SBA preferred lender and fintech, we are funding SBA 7(a) loans, which traditionally take up to 90 days to process, in as little as two weeks

III. An Army of Lenders Stand Ready: State of Small Business Capital Needs Post-Pandemic

The capital access landscape many small businesses traversed before and since the pandemic resembles a desert, where the lifeblood of responsibly-priced capital is scarce. Worse, it is a desert that is made almost impossibly steep by the prevalence of predatory lenders that have filled a void left by two decades of bank consolidation. The small businesses that tend to be most affected by these arduous conditions are those owned by minorities, women, and veterans; those located in rural areas; and those which, regardless of their ownership demographics, have capital requirements that are simply too small to be profitably served by traditional banks, whose median asset size ballooned by more than 500% between 2000 and 2019.[1]

The economic relief efforts in response to COVID have provided ample evidence that dramatic actions to increase the availability of capital will only benefit these underserved small businesses if the capital is connected to effective conduits that are willing and able to reach them. While traditional banks are very effective in deploying very large amounts of capital, their operational incentive is to do so through as few separate underwritings as are prudent from a risk management perspective, resulting in a very large average loan size. This logic also bears out in Federal Reserve survey data regarding the businesses that traditional banks tend to establish relationships with. Minority-owned businesses—which are disproportionately small businesses—are much less likely than other businesses to have banking relationships.[2] Thus, well-intended measures that push more capital to traditional banks can have the effect of incentivizing banks to make larger loans, as we saw with the original version of PPP, or can result in vast amounts of available capital simply going untapped, as we saw occur with the original version of the Main Street Lending Program.

Congress responded to the economic threat posed by COVID in bold and historic ways, and while there is more that can be done, entrepreneurs always look ahead, and I want to focus today on enduring solutions for small business capital access. The response to the pandemic shone a bright light on what works when it comes to financing underserved communities.

The good news is that the small business COVID relief effort also has validated that CDFIs are effective conduits for deploying capital to small businesses, and that when systemic hurdles are cleared for CDFIs, the accessibility of responsibly-priced capital improves for small businesses generally, and for underserved small business especially. For example, using PPP loan size as a rough indicator for the relative size of businesses, according to SBA data for the 2021 PPP program, the overall average loan size was $45,000, the average size of loans originated by banks was $62,000, and the average size of loans originated by CDFIs was less than $27,000. Likewise, according to SBA data for the 2020 PPP program, the overall average loan size was $101,000, the average size of loans originated by banks was $141,000, and the average size of loans originated by CDFIs and Minority Depository Institutions together was about $74,000.

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[1] Most banks simply are too large to efficiently make small loans. Twenty years of bank consolidation has cut the number of FDIC-chartered banks in the U.S. by 45%. According to FDIC data, there were 8,315 FDIC-insured banks in 2000, compared to 4,519 in 2019, with just 32 new FDIC-insured bank charters issued since 2010. As a result, the median asset size of remaining banks has grown by more than 500%, from $751 million in 2000 to $3.9 billion in 2019.

[2] Federal Reserve Banks, 2019 Small Business Credit Survey and 2020 Report on Employer Firms. Fewer than 1 in 4 Black owned businesses with employees and fewer than 1 in 3 Latinx-owned businesses with employees had received funding from a bank in the prior five years, compared with nearly half of white-owned firms with employees. Moreover, just 1 in 10 Back-owned sole proprietorships or independent contractors – which comprise a disproportionate share of all Black-owned businesses – had a recent borrowing relationship with a bank, compared with 1 in 4 white-owned non-employer businesses.

Paradoxically, this time of upheaval and uncertainty was an inspiring time for entrepreneurs. Nearly ten million new businesses were formed in 2020 and 2021, according to the U.S. Census Bureau.[3] The nearly 4.4 million new businesses formed in 2020 was more than 50 percent higher than the average annual number of new businesses formed between 2010 and 2019.[4] In fact, 2020's new business formation figure was a record, but it stood for just one year before it was far surpassed by the 5.4 million new businesses formed in 2021.[5]

Furthermore, a raft of data reveals how significant a role minority and women entrepreneurs have played in the recent new business formation activity[6][7][8], building on their already-strong pre-pandemic entrepreneurial representation.[9] It is urgent that policymakers and large enterprises alike recognize the implications of these trends. It means minorities and women will be increasingly impacted by policies around small business and capital access.

Emerging from the pandemic, we have learned that the need for access to responsible loans in smaller amounts is essential for the new businesses I've described to grow out of the early stages, evolving from employing only their founders, to employing and empowering their communities as job creators. The demand for loans in small amounts is clear. In 2023, 77% of SBA 7(a) loans were under $500,000. This amounts to a quarter of all 7(a) dollars approved. To dial down further, 27% of 7(a) loans in 2023 were under $50,000. [10] In 2021, over 80% of SBA microloan applicants ($50K and under) were in underserved communities as defined by SBA. Of these microloans, 50% went to minority-owned businesses and 48% went to women-owned businesses.[11]

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[3] "New Startups Break Record in 2021: Unpacking the Numbers," Daniel Newman and Kenan Fikri for Economic Innovation Group, January 19, 2022. https://eig.org/news/new-start-ups-break-record-in-2021-unpacking-thenumbers

[4] "Entrepreneurs Started Businesses in Record Numbers During the Pandemic," Brett Grossfeld for Salesforce.com's The 360 Blog, June 29, 2021. https://www.salesforce.com/blog/small-business-pandemicentrepreneurs/

[5] D. Newman and K. Fikri

[6] "Black Business Owners Are Up 38% from Pre-Covid Levels," Michael Sasso, *Bloomberg*, September 15, 2021. https://www.bloomberg.com/news/articles/2021-09-15/black-business-owners-are-up-38-in-u-s-from-pre-covidlevels?sref=2gRlZMND

[7] "Black-owned businesses took a pandemic hit, but they're doing better than ever now – largely because of Black women," Jason Lalljee, *Insider*, February 7, 2022. https://www.businessinsider.com/black-women-businesses-fuelincrease-pandemic-hit-entrepreneurship-covid-2022-2

[8] "Black women are the fastest growing group of entrepreneurs. But the job isn't easy," Elana Dure, J.P. Morgan Chase, October 21, 2021. https://www.chase.com/personal/investments/learning-and-insights/article/blackwomen-are-the-fastest-growing-group-of-entrepreneurs-but-the-job-isnt

[9] "Black Entrepreneurship Represents Highest Rate in U.S.," Bryan Lipiner, Global Enterpreneurship Monitor, August 13, 2020. https://entrepreneurship.babson.edu/gem-data-black-entrepreneurship-us/

[10] NAGGL, https://cdn.ymaws.com/www.naggl.org/resource/resmgr/gross_loans_fy23/09_30_23.pdf

[11] "Evaluation of Microloan Program Outcomes," SBA, November 2021, https://www.sba.gov/sites/default/files/2022-01/Evaluation%20of%20Microloan%20Program%20Outcomes%20Final%20Reportv2_508v4.pdf

According to the Intuit QuickBooks Small Business Index's Annual Report, access to financing is harder to obtain for new businesses and those owned by women or underrepresented racial groups. Small businesses owned by underrepresented racial groups are twice as likely to say "getting funding" is their #1 challenge. 72% of men who own small businesses say they can get funding over the next 12 months but among women, this drops to 64%[12]. In my experience, continued access to nonbank fintech credit is key for small businesses, particularly those who tend to need smaller dollar loans.

My recommendations today are directly related to empowering CDFIs to effectively lend in smaller amounts and serve the businesses Congress aims to unleash.

IV. Unleashing CDFIs: Universal Licensing for a Nationwide Footprint

The anachronistic state-by-state licensing requirement for CDFIs not only limits how quickly capital can be distributed but also how effective the CDFI designation can be as a force for deploying responsible capital in lower loan amounts.

What a business owner sees:

A single mom in Maryland has a sole proprietor business, the most common business structure in the U.S. She needs a loan for $12,000 to market her business and make sure she has the kind of digital presence her customers expect. Bank loans start in the millions, and she needs some technical assistance with the application, so she applies at a CDFI. Her credit is solid, and with some help she has presented all the documents she needs to apply. But she finds that no CDFI can help her.

What happened at the CDFI:

The customer has strong credit and her cashflow looks like she can repay the loan. There's one big problem: Maryland's commercial lending laws set the commercial loan minimum at $15,000 unless the business is a corporation. In order to serve this business owner and others like her and help them grow, the CDFI has to apply for a separate license to offer personal loans. This is a long and costly process the CDFI's team hasn't had the bandwidth to pursue.

Recommendation: CDFIs should be exempt from state-by-state licensing requirements, thereby bringing about three clear benefits:

1. CDFIs can move much faster to deploy capital where it's needed
2. CDFIs can more easily attain the risk management benefits of geographic diversification

[12] Intuit QuickBooks Small Business Index Annual Report 2023, October 6, 2023, https://quickbooks.intuit.com/r/small-business-data/index-annual-report-2023/?cid=pr_TOF_QBB_press-release_US_EN_SMBIndex_AR

3. Many more lenders would be motivated to attain CDFI designation, which would have the effect of significantly increasing the supply of capital provided on responsible terms and, through market forces, make predatory lending businesses less economically viable

The Nationwide Mortgage Licensing System has already proven that this can be done!

V. Unleashing Lenders: Increase access to FRB and FHLB for CDFIs

The current market environment has provided two handicaps for CDFIs, lack of liquidity due to a tightening of banks' credit parameters and higher interest rates affecting the affordability of loans.

What the business owner sees:

A local grocery store in Austin, TX wants to expand its hours to accommodate the working schedules of its local customer base. The owner needs $50,000 to hire more employees for the added shifts. This will also increase their revenue by bringing in new customers who need to do their shopping early in the morning or late at night. He goes to a CDFI for the loan. The process is going well, but when he gets the offer, the interest rate is much higher than he can afford.

What happened at the CDFI:

As the loan officer worked with the finance team to determine the offered rate, they took several factors into account.

1. The Wall Street Journal Prime rate that sets the base for all small business loans, currently 8.5%
2. The customer's risk profile, which tells them this customer is in the middle range of likelihood to pay the loan back in full
3. The operational cost associated with processing and servicing the loan
4. The cost of the capital it will use to support the loan, which it borrowed from a bank partner and pays back at Prime

The CDFI does not have low-cost sources of liquidity, and has not received adequate lending capital from banks, so it has to make the decision to either leverage higher-cost capital, or not provide the loan to the business owner. Likewise, on a small amount like $50,000, the interest rate the customer can afford is simply not financially feasible for the lender to stay in business, let alone grow and innovate. With heavy hearts, the leadership decides to raise their loan minimum or charge higher interest rates on the small dollar loans.

Recommendation: In addition to state-by-state licensing discussed in the previous section, CDFIs should get access to the Federal Reserve Bank and expanded access to the Federal Home Loan Bank. Here are the benefits:

1. With additional sources of liquidity, CDFIs can provide additional lending to underserved and undercapitalized communities as seen with the PPPLF loans provided by FRB to CDFIs
2. Access to lower costs of funding will immediately decrease the interest rates CDFIs provide to their customers
3. Today, the Federal Home Loan Bank does not allow CDFIs to pledge small business loans. This should be immediately changed.

In combination with blended rates made possible by state loan guarantees and State Small Business Credit Initiative (SSBCI) support, this recommended system would be a game changer for CDFIs and their borrowers.[13]

VI. Government Capital: Catalytic, Responsive & Engaged

As evidenced by PPP, SSBCI and the many programs implemented to provide pandemic relief, our government can rise to the occasion to deploy assistance and save small businesses. From the capital deployer's perspective, government support is at its best when it's:

- Catalytic – Tuned into helping new industries, like renewable energy, thrive and innovate
- Responsive – Considerate of current market conditions, like inflation
- Engaged – Built with processes in place for reporting, and adjusting based on reporting

Though public programs geared to Socially and Economically Disadvantaged Individuals (SEDIs) exist for the purposes of deploying allocated capital to institutions, both to support lending activities and to support technical assistance for borrowers, no system currently exists for adjusting after measuring and reporting on the effectiveness of the administration such programs in relation to their missions. This means that, though a great deal of money is pushed toward states to support small businesses, there is no system in place to make sure they continue to fit market conditions. Instead of adjusting current programs to keep them effective, new programs are formed to meet new needs.

Recommendation: Require development and implementation of a reporting system to measure the performance, annual progress, and market adaptations of public agencies and entities responsible for administering capital deployment programs that are geared to SEDIs, covering allocations for investments, lending and technical assistance (e.g., financing for licensing and

[13] Blended rates allow CDFIs to vary their capital sources. I'll use the State Small Business Credit Initiative (SSBCI) as an example. So, let's say that $50,000 loan is for a business in a state whose SSBCI program will guarantee half the loan amount at 1%. This greatly decreases the lender's need to rely on the bank's capital, which it has to pay back at Prime, and even with a lower rate, the CDFI can offer a lower rate AND turn more of a profit to grow and serve more businesses.

certifications, bonding, financial empowerment tools, HR services, cybersecurity, marketing, mobile-readiness).

VII. Conclusion

Congress has taken great strides in recent years to increase access to capital for borrowers and remove roadblocks for our most effective lenders, CDFIs. For mission-led lenders, part of the end game is disrupting predatory lenders by offering accessible, responsible alternatives. In my experience, knowledge and innovation are at their most powerful when paired with execution. It is my hope that from the information gathered in this room from myself and my fellow witnesses, swift action will follow. Only then can Main Street's potential truly be unleashed.