January 4, 2023

Submitted online at https://www.regulations.gov/document/SBA-2022-0013-0001

Dianna Seaborn
Director, Office of Financial Assistance
Office of Capital Access
Small Business Administration
409 3rd Street SW
Washington, DC 20416

Re: Small Business Lending Company Moratorium Rescission and Removal of the Requirement for a Loan Authorization – RIN 3245-AH92

Dear Madam:

We are writing in response to the Proposed Rulemaking (RIN 3245-AH92) proposing to lift the moratorium on licensing new Small Business Lending Companies (SBLCs) and add a new type of entity called a Mission-Based SBLC.

About Upstart

Upstart is the leading artificial intelligence ("AI") lending marketplace, which is designed to improve access to convenient and affordable credit while reducing the risk and costs of lending for our bank and credit union partners. By leveraging Upstart's AI marketplace, which harnesses over 1,000 data points that go beyond a traditional credit score, Upstart-powered banks and credit unions of all sizes can offer higher approval rates and experience lower loss rates. Those banks and credit unions are able to simultaneously expand access to credit and deliver the exceptional digital-first lending experience their customers' demand, the same experience that 7(a) small business customers deserve. Upstart has helped its bank and credit union partners serve over 2.5 million customers, originating over $30.5 billion in loans while fully automating 75% of those loans.[1]

Lending is centuries old, but has changed little in recent decades. Traditional lenders use simple FICO-based credit scoring models to decide who is approved for credit and at what interest rate. While simple and intuitive, these "scorecard" methods are limited in their ability to quantify risk. Four in five Americans have never defaulted on a credit product, yet less than half have access to

[1] As of 9/30/2022. Fully Automated metric is calculated on a quarterly basis.

prime credit.[2] The implication is eye-opening. With a smarter credit model, such as the AI-based methods developed by Upstart, banks and credit unions approve almost twice as many borrowers at generally lower interest rates and with fewer defaults.

Upstart is one of the first companies to apply AI to the multi-trillion-dollar credit industry by using non-conventional variables at scale to provide superior loan performance and improve consumers' access to credit. We currently work with our bank and credit union partners to help them originate small business (SMB) loans, personal loans (e.g., loans that are used for consolidation of high-cost credit card debt, cover wedding expenses, fund home improvements, or pay for large or unexpected medical costs), auto refinance loans, and other small dollar loans.

Results from an internal access to credit comparison demonstrate the ability of our approach to expand access to credit in a financially safe and sound manner. The Upstart model approves 43.4% more borrowers than traditional credit-score only models and yields 43.2% lower average APRs for approved loans.[3] The Upstart model approves 43% more Black borrowers than a traditional model, while offering those customers APRs that are 23.8% lower than a traditional credit-score driven lending model.[4] Similarly, the Upstart model approves 45.6% more Hispanic borrowers than a traditional credit-score model while offering APRs that are 25% lower than a traditional model.[5] As a result of its innovative approach to underwriting, Upstart is uniquely positioned to help our bank and credit union partners meet the credit needs of their entire communities, particularly low-to moderate-income ("LMI") communities and communities of color.

Generally, all financial institutions, but the largest banks, face challenges in building advanced credit underwriting models in-house. Small and intermediate-sized banks with more limited resources are especially disadvantaged given the resource-intensive nature of building and managing such technology. While many fintech companies have decided to compete with banks or become a bank themselves through either a charter application or acquisition of a bank, Upstart has chosen the decidedly different path of partnering with banks and credit unions to help them better serve their customers. Upstart provides the technology to banks and credit unions that allows them to offer fully digital experiences across multiple small business and consumer lending products. Importantly, Upstart's marketplace allows financial institutions of all sizes to launch and maintain top-rated digital lending experiences without a substantial investment in technology and personnel that would be out of reach for all but the largest banks.

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[2] According to an Upstart retrospective study completed in December 2019.

[3] As of December 31, 2021, and based on a comparison between the Upstart model and a traditional credit-score only model. The APR calculation compares the two models based on the average APR offered to borrowers up to the same approval rate. The hypothetical credit score only model used in Upstart's analysis was developed in connection with the CFPB No Action Letter access to credit testing program and was built from a traditional credit score only model trained on Upstart platform data. APR for the scorecard was averaged for each given traditional credit score grouping.

[4] As of December 31, 2021, and based on a comparison between the Upstart model and a traditional credit-score only model. Upstart does not collect demographic data on borrowers. Upstart uses standard industry methodology to estimate borrower demographic status to conduct access-to-credit analysis comparing Upstart to traditional credit model outcomes.

[5] As of December 31, 2021, and based on a comparison between the Upstart model and a traditional credit score only model. Upstart does not collect demographic data on borrowers. Upstart uses standard industry methodology to estimate borrower demographic status to conduct access-to-credit analysis comparing Upstart to traditional credit model outcomes.

Upstart launched a small business term loan product in the summer of 2022 that provides loans of up to $200,000 in one and two year terms. To date, we have facilitated with a lending partner tens of millions in loan origination volume to small businesses across the country with an average APR that is one-third less than the market average for similar products. These SMB loans are mostly used for working capital, expansion, inventory, business refinancing and payroll.

SBLC Moratorium Rescission

Upstart supports the SBA's proposal to lift the moratorium on licensing new SBLCs and their proposal to create a new type of Mission-Based SBLC. The SBLC moratorium has been in place since January 1982 and the number of licensed SBLCs has remained stagnant at 14. As a result, a lender would need to purchase a license from an existing license holder and likely acquire an existing lender's business and portfolio to offer 7(a) loans nationally. This has effectively created a situation that some have compared to a "taxi-cab medallion" of 7(a) lending licenses. Some argue that the SBLC licenses only add value to the holder of the license and have created a virtual monopoly over the $36 billion a year government-guaranteed lending market for the last 40 years.

If the SBA wants to expand access to 7(a) loans for small businesses in underserved communities, it must increase the number of SBLCs. If the SBA wants to expand access to 7(a) loans in a cost-efficient and streamlined manner, we believe the SBA should leverage responsible and vetted fintechs that provide online small business loans and have proven themselves in their ability to reach underserved communities by welcoming them into the program.

Traditional financial institutions have left small businesses behind in tough economic times, when small businesses needed them the most. A 2020 CFPB report examined banking trends in small business lending from pre-Great Recession (2004-2007), through the Great Recession (2008-2009), and then through the post-Great Recession (2010-2017) period. The study revealed that, by 2017, small business lending from banks had not returned to pre-Great Recession levels and, in fact, had only recovered to just half of the lending levels of 2004.[6] This left a void and fintechs stepped in to provide capital to needy small businesses. A 2022 Federal Reserve Small Business Credit Survey (SBCS) of employer small businesses found that compared to 2020, applicants were more likely to apply at an online lender/fintech and less likely to apply at a small bank in 2021.[7] In 2019, the SBCS found a growing number of small businesses apply to online lender/fintechs when seeking credit—rising from 19% in 2016 to 32% in 2018, indicating the increasing importance of the online lending market.[8]

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[6] "Data Point: Small Business Lending and the Great Recession," Consumer Financial Protection Bureau. https://files.consumerfinance.gov/f/documents/cfpb_data-point_small-business-lending-great-recession.pdf

[7] See "Small Business Credit Survey: 2022 Report on Employer Firms," at https://www.fedsmallbusiness.org/survey/2022/report-on-employer-firms

[8] See "Small Business Credit Survey: 2019 Report on Employer Firms", 2019 at www.fedsmallbusiness.org/medialibrary/fedsmallbusiness/files/2019/sbcs-employer-firms-report.pdf. Within this report online lenders encapsulate a wide variety of nonbank online-based sources "including retail/payments processors, peer-to-peer lenders, merchant cash advance lenders, and direct lenders.

Lifting the moratorium will provide the SBA the flexibility to respond to market conditions while balancing its oversight capacity, thus increasing the number of SBLCs to improve capital access for small businesses. Finally, lifting the moratorium should not be interpreted as advocating for the weakening or lessening of regulatory requirements regarding the oversight of new licensees, which we believe the proposed rule does not. In fact, we believe new SBLC licensees should be held to the same regulatory and compliance requirements that have governed all SBA non-federally regulated lenders and the existing fourteen SBLC licensees for the last 40 plus years.

Thank you for the opportunity to comment. If you have any questions, please contact Gilberto Soria Mendoza (gilberto.mendoza@upstart.com) or Nat Hoopes (nat.hoopes@upstart.com).

Sincerely,

Nathaniel Hoopes
VP - Head of Government and
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