

FACT SHEET: MARKET & POLICY ISSUES IN THE USE OF CASH-FLOW DATA FOR UNDERWRITING CREDIT

Resolving Data Transfer Issues Could Facilitate Use of Cash-Flow Data, with Particular Opportunity to Expand Access to Credit for Millions of Underserved Consumers and Small Businesses

As digital information has exploded in the past 15 years, the U.S. financial sector has accelerated its search for “alternative” or “non-traditional” data to strengthen credit underwriting. One of the most promising sources is cash-flow information—particularly data from deposit and prepaid accounts—because it can provide a more detailed and timely picture of how applicants manage their finances than traditional credit reports.

This information could be vital for millions of consumers and small businesses that struggle to access affordable credit because of information barriers. Approximately 20 percent of U.S. consumers lack sufficient traditional credit history to predict their repayment risk using traditional scoring models. Millions of small businesses also struggle to access credit because they have not yet built financial track records. And even for more established applicants, the data can potentially help lenders better differentiate risks, particularly when evaluating borrowers with non-prime credit scores.

These developments suggest that widescale adoption of cash-flow data in credit underwriting could produce substantial benefits for borrowers and lenders alike, most notably by expanding access to credit, improving risk prediction and lender efficiency, and enhancing competition and innovation. Yet while cash-flow data appears to have substantial potential for increasing access to credit among underserved populations, its use is primarily concentrated among fintech lenders in U.S. credit markets today.

FinRegLab’s new report, *The Use of Cash-Flow Data in Underwriting Credit: Market Context & Policy Analysis*, analyzes the market and policy issues that will determine whether and when cash-flow underwriting can reach scale and options for managing data access, privacy, and consumer protection needs as use of the data expands and evolves. A Policy Overview summary can be found [here](#), and the full report will be available [here](#).

The report finds that competition, coordination, and compliance issues are limiting cash-flow adoption and its potential to improve borrowers’ access to credit. While industry efforts on some issues are already underway, deeper engagement by both private stakeholders and public policymakers is necessary for reaching scale. Key insights include:

- **Cash-flow data underwriting holds substantial promise.** While the data’s most obvious use in underwriting is to evaluate consumers and businesses that lack traditional credit history, the report suggests that the information adds meaningful predictive power for a substantially broader swath of applicants. The data could be particularly important for increasing access to credit for African American and Hispanic populations, though it is not likely to close all gaps in credit availability and use between demographic groups.
- **Yet there are critical challenges to adoption.** Whether and when cash-flow underwriting can reach scale will depend largely on the extent to which: (1) lenders are able to secure reliable data access; and (2) banks and investors determine that the information is sufficiently useful to warrant changes to their business processes. Although market developments are reducing some operational hurdles, competitive dynamics and coordination challenges are affecting both issues. And open questions

with regard to regulatory compliance and liability issues are creating substantial uncertainty in affected markets.

- **Emerging risks also warrant attention.** While the increasing use of cash-flow data in credit underwriting is providing benefits for consumers and small businesses, it also raises privacy tradeoffs and potential concerns about fairness, accuracy, data security, and transparency. These issues are not limited to loan origination, but also can arise in connection with loan servicing and firms' re-use of cash-flow data for other commercial purposes. Although some positive developments are occurring, uncertainty about the application of existing laws and inconsistency among market actors could become an increasing source of risk as the market continues to expand and evolve.
- **Industry and policy action are warranted now to ensure cash-flow data is able to achieve its potential to foster a more inclusive, efficient, and competitive marketplace.** Constructive action by industry, regulators, and Congress may each be needed to improve outcomes with regard to both cash-flow underwriting and the broader data transfer system.

The report analyzes both current initiatives and future options for action, including accelerating the adoption of safer and more efficient data transfer technologies, developing data processes and tools to foster meaningful customer control over their information, clarifying and strengthening existing customer protections, and increasing supervision of non-bank actors.

In the near term, increased engagement by federal regulators through research, monitoring, and interpretive activities could be particularly useful, in part by providing sharper focus and greater certainty to initiatives by industry and Congress. Addressing market challenges and customer protection issues in the underlying data transfer system in the next few years could be particularly helpful by setting the stage for more rapid expansion of cash-flow underwriting in years to come. These issues are potentially important to helping beneficial practices reach scale and to reducing risks to both borrowers and firms.

The Market Context & Policy Analysis report is the third in a series on the use of cash-flow data in credit underwriting by FinRegLab. The first [Empirical Research Findings report](#) summarizes the results of an independent analysis by FinRegLab in conjunction with Charles River Associates of loan data from a range of non-bank financial services providers —Accion, Brigit, Kabbage, LendUp, Oportun, and Petal— that have begun using cash-flow variables and scores in an effort to provide unsecured credit to consumers and small businesses who may have difficulty obtaining loans from traditional sources. The analysis evaluated the data with regard to its general predictiveness, its ability to increase access to credit, and its potential fair lending effects.

The second [Small Business Spotlight](#) detailed the increasing use of electronic cash-flow data in small business credit markets, which has allowed lenders to engage in faster, more sophisticated, and more consistent analysis than relying on paper records. The report tracked how use of cash-flow data has spread among both traditional lenders and new entrants and noted issues that could affect its further expansion.

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