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Inside

An Overview of Community Development Financial Institutions

By Anna Alvarez Boyd, Senior Associate Director, Division of Consumer and Community Affairs, Board of Governors of the Federal Reserve System, and Charlene Van Dijk, Senior Community Economic Development Advisor, Federal Reserve Bank of Atlanta

The economic impacts of the COVID-19 pandemic and the subsequent recovery response underscore the importance of Community Development Financial Institutions (CDFIs) in responding to the financial needs of historically underserved consumers and borrowers in times of crisis.[1] In a recent conversation, Calvin Holmes, president of the Chicago Community Loan Fund, a Chicago-based CDFI, described CDFIs as "financial first responders, who run into the face of danger to triage and treat those who need it most." To build on the allegory further, this article identifies the "financial triage centers," probes how they operate, examines several new tools in CDFIs' "first aid kits," and diagnoses challenges CDFIs face in ensuring the "capillaries" of our nation's financial system channel credit and capital to low- and moderate-income (LMI) communities and communities of color.[2]

WHAT IS A CDFI?

At the simplest level, a CDFI is a private financial institution whose mission is to provide financial products and services, along with training and technical assistance, to underserved communities, including LMI consumers, communities of color, women, or minority groups who can experience challenges accessing credit. CDFIs deliver financial community assets in disinvested places, whether they are rural, urban, suburban, or otherwise. CDFIs exist to help grow local economies, provide affordable housing, and support small minority-owned businesses. CDFIs offer a creative solution to counterbalance harmful practices such as redlining, a historical practice that continues to have implications for the racial wealth divide in the U.S.[3] The U.S. Department of the Treasury administers the CDFI Fund, to which certified CDFIs can apply for certain types of financial benefits.[4]

Common uses of CDFI loans include financing affordable housing developments, commercial real estate, small businesses, community centers, nonprofit and religious institutions that provide community benefits, and health-care centers. As of September 2021, 1,390 CDFIs were certified, and all 50 states and several U.S. territories have at least one certified CDFI.[5]

The 1994 Riegle Community Development and Regulatory Improvement Act[6] established the Community Development Financial Institutions Fund. This law defined the requirements for organizations to attain CDFI status and increased access to federal resources through the congressional appropriations process to support organizations that fill gaps in financing for economically disadvantaged communities. Subsequent congressional legislation such as the 2009 American Recovery and Reinvestment Act, the 2010 JOBS Act, and the 2021 American Rescue Plan Act established additional conduits through which the CDFI

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The Bureau's Final Rule Under Regulation Z to Address LIBOR's Sunset

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On December 7, 2021, the Consumer Financial Protection Bureau (Bureau) issued a final rule under Regulation Z to address the sunset of the London Interbank Offered Rate (LIBOR) on consumer credit cards, home equity lines of credit (HELOCs), and closed-end, variable-rate loans using LIBOR as a reference rate.[1] The rule generally became effective on April 1, 2022, although compliance with some provisions is not required until later dates. This article summarizes the rule.

BACKGROUND

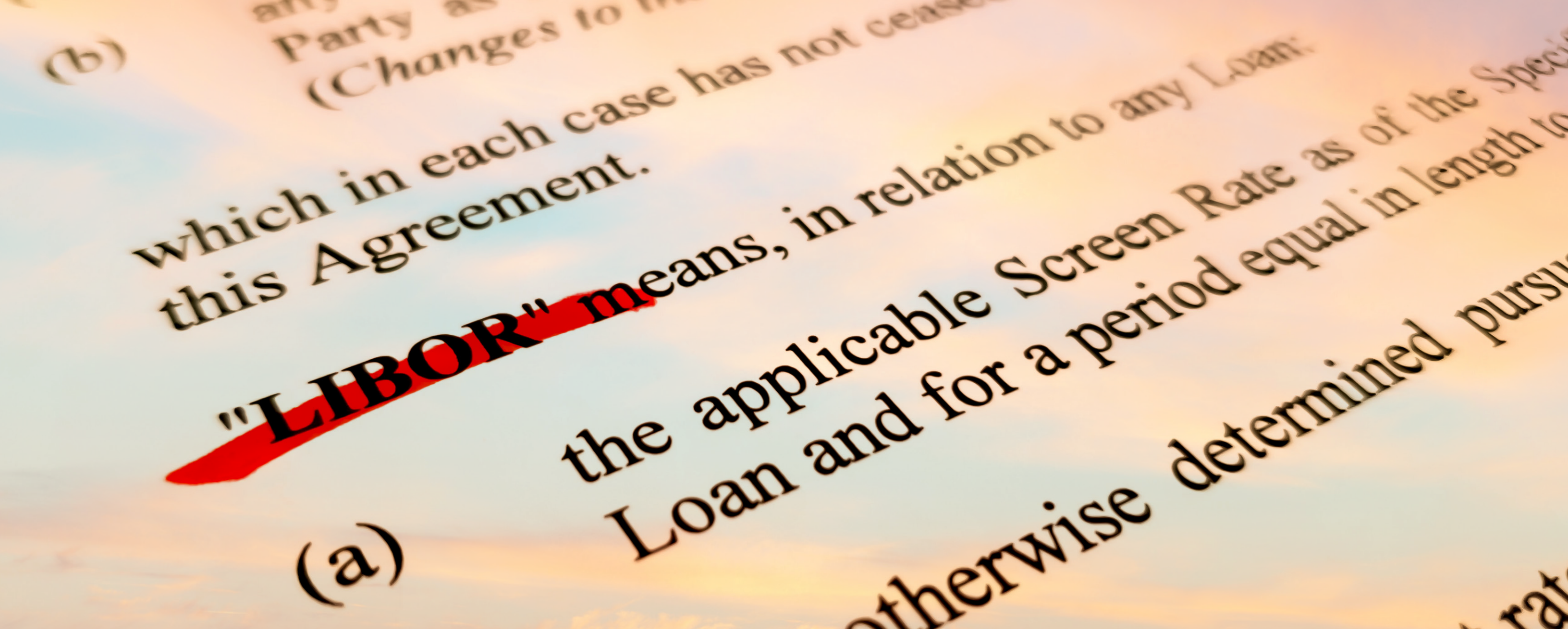
LIBOR, which is calculated "by polling more than a dozen large global banks in London about the interest rate at which they can borrow for various lengths of time ('tenors') in U.S. dollars and four other currencies,"[2] is a key benchmark in many variable-rate, consumer credit products, including closed-end mortgages, HELOCs, reverse mortgages, credit cards, and student loans. The Congressional Research Service estimates that LIBOR was referenced in approximately $223 trillion of financial instruments as of 2020.[3]

LIBOR's future came into question in 2012 when a scandal revealed that some of the panel banks were manipulating their LIBOR submissions for financial gain and to mask their financial condition during the financial crisis.[4] In response, the Financial Stability Board issued a report in 2014 titled *Reforming Major Interest Rate Benchmarks* that recommended transitioning from LIBOR to alternative benchmarks.[5] In November 2020, the ICE Benchmark Administration, LIBOR's administrator, announced its intention to consult with the Financial Conduct Authority, LIBOR's regulator, on ending LIBOR after December 31, 2021, for the one-week and two-month U.S. dollar (USD) tenors, and after June 30, 2023, for the remaining overnight, one-month, three-month, six-month, and 12-month USD tenors.[6] The ICE LIBOR® Feedback Statement on Consultation on Potential Cessation, in explaining the different expiration dates, noted that the one-week and two-month tenors are not as widely used as the remaining tenors.[7]

SECURED OVERNIGHT FINANCING RATE (SOFR)

In 2014, as regulators explored alternatives to LIBOR, the Federal Reserve Board (Board) and the Federal Reserve Bank of New York (FRBNY) jointly convened the Alternative Reference Rates Committee (ARRC), with the goals of identifying and implementing risk-free alternative rates for the USD LIBOR.[8] In 2017, the ARRC announced the Secured Overnight Financing Rate (SOFR) as an alternative benchmark, which broadly measures the cost of borrowing cash overnight collateralized by Treasury securities and is published daily on the FRBNY's website.[9]

In November 2020, the Board, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation (agencies) encouraged supervised institutions to stop entering into new contracts that use LIBOR as a reference rate as soon as practicable and in any event by December 31, 2021. The guidance also recommended that financial instruments entered into before December 31, 2021, should either use a reference rate other than LIBOR or have



robust fallback language with a clearly defined alternative reference rate after LIBOR is discontinued.[10] In October 2021, the agencies issued additional supervisory guidance to facilitate the transition from LIBOR.[11]

Against this backdrop of supervisory guidance for creditors to phase out LIBOR in their financial instruments, the Bureau's final rule provides the framework under Regulation Z for implementing this change for consumer credit. The rule primarily addresses 1) replacement indexes for variable-rate products, 2) change-in-terms notices (CITN), and 3) reevaluations of credit card rate increases.

REPLACEMENT INDEXES

HELOCs and Credit Cards

The Bureau's final rule generally provides HELOC creditors and credit card issuers with the option of 1) waiting until the LIBOR indexes specified in their instruments are no longer available, or 2) to begin transitioning from the LIBOR index to a replacement index on or after April 1, 2022. Currently, Regulation Z only permits an index change for these products when the original index is no longer available.[12] The final rule thus provides flexibility to creditors seeking to replace LIBOR before it is no longer available.

For both credit cards and HELOCs, if the creditor replaces the LIBOR index before it becomes unavailable, the replacement index must meet the following standards:

- Historical fluctuations in the LIBOR index and replacement index are substantially similar.[13]
- The replacement index and replacement margin produce an annual percentage rate (APR) substantially similar to the APR based on adding the LIBOR index in effect on October 18, 2021, to the account's existing margin.[14]

The commentary includes this example to illustrate a HELOC that uses a replacement index and replacement margin that result in an APR substantially similar to the rate calculated using the LIBOR index:

> Assume a variable rate used under the plan that is based on the 1-month U.S. Dollar LIBOR index and assume that LIBOR becomes unavailable after June 30, 2023. On October 18, 2021, the LIBOR index value is 2%, the margin on that day is 10% and the annual percentage rate using that index value and margin is 12%. Assume on January 1, 2022, a creditor provides a change-in-terms notice under §1026.9(c)(1) disclosing a new margin of 12% for the variable rate pursuant to a written agreement under §1026.40(f)(3)(iii), and this change in the margin becomes effective on January 1, 2022, pursuant to §1026.9(c)(1). Assume that there are no more changes in the margin that is used in calculating the variable rate prior to April 1, 2022, the date on which the creditor provides a change-in-terms notice under §1026.9(c)(1), disclosing the replacement index and replacement margin for the variable rate that will be effective on April 17, 2022. In this case, the margin that applied to the variable rate immediately prior to the replacement of the LIBOR index used under the plan is 12%. Assume that the creditor has selected the prime index published in the *Wall Street Journal* as the replacement index, and the value of the prime index is 5% on October 18, 2021. *A replacement margin of 9% is permissible under §1026.40(f)(3)(ii)(B) because that replacement margin combined with the prime index value of 5% on October 18, 2021, will produce an annual percentage rate of 14%, which is substantially similar to the 14% annual percentage rate calculated using the LIBOR index value in effect on October 18, 2021, (which is 2%) and the margin that applied*

to the variable rate immediately prior to the replacement of the LIBOR index used under the plan (which is 12%). (Emphasis added).[15]

What If the Creditor Waits Until the LIBOR Index Is No Longer Available?

In that circumstance, the replacement index must have historical fluctuations substantially similar to the original index. In addition, the replacement index and margin must result in an APR substantially similar to the APR in effect before the original index "became unavailable."[16] But the regulation does not define when an index is no longer available.

What If the Replacement Index Has No Rate History?

A new replacement index with no rate history generally can be used if its value on October 18, 2021, plus its replacement margin, will produce an APR substantially similar to the APR under the LIBOR index in effect on October 18, 2021, or the next calendar day if the replacement index is not available on October 18.[17]

Safe Harbor

To facilitate compliance, the final rule provides a safe harbor to replace the LIBOR index for HELOCs and credit cards with either the prime rate published in the *Wall Street Journal* or the SOFR, provided certain other requirements are satisfied.[18]

REFINANCING OF A CLOSED-END VARIABLE RATE LOAN

For closed-end variable-rate loans, a change in the index could constitute a refinancing under §1026.20(a), which would trigger new Regulation Z disclosures and certain other requirements.[19] A refinancing occurs if the replacement index is not comparable with the existing index.[20] Comment 20(a)-3.iv lists the relevant factors to determine if the new index is comparable, including (but not limited to) whether:

- the movements over time are comparable;
- the consumers' payments using the replacement index compared with payments using the LIBOR index are comparable if there is sufficient data for this analysis;
- the index levels are comparable;
- the replacement index is publicly available; and
- the replacement index is outside the control of the creditor.

The comment also notes that "these determinations may need to consider certain aspects of the historical data itself for a particular replacement index, such as whether the replacement index is a backward-looking rate (e.g., historical average of rates) such that timing aspects of the data may need to be adjusted to match up with the particular forward-looking LIBOR term-rate being replaced."

Safe Harbor

The commentary includes a safe harbor for replacing the index of a variable-rate loan with a USD LIBOR index for a one-month, three-month, or six-month tenor.[21] The Bureau did not include the LIBOR one-year tenor because ARCC has not yet released the corresponding SOFR. "Once the Bureau knows which SOFR-based spread adjusted index the ARRC will recommend to replace the one-year USD LIBOR index for consumer products, the Bureau may determine whether that index meets the 'comparable' standard based on information available at that time."[22]

CHANGE-IN-TERMS NOTICE

Regulation Z requires advance notices for certain changes to open-end consumer credit agreements.[23] The final rule addresses how this provision applies to HELOCs and credit cards transitioning from LIBOR to a replacement index.

Credit Cards

Creditors for open-end, nonhome secured credit generally must provide a CITN for certain changes at least 45 days prior to the change.[24] The final rule clarifies that when a card issuer changes the reference index, it must disclose the new index as well as the margin 45 days prior to the change, regardless of whether the new index or the margin increases or decreases the finance or other charges.[25]

CITN Credit Card Formatting Requirements

The notice must be in a tabular format that discloses:

- the amount of the new rate based on the new index;
- that it can vary; and
- how it is determined.[26]

In addition, if the rate with the replacement index will increase when the CITN is provided, a creditor must disclose the new periodic rate and APR calculated using the replacement index.[27]

HELOCs

A CITN is required whenever any term required to be disclosed under §1026.6(a) is changed, or the required minimum periodic payment is increased, at least 15 days prior to the effective date of the change.[28] Under the final rule, creditors must provide notice of the index replacement, as well as any change in the margin.[29] Regulation Z currently does not require a CITN if a change reduces the finance charge or any other charge. The final rule amends this to require a CITN when an index is replaced, even if the margin decreases.[30] The format requirements for the CITN described previously for credit cards do not apply to HELOCs.[31]

CREDIT CARD RATE REEVALUATION REQUIREMENTS

Regulation Z generally requires that if a card issuer increases a consumer's rate, it must evaluate the increase at least every six months to see if the consumer qualifies for a lower rate.[32] The final rule provides this requirement will not apply if the rate increased because a LIBOR index was replaced in accordance with the rule. Rate increases effective prior to the replacement of a LIBOR index are not covered by this exception.[33]

CONCLUSION

As affected creditors begin the process of transitioning from the LIBOR index for their variable-rate consumer credit agreements to a replacement index, the Bureau's final rule, and accompanying resources, provide a detailed roadmap and framework to implement these changes. Specific issues and questions should be raised with your primary regulator. ■

Endnotes*

1 See 86 *Federal Register* 69716 (December 8, 2021).

2 See "The LIBOR Transition," Congressional Research Service (December 15, 2021).

3 See "The LIBOR Transition," p. 1.

4 See "The LIBOR Transition," p. 1.

5 See *Reforming Major Interest Rate Benchmarks,* Financial Stability Board (July 22, 2014).

6 See "ICE Benchmark Administration to Consult on Its Intention to Cease the Publication of One Week and Two Month USD LIBOR Settings at End-December 2021, and the Remaining USD LIBOR Settings at End-June 2023", (November 30, 2020).

7 See ICE LIBOR Feedback Statement on Consultation on Potential Cessation, ICE Benchmark Administration, March 5, 2021.

8 See ARCC.

9 See "Secured Overnight Financing Rate Data," Federal Reserve Bank of New York. The ARCC website provides additional information about SOFR.

10 See SR 20-27: Interagency Statement on LIBOR Transition (November 30, 2020).

11 See SR 21-17 / CA 21-15: Interagency Statement on Managing the LIBOR Transition (October 22, 2021).

12 See 12 C.F.R. §1026.40(f)(3)(ii)(A) for HELOCs and §1026.55(b)(7)(i) for credit cards.

13 Comments 40(f)(3)(ii)(B)-1.iii and 55(b)(7)(ii)-1.iii address the factors to determine whether a replacement index has historical fluctuations substantially similar to a LIBOR index, for HELOCs and credit cards, respectively.

14 See 12 C.F.R. §1026.40(f)(3)(ii)(B) and commentary for HELOCs, and §1026.55(b)(7)(ii) and commentary for credit cards.

15 See Comment 40(f)(3)(ii)(B)-2.i.

16 See 12 C.F.R. §1026.40(f)(3)(ii)(A) for HELOCs and 12 C.F.R. §1026.55(b)(7)(i) for credit cards.

17 See 12 C.F.R. §1026.40(f)(3)(ii)(A) for HELOCs and 12 C.F.R. §1026.55(b)(7)(ii) for credit cards.

18 See Comments 40(f)(3)(ii)(B)-1 for HELOCs and 55(b)(7)(i)-1 for credit cards.

19 See 12 C.F.R. §1026.20(a).

20 See Comment 20(a)-3.ii.B.

21 See Comment 20(a)-3.ii.B.

22 See 86 *Federal Register* at 69730.

23 See 12 C.F.R. §1026.9(c).

24 See 12 C.F.R. §1026.9(c)(2). An exception applies to the 45-day period if the consumer agrees to the change. See 12 C.F.R. §1026.9(c)(2)(i)(A).

25 See 86 *Federal Register* at 69725 (codified at 12 C.F.R. §1026.9(c)(2)(v)(A)) and Comment 9(c)(2)(v)-14. The Bureau also clarified while notices are generally not required for rate changes to a variable rate loan based on an index not under the creditor's control, that exception does not apply here because the index is being *replaced*. 86 *Federal Register* at 69725.

26 See 86 *Federal Register* at 69725.

27 See 86 *Federal Register* at 69725.

28 See 12 C.F.R. §1026.9(c)(1)(i). If the consumer consents to the change, the notice must still be provided, but can be delivered as late as the effective date. Comment 9(c)(1)(i)-3.

29 See Comment 9(c)(1)(ii)-3.

30 See 12 C.F.R. §1026.9(c)(1)(ii) and Comment 9(c)(1)(ii)-3.

31 Regulation Z imposes one set of CITN requirements for HELOCs at 12 C.F.R. §1026.9(c)(1) and a different set of requirements for nonhome secured, open-end credit at §1026.9(c)(2). The specific CITN formatting requirements for nonhome secured credit CITNs at §1026.9(c)(2)(iv)(D) are not required for HELOCs. The Board issued a rulemaking proposal for HELOCs in 2009, when it still had general rulemaking authority for Regulation Z, that included tabular format requirements for certain HELOC CITNs. 74 *Federal Register* 43428, 43542 (August 26, 2009). However, in 2011, the Board announced it would not proceed with this proposal because of the transfer of rulemaking authority to the Bureau.

32 See 12 C.F.R. §1026.59.

33 See 12 C.F.R. §1026.59(h)(3).

*Note: The links for the references listed in the Endnotes are available on the *Consumer Compliance Outlook* website at consumercomplianceoutlook.org.

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An Overview of Community Development Financial Institutions

Fund can provide federal funding to reach deeper into communities where access to credit and capital remain a barrier to economic growth.

More broadly, certified CDFIs can be separated into two groups: 1) depository CDFIs that consist of banks, thrifts, depository institutions, and credit unions, including Minority Depository Institutions (MDIs); and 2) nondepository CDFIs, many of which are not-for-profit loan funds, and venture capital funds (**Figure 1**). In terms of total portfolio amounts, in 2020, depository CDFIs held 83.6 percent of the CDFI industry's loan dollar value and composed about 50 percent of the industry, while loan funds largely comprised the other half of the industry.[7] The Treasury Department annually reviews certified CDFIs to ensure their business model still meets the congressionally mandated CDFI requirements.[8]

HOW CDFIs OPERATE

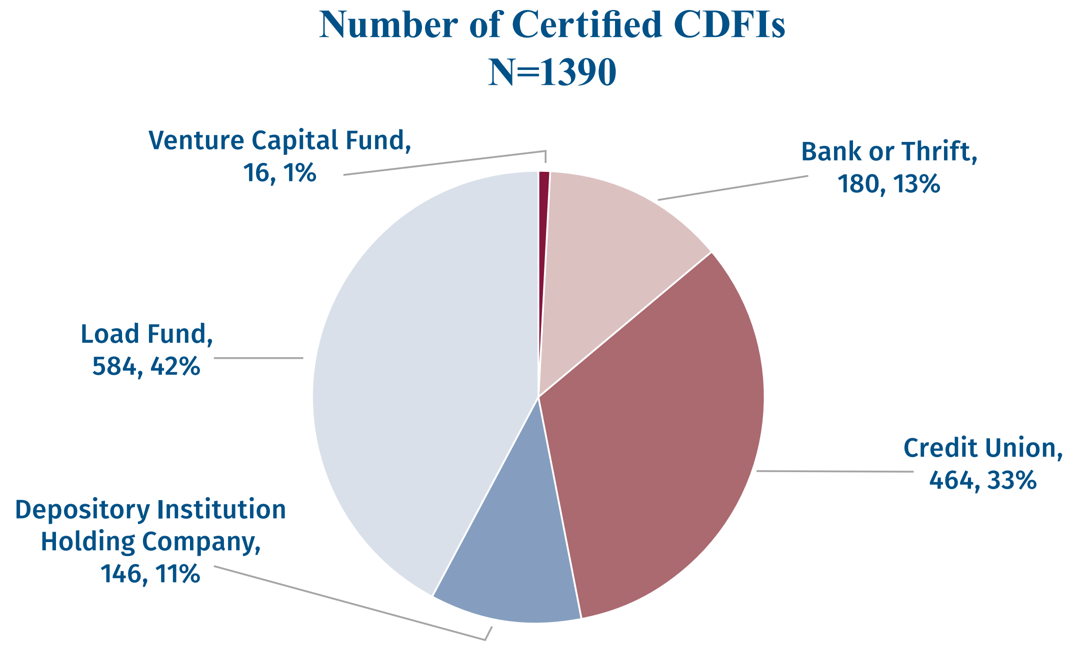
Business Model

At its core, the business model of a CDFI is to lend money, while having a socioeconomic return for an identified community with location-based or identity-related characteristics.[9] CDFIs must obtain capital to pay for the loans they disburse to clients, along with the salaries and operations that help underwrite and service loans, as well as provide technical assistance to clients. The specialization of CDFIs lies in their ability to acquire and blend various forms of capital so they can make loans that others will not or cannot.

One key source of capital for certified CDFIs is the CDFI Fund, which considers applications for grants, loans, and, in some cases, equity from the CDFI Fund and other federal programs, many of which use CDFI certification as a preliminary requirement to access funds.[10] The need for alternative access to credit and capital in LMI and minority communities exceeds taxpayer funding provided through the congressional appropriations process. As a result, CDFIs use these funds to leverage private capital. For example, the interest rates and fees nonprofit loan fund CDFIs charge are designed to be affordable for economically distressed clients but are typically not enough to cover the entire cost of lending operations.[11] CDFIs must therefore rely on other earned income, grant donations, fundraising, equity investments, debt instruments, and — in the case of CDFI banks and credit unions — deposits to support their business models.

In addition to the aforementioned CDFI certification provided by the Treasury Department and its affiliated funding programs for certified CDFIs, numerous federal agencies and others administer programs that provide capital, technical support, or research for CDFIs, including the Board of

Figure 1: CDFIs by the Numbers



Source: CDFI Fund Certification Data, CDFI_Cert_List_02_14_2022_Final.xlsx (live.com) (02/14/2022)

Governors of the Federal Reserve System, Small Business Administration, Department of Housing and Urban Development, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, National Credit Union Administration, Department of Agriculture, and private entities, including banks through the CRA. Some corporations and foundations also have resources available for CDFIs.[12]

CDFIs' Role in Financial Inclusion

CDFIs, CRA-motivated banks, philanthropies, and private investors help comprise what CDFI practitioners call the "community development finance ecosystem."[13] Entities, community members, and other nonprofits and small businesses operate symbiotically within this community development finance ecosystem. CDFI loans and investments support catalytic community assets that help to grow local economies, revitalize disinvested places, and uplift downtrodden communities with legacies of racial exclusion.

These typically hyperlocal, mission-driven financial institutions play a key role in improving financial and economic inclusion, especially in challenging times. While recent data on the industry's performance as a whole are limited because of the nonprofit status of half the industry and a lag in CDFI Fund reporting requirements, we know from the Great Recession that CDFIs concentrate their lending activity in census tracts with signs of distress such as high poverty or unemployment rates, even more so than conventional lenders.[14, 15] Further, based on call reports and other public information about subsets of the CDFI industry, we know that many, if not most, CDFIs have historically maintained charge-off rates comparable to traditional depository institutions, all while serving clients that other lenders deem too risky.[16]

By creatively blending federal, private, philanthropic, and state and local funding, community-based lenders develop a diversified stack of capital to cushion more risk-averse funders from losses, while stretching and leveraging dollars further than one source of capital alone would have provided. This stitching together of different kinds of capital to fund community investments is where CDFIs adroitly blend different funding sources based on investors' risk tolerance to create viable financial transactions (**Figure 2**).[17]

All of these resources together help support a healthy ecosystem of financial services available to individuals and households along the financial inclusion spectrum. As the COVID-19 pandemic reemphasized, researchers continually demonstrate that low- and moderate-income communities, communities of color, and women have a harder time accessing capital from traditional financial institutions overall.[18]

CDFIs and the Community Reinvestment Act

CDFIs also obtain private sector funding when banks make or participate in loans, provide investments, or deliver services such as technical assistance and training. Many of these activities are eligible for consideration under the Community Reinvestment Act (CRA), provided they are conducted in a safe and sound manner.

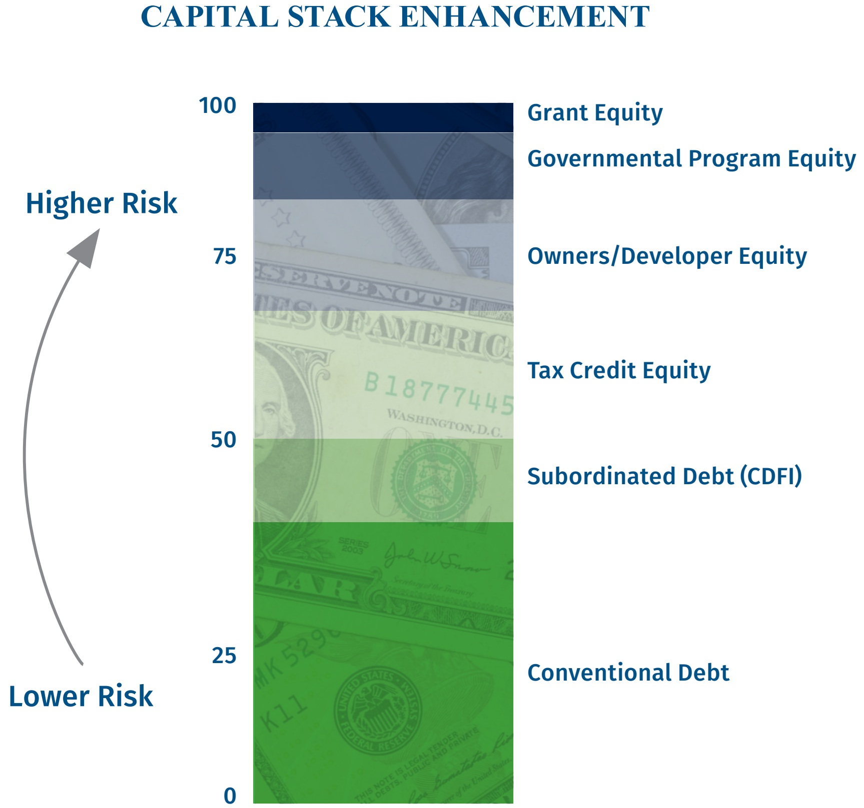
Several of the 2016 Interagency CRA Q&As specifically address CRA consideration for certain loans, services, and investments in CDFIs:

- "§__.12(g)(3)—1: 'Community development' includes activities that promote economic development by financing businesses or farms that meet certain size eligibility standards. The agencies will presume that any loan or service to or investment in a … CDFI that finances small businesses or small farms, promotes economic development."
- "§__.12(h)—1: Examples of community development "loans include, but are not limited to, loans to … financial intermediaries including CDFIs."
- "§__.12(t)—4: Examples of qualified investments include, but are not limited to, investments, grants, deposits, or shares in or to financial intermediaries (including CDFIs …) that primarily lend or facilitate lending in low- and moderate-income areas or to low- and moderate-income individuals in order to promote community development, such as a CDFI that promotes economic development on an Indian reservation."

Other activities related to CDFIs may qualify for CRA consideration. For example, Q&A §__.12(i)—3 discusses qualifying community development services that include providing technical assistance to a community development organization, such as a CDFI. The examples in this Q&A include:

- serving on a loan review committee;
- developing loan application and underwriting standards;
- developing loan-processing systems;
- assisting in marketing financial services;
- providing financial services training to staff;
- helping with fundraising; providing bookkeeping services; and
- providing services reflecting financial institution employees' areas of expertise at the institution, such as information technology and legal services.

Figure 2: Blending Funding Sources Based on Risk Tolerance



Source: CRAtoday

A Variety of Instruments

Within the realm of CDFIs, entities can obtain designations, apart from their depository or nondepository status or for-profit or nonprofit status, that help to attract specific types of funding that can be used to develop unique capital stacks for diverse and distinct financing transactions.

For example, one CDFI segment focuses exclusively on supporting Native American communities across the country. These Native American CDFIs provide essential capital in some of the most historically disinvested parts of our nation with the highest unemployment and poverty rates and the greatest need for alternative sources of capital.[19]

Because MDIs are generally chartered to lend and provide services to underserved communities, they typically satisfy the standards of a certified CDFI. An *MDI* is defined in the Financial Institutions Reform, Recovery and Enforcement Act of 1989 as a "depository institution where 51 percent or more of the stock is owned by one or more 'socially and economically disadvantaged individuals.'"[20]

Not all MDIs are CDFIs, however, and only those MDIs that apply for CDFI certification from the Treasury Department can tout their status as both types of entities. Currently, there are 144 MDIs, 32 of which are also CDFIs.[21]

CDFI Companions

Several of the CDFI Fund's programs exist to support entities that are not necessarily certified CDFIs but have similar missions and purposes to certified CDFIs. For example, the Capital Magnet Fund provides "competitively awarded grants to CDFIs *and* qualified non-profit housing organizations" to finance affordable housing activities, related economic development activities, and community service facilities.[22]

Another program that certified CDFIs and CDFI-like entities can potentially access is the New Markets Tax Credit Program (NMTC). Through the NMTC, individual and corporate investors can receive a tax credit against their federal income tax in exchange for making equity investments in specialized financial intermediaries called *Community Development Entities* or *CDEs*. CDEs must also apply for that designation, have a primary mission of serving low-income communities, and maintain accountability to the residents of their targeted low-income communities.

Bank Enterprise Awardees are FDIC-insured depository institutions that have been awarded by the CDFI Fund for "increasing their investments and support of CDFIs and advancing their community development financing and service activities in the most economically distressed communities."[23] The program leverages federal investments with private funds, multiplying the funding that can be used to support affordable housing, improve access to finance, and grow local, distressed economies.[24]

Another CDFI program that encourages CDFI banks, banks, and nondepository CDFIs to collaborate is the CDFI Fund's Small Dollar Loan Program (SDLP), which launched its inaugural round in September 2021.[25] The SDLP's purpose is to expand consumer access to financial institutions by providing alternatives to high-cost, small-dollar lending, such as payday loans and check cashers, which nearly a quarter of American households use in lieu of traditional bank accounts.[26] By providing funds to support Loan Loss Reserves and Technical Assistance, certified CDFIs are encouraged to establish and maintain small-dollar loan programs that provide term loans of no more than $2,500. While these loan amounts may seem small individually, in aggregate, U.S. consumers borrow nearly $90 billion every year in short-term, small-dollar loans that typically range from $300 to $5,000.[27] Given the market size, and the increased demand for funding because of the COVID-19 pandemic, the SDLP is an important source of institutional capacity building to provide small-dollar loans.

"Newer" CDFI Resources

In addition to the CDFI-focused financial resources and programs discussed previously, the COVID-19 pandemic, the racial injustices it exposed, and subsequent responses catalyzed various new types of capital or support for certified CDFIs. Each provides a specific tool to help CDFIs lend to their designated target markets — some delivering liquidity so that CDFIs free up their balance sheets and continue to lend, some providing loan loss reserves so that CDFIs can shore up their portfolios from anticipated loan losses, and some providing direct lending capital or operating support, among other uses.

EMERGENCY CAPITAL INVESTMENT PROGRAM (ECIP)

One of the newer federal programs available to CDFIs and MDIs is the Treasury's Emergency Capital Investment Program (ECIP), which Congress created in response to the pandemic in the Consolidated Appropriations Act of 2021 to augment CDFIs' efforts to support small businesses and consumers in their communities. The program provides capital to certified CDFIs "to provide loans, grants, and forbearance for small businesses, minority-owned businesses, and consumers, especially in low-income and underserved communities, that may be disproportionately impacted by the economic effects of the COVID-19 pandemic." The Treasury Department recently awarded $9 billion in capital directly to 160 CDFI banks and 59 MDIs.[28] The banking agencies have helped implement the ECIP. For example, the Board, OCC, and FDIC recently released an accompanying interim final rule to provide the regulatory capital treatment for instruments issued under the program. Depending on its implementation, ECIP has the potential to provide an important source of previously unavailable Tier One capital for CDFI banks and MDIs, which would enable these entities to not just lend, but also grow through acquisition or expansion, thus being able to serve more clients.

PAYCHECK PROTECTION PROGRAM LIQUIDITY FACILITY

The congressionally appropriated SBA Paycheck Protection Program and the Federal Reserve's related Paycheck Protection Program Liquidity Facility (PPPLF) have provided liquidity totaling more than $180 billion since their inception in 2020. These programs provided funds for 67 nonbanks, many of which were not-for-profit CDFI loan funds, in addition to 38 CDFI banks and MDIs that participated in the PPPLF. In fact, the PPPLF was the most heavily used of the emergency lending facilities established by the Federal Reserve to support the continued flow of credit to households, businesses, and state and local governments during the height of the pandemic.[29] The PPPLF provided important support for enabling mission-oriented CDFIs, MDIs, and other small banks to support very small businesses. Among banks that participated in the facility, community banks, including CDFI banks (those with $10 billion or less in assets), have received more than 90 percent of the advances from the PPPLF.[30] This example demonstrates that CDFIs and MDIs stepped up to the plate to help ensure pandemic relief capital flowed to the communities and small businesses that needed it most, and that without their efforts, the capital likely would not have reached as deeply into LMI markets.

CDFI RAPID RESPONSE PROGRAM

As part of the 2021 Consolidated Appropriations Act, the CDFI Fund awarded $1.25 billion to CDFIs in support of communities impacted by the COVID-19 pandemic. The CDFI Fund designed the CDFI Rapid Response Program (CDFI RRP) to quickly deploy capital to certified CDFIs through a streamlined application and review process.[31] The historic pot of award dollars represents a watershed moment. Prior to this appropriation, since its inception in 1994, the CDFI Fund had awarded nearly $3.9 billion to CDFIs through its CDFI Financial Assistance, Bank Enterprise Award, and other programs over 27 years. The $1.25 billion CDFI RRP funding is equivalent to about one-third of that amount, awarded in just one year; 863 qualified CDFIs are currently in the process of deploying these dollars toward financial products and services, loan loss reserves, providing development services, or in the case of depository institutions, capital reserves.[32] Further, CDFIs can expend $200,000 or 15 percent of the award value, whichever is greater, toward operations including salaries, fringe benefits, professional services, travel, training, and education for staff, as well as equipment and supplies. Recipients will begin providing their first reports about uses of award funds and loan transactions shortly. This information will be of great interest to researchers and policymakers alike once it becomes available to the public, providing a window into how CDFIs met the needs of borrowers and where loans were made, and enable econometric analysis to be conducted to assess the effectiveness of disbursements.

CDFI MINORITY LENDING PROGRAM

One program from the 2021 Consolidated Appropriations Act is still under development: the Emergency Support and Minority Lending Program. This program has a $1.75 billion budget intended to expand lending, grant making, or investment activity in LMI minority communities that have significant unmet capital or financial services needs.[33] Once available, depository and nondepository CDFIs, including a new category of CDFIs, "minority lending institutions," can apply for these funds.[34] How the CDFI Fund will implement this program remains an open question — and banks should follow developments on the CDFI Fund's website to determine award eligibility and deadlines once the information is publicly available.

PRIVATE SECTOR AND EARNED INCOME

Corporations and private foundations have also substantially increased their investments in CDFIs in light of the pandemic and the racial injustices it highlighted further. Companies such as Netflix, Microsoft, Google, and Nike, as well as philanthropist MaKenzie Scott, have all committed to supporting CDFIs and MDIs as a means to promote economic opportunity and racial equity through various investment vehicles and grant funding.[35] Meanwhile, S&P-rated nonprofit CDFIs continue to structure bonds with large financial institutions to access long-term, patient capital to address financing challenges that extend beyond a five- or 10-year term, such as affordable housing developments or community health-care centers, which all benefit from 30-year financing terms.[36]

Challenges CDFIs Still Face

Given the recent increase in the flow of capital to support CDFIs, researching whether the capital flowed to its intended recipients, and identifying the impediments to the flow to end users, will help inform policymakers' approach to providing access to capital for LMI communities and communities of color, particularly in times of financial distress. It is also important to understand that while the federal pandemic response provided CDFIs with much-needed sources of capital to support their operations and continued lending in economically distressed communities, the pandemic itself also exacerbated the challenges many CDFIs previously faced.

Working within the confines of, and fighting against, institutionalized systemic racism perhaps remains the thorniest challenge for CDFIs. Working with harder-to-reach clients continues to be extremely challenging. Examples of such challenges include: the subjectivity of appraisals that can significantly undervalue properties;[37] the need for collateral, which is limited in low-wealth communities of color; requirements for personal guarantees, which can put business owners with limited assets in jeopardy; and a preference for lending to those with the highest credit scores in spite of research and analysis demonstrating that there is bias baked into these scores.[38] CDFIs also struggle with how to adjust these requirements so they can ensure repayment, while being flexible in understanding that credit models likely have their own racially motivated biases, and that CDFIs must work harder to reach the communities of color they serve.[39]

Another challenge is staffing, which in many industries has only become more difficult in the last two years. It takes time to recruit and train culturally competent staff members who understand both CDFI business models and the needs of the clients they serve. Competition for staffing has increased with the growing need for staff to process more requests for financing from clientele. Additionally, the skill sets in CDFIs have evolved, with many CDFIs vying for talented, diverse individuals who can help grow the balance sheets of CDFIs and communicate to the public and investors about the impact CDFIs provide both financially and socially. A recently developed program, the Economic Mobility Corps, has the potential to address some fluctuating staff issues and build a pipeline of future CDFI practitioners; however, while innovative, with an initial budget to provide 61 full-time AmeriCorps service members to CDFIs over a two-year period, this joint initiative between the CDFI Fund and AmeriCorps will likely only make a small dent in the current dearth of CDFI staffing options.

Back-office management, work that many CDFIs conduct themselves, continues to cause many operational headaches. With increased demand for loans comes an increased need for back-office capacity; however, the ways in which CDFIs model their staffing now, when coffers are full, could have repercussions when demand wanes. Shared service and fee-for-service models can be advantageous; however, many CDFIs prefer to keep many operations in house. Examples include repayment and collection work, which many CDFIs like to perform themselves so they can maintain positive relationships with clients, which in turn can help repayment.[40] As balance sheets and the number of transactions grow, and hybrid work models prevail, CDFIs will need to assess the trade-offs between ownership of back-office processes and return on investment. Trade-offs will also be particularly relevant as living in an increasingly digitized world requires budgets and infrastructure to support online access and cybersecurity around the clock.

To this end, partnerships will become increasingly necessary, particularly as competition increases from fintechs and other nonbank financial service providers that can provide fast, digital financing options. Several CDFIs have worked to create partnerships with such organizations, and finding the right strategic partners that are mission-aligned remains of the utmost importance.[41] Other partnerships, such as those that CDFIs naturally pursue with employers, utility companies, and other local actors, hold creative potential to address the industry's latest challenges.

Ebbing loan demand, changes in appropriations, and the appetite of funders will also likely have repercussions for CDFI capitalization. To address potential future funding shortfalls, CDFIs will need to explore capital from other sources such as secondary markets and other private investors. Investments from these sources will require CDFIs to address an issue that has plagued the industry for over a decade, if not longer — the lack of standardized financial data. Determining how to standardize data collection in a nonstandardized industry is no small feat. If successful, CDFIs will be able to provide investors with consistent and transparent information about their operations and loan portfolios, which investors require to justify the investments.[42]

Finally, the influx of capital from existing federal funding that is currently in play will necessitate adroit compliance, data tracking, and impact evaluation and measurement to meet government requirements. The customized nature of CDFI loan products makes data collection challenging but not impossible. Several CDFIs have mastered this art, and regularly produce reliable, comprehensive data sets. The CDFI Fund itself is continuously working to improve its own data collection systems and instructions, but funding and resources to support the accurate collection of usable, analyzable data at the scale required to conduct meaningful econometric analysis remain elusive.

CONCLUSION

The Federal Reserve has a longstanding commitment to support the missions of CDFIs and the communities they serve, regardless of the economic cycle in which we may find ourselves. We are at an exciting and important time in the history of the CDFI industry. While CDFIs are not a panacea for our economic challenges, they do play a role in an inclusive recovery from the pandemic and its associated economic turmoil. With the growth that has occurred in the CDFI industry since the mid-1990s, repeated evidence of the ability to respond in times of national economic duress, and the challenges our nation faces in creating an equitable economic recovery from the COVID-19 pandemic, it is no surprise that the tent of partners with the CDFI sector has grown in size. The issue now is to ensure these entities are fully equipped to do this extremely challenging and important work for the long haul and document their success with sound econometric analysis to state with empirical confidence that CDFIs can and do improve economic outcomes for the clients they serve. ■

Endnotes*

1 Congress provided $1.25 billion to the CDFI Fund in the 2021 Consolidated Appropriations Act to award grants to CDFIs to deliver assistance to communities impacted by COVID. See CDFI Rapid Response Program (CDFI Fund, June 15, 2021).

2 See Jonathan Shieber, "Vista Partners founder calls for a fintech revolution to help pandemic-hit, minority-owned small businesses" (TechCrunch, May 10, 2020).

3 See Price Fishback, Jonathan Rose, Ken Snowden, and Thomas Storr, "New Evidence on Redlining by Federal Housing Programs in the 1930s" (Federal Reserve Bank of Chicago, January 3, 2022) and "Tracing the Legacy of Redlining: A New Method for Tracking the Origins of Housing Segregation" (National Community Reinvestment Coalition, February 24, 2022).

4 See the Treasury Department CDFI.

5 See the *CDFI Annual Certification and Data Collection Report (ACR): A Snapshot for Fiscal Year 2020* (U.S. Treasury Department, October 2021).

6 See Pub. L 103-325, 108 STAT. 2160 (September 23, 2004). The provisions of the act creating the CDFI Fund appear in subtitle A, "Community Development Banking and Financial Institutions Act of 1994," and is codified at 12 U.S.C. §4701 et seq.

7 See *CDFI Annual Certification and Data Collection Report (ACR): A Snapshot for Fiscal Year 2020*.

8 See the Treasury Department FAQs on "Certification, Compliance Monitoring and Evaluation."

9 CDFIs elect to serve certain target markets, which can be geographical, or focus activities in a nondiscriminatory way on specific low- and moderate-income (LMI) population groups.

10 Such programs include the CDFI Fund's competitive CDFI and Native CDFI Financial Assistance Programs, and the CDFI Bond Guarantee Program, among others; free training and technical assistance opportunities sponsored by the CDFI Fund; and funding from external parties like foundations, corporations, and philanthropies that focus their work with certified CDFIs. See also "CDFI Certification" (CDFI Fund); Programs | Community Development Financial Institutions Fund; NCUA-CDFI Certification Initiative (National Credit Union Administration).

11 See Michael Swack, Jack Northrup, and Eric Hangen, "CDFI Industry Analysis: Summary Report," Vol. 24 *Community Investments* No. 2 (Federal Reserve Bank of San Francisco, 2012); see Community Development Consulting, Inc. for a discussion of CDFI self-sufficiency ratios, where even CDFIs with the highest asset size were not 100 percent self-sufficient. Also note, CDFIs are prohibited from charging excessively high or usury rates, while similar lending businesses without a social mission are not subject to these prohibitions.

[12] If you know of a community bank or nonprofit that has inherently been providing socially responsible financial products and services in LMI communities, with an institutional commitment to including those community members within leadership or boards of directors, it might be worth exploring whether applying for CDFI certification could help the entity meet its goals and the needs of the communities it serves.

[13] See Annie Donovan, "Outcomes-Based Funding and the Community Finance Ecosystem."

[14] See Jamie R. McCall and Michele M. Hoyman, "Community Development Financial Institution (CDFI) program evaluation: a luxury but not a necessity?" *Community Development* (October 31, 2021).

[15] See Michael Swack, Eric Hangen, and Jack Northrup, "CDFIs Stepping into the Breach: An Impact Evaluation — Summary Report" (August 2014).

[16] See Brent Howell, Lisa Mensah, and Dafina Williams, "Lending Where Others Will Not: How CDFIs Build Family and Community Wealth," Federal Reserve Bank of St. Louis (2021).

[17] See "What's a Capital Stack and How Does It Work?" *CRA Today.*

[18] See "Double Jeopardy: COVID-19 and Black Owned Businesses" (Federal Reserve Bank of New York, August 2020); Alicia Robb, "Access to Capital Among Young Firms, Minority-owned Firms, Women-owned Firms, and High-tech Firms" (April 2013); "Access to Capital Is Still a Challenge for Minority Business Enterprises" (Minority Business Development Agency, September 2006); "Racial Disparities and Housing Policy" (Habitat for Humanity, August 2020).

[19] See "Access to Access to Capital and Credit in Native Communities and Credit in Native Communities," (University of Arizona Native Nations Institute).

[20] Note to 12 U.S.C. §1463. "'Socially and economically disadvantaged individuals' refers to minority communities such as 'Black American, Asian American, Hispanic American, or Native Americans.'" FDIC: Minority Depository Institutions Program.

[21] See FDIC: Minority Depository Institutions Program and CDFI Fund's "List of Certified Community Development Financial Institution (CDFIs) with Contact Information as of December 14, 2021."

[22] See Capital Magnet Fund (CDFI Fund).

[23] See Bank Enterprise Award Program (CDFI Fund).

[24] See Bank Enterprise Award Program.

[25] See Small Dollar Loan Program (CDFI Fund).

[26] See Small Dollar Loan Program.

[27] See "Comptroller Urges Banks to Meet Consumers' Short-Term, Small-Dollar Credit Needs" (U.S. Department of the Treasury).

[28] Note some CDFIs are also MDIs, and there is overlap in these two numbers. See Emergency Capital Investment Program (U.S. Department of the Treasury) and Financial Institutions Approved to Receive ECIP Investments.

[29] See Financial Stability Report: "Borrowing by Businesses and Households" (Federal Reserve Board, May 2021).

[30] See Financial Stability Report: "Borrowing by Businesses and Households."

[31] See "U.S. Treasury Awards $1.25 Billion to Support Economic Relief in Communities Affected by COVID-19" (CDFI Fund, June 15, 2021).

[32] See CDFI RRP Application Overview Presentation (CDFI Fund, February 21, 2021).

[33] See "Treasury to Invest $9 Billion in Community Development Financial Institutions and Minority Depository Institutions Through Emergency Capital Investment Program (ECIP)" (U.S. Department of the Treasury, March 4, 2021).

[34] See "Treasury to Invest $9 Billion in Community Development Financial Institutions and Minority Depository Institutions Through Emergency Capital Investment Program."

[35] See "Netflix to Invest 2% of Cash Holdings in CDFIs and Other Organizations Serving Black Communities" (Opportunity Financial Network, June 30, 2020); "Nike, CDFI Leaders Reflect on Company's Decision to Invest in Opportunity Through Hope Credit Union" (Opportunity Financial Network, December 17, 2021); "Google Announces New $50 Million Investment in CDFIs and Black Community | Opportunity Finance Network" (Opportunity Financial Network, June 18, 2020); "FDIC Launches Mission-Driven Bank Fund with Microsoft, Truist to Support CDFIs" (Opportunity Financial Network, September 21, 2021); "Philanthropist MacKenzie Scott Supports 24 OFN Member CDFIs in Latest Giving" (Opportunity Financial Network, December 16, 2020).

[36] See "Missions Possible: How U.S. CDFIs Meet Financial and Social Missions, and the Rating Implications That Follow" (Standards & Poor); "LISC Impact Notes Named Social Bond of the Year by Environmental Finance" (Local Initiatives Support Corporation, March 31, 2021).

[37] In June 2021, the Interagency Task Force of Property Appraisal and Valuation Equity (PAVE) was created to address this issue. Additional information, including a March 2022 report and action plan, is available on PAVE's website.

[38] See Neil Bhutta, Aurel Hizmo, and Daniel Ringo, "How Much Does Racial Bias Affect Mortgage Lending? Evidence from Human and Algorithmic Credit Decisions" (SSRN, July 19, 2021); Ashlyn Aiko Nelson, "Credit scores, race, and residential sorting," *Journal of Policy Analysis and Management* (November 30, 2009).

[39] See the Letter to Congressional Leaders (April 9, 2020).

[40] See "Scaling Lending to Entrepreneurs of Color: Part I Core Operational Challenges" (Aspen Institute).

[41] See "TILT Forward Initiative and DreamFund" (Association for Enterprise Opportunity, November 20, 2017).

[42] See Sean Campbell and Christopher Shin, "Securitization for Social Innovation: Jump-Starting Commercial Intermediation for the CDFI Industry" (Local Initiatives Support Corporation, January 2021).

*Note: The links for the references listed in the Endnotes are available on the *Consumer Compliance Outloo*k website at consumercomplianceoutlook.org.

Federal Reserve Board Consumer Affairs Letters for 2021 and 2022

Consumer Affairs (CA) Letters address significant policy and procedural matters related to the Federal Reserve System's consumer compliance supervisory responsibilities. CA letters are numbered sequentially by year. For example, the second CA letter issued in 2022 is numbered CA 22-2. Letters that have been superseded or contain confidential supervisory information are not included. In some cases, CA letters are issued jointly with the Federal Reserve's Banking Supervision and Regulation Division. Letters issued by that division are commonly known as SR letters.

CA 22-3 / SR 22-4	Contact Information in Relation to Computer-Security Incident Notification Requirements
CA 22-2	Interagency Statement on Special Purpose Credit Programs Under the Equal Credit Opportunity Act and Regulation B
CA 22-1 / SR 22-3	Federal Financial Institutions Examination Council Issues Statement of Principles on Examination Information Requests
CA 21-17	Revised Home Mortgage Disclosure Act Examination Procedures
CA 21-16	Interagency Statement on Supervisory and Enforcement Practices Regarding the Mortgage Servicing Rules in Response to the Continuing COVID-19 Pandemic and CARES Act
CA 21-15 / SR 21-17	Interagency Statement on Managing the LIBOR Transition
CA 21-14	Revised Interagency Examination Procedures for Regulation Z
CA 21-13 / SR 21-16	Community Bank Access to Innovation Through Partnerships
CA 21-12	Supervisory Expectations for Supervised Institutions Regarding Juneteenth Federal Holiday and Certain Provisions of Regulation Z
CA 21-11 / SR 21-15	Guide for Community Banking Organizations Conducting Due Diligence on Financial Technology Companies
CA 21-10 / SR 21-13	Revised Special Post-Employment Restriction for Senior Examiners and Work Paper Reviews for Departing Examiners
CA 21-9	Extension of CRA Consideration for Community Development Activities in Puerto Rico and the U.S. Virgin Islands in Response to Hurricane Maria
CA 21-8	Resumption of Home Mortgage Disclosure Act Quarterly Reporting
CA 21-7	Revised *A Guide to HMDA Reporting: Getting It Right!*
CA 21-6	Suspension of Regulation D Examination Procedures
CA 21-5	Community Reinvestment Act Consideration for Activities in Response to the Coronavirus
CA 21-4 / SR 21-6	Highlighting the Federal Reserve System's Partnership for Progress Program for Minority Depository Institutions and Women's Depository Institutions
CA 21-3	Revised Interagency Examination Procedures for Regulation Z
CA 21-2 / SR 21-4	Inactive or Revised SR Letters Related to the Federal Reserve's Supervisory Expectations for a Firm's Boards of Directors
CA 21-1 / SR 21-3	Supervisory Guidance on Board of Directors' Effectiveness

News from Washington: Regulatory Updates*

The Federal Reserve releases a Synthetic Identity Fraud Mitigation Toolkit. On February 8, 2022, the Federal Reserve released a toolkit to help the financial industry and consumers understand and combat synthetic identity theft. According to Jim Cunha, an executive vice president at the Federal Reserve Bank of Boston, "synthetic identity fraud, where fraudsters create an identity out of pieces of real and/or fictitious information, continues to grow and resulted in an estimated $20 billion in losses for U.S. financial institutions in 2020." The toolkit, which the Federal Reserve developed after researching this issue and collaborating with industry experts, contains these five modules:

- Synthetic Identity Fraud Mitigation Toolkit
- Synthetic Identity Fraud Defined
- Synthetic Identity Fraud Definition Overview
- Synthetic Identity Fraud: Defined It to Fight It
- Progress Made in Defining Synthetic Identity Fraud

On a related note, *Outlook* previously published an article titled "Overview of Federal Consumer Privacy and Security Laws for Financial Services" that discussed the electronic consent-based Social Security number verification service, which allows certain entities to verify if an individual's Social Security number, name, and date of birth combination match the Social Security Administration's records to help combat identity theft.

The Consumer Financial Protection Bureau (Bureau) issues a request for information (RFI) about fees imposed by providers of consumer financial services. On February 2, 2022, the Bureau published an RFI in the *Federal Register* to address its concern about fees for consumer financial services and products. The RFI solicits information from consumers for several issues related to fees, including:

- fees that were high, unexpected, or unclear;
- fees that obscure the true cost of the product or service by not being built into the upfront price;
- fees that exceed the cost of the service covered; and
- the tools the Bureau should use to address this issue.

The RFI highlighted various fees across many different financial products and services including deposit accounts, credit cards, remittance transfers, prepaid cards, and mortgages. The deadline to respond was March 31, 2022.

HUD's Office of General Counsel determines that Special Purpose Credit Programs under the Equal Credit Opportunity Act (ECOA) generally do not violate the Fair Housing Act. On December 6, 2021, the Office of General Counsel of the U.S. Department of Housing and Urban Development (HUD) issued a statement clarifying that the use of Special Purpose Credit Programs (SPCPs) under the ECOA generally would not violate the Fair Housing Act (FHA). The ECOA prohibits creditors from discriminating on a prohibited basis in any aspect of a credit transaction; however, the ECOA contains a limited exception for SPCPs. After a firm has conducted the analysis required by Regulation B and established a written program, this exception permits offering special underwriting or pricing for applicants meeting eligibility requirements. Eligibility requirements may include that an applicant is part of a traditionally disadvantaged group, including those protected by the ECOA and/or the FHA. HUD, which has rulemaking and interpretive authority for the FHA, concluded that "SPCPs offered by non-profit organizations to serve economically disadvantaged classes and those offered by for-profit organizations to meet special social needs that are carefully tailored and targeted to meet ECOA and Regulation B's specifications will generally not 'discriminate' within the meaning of the [FHA], just as they do not constitute discrimination under ECOA."

Bureau opens inquiry into "buy now, pay later" (BNPL) credit. On December 16, 2021, the Bureau announced an inquiry into BNPL, a form of credit that allows consumers to finance purchases with an interest-free loan, provided the consumer repays it within a specified time frame. BNPL lenders typically require four, equal bimonthly payments, starting with a 25 percent down payment at purchase. In recent years, the BNPL market has rapidly grown, raising potential consumer protection concerns. In particular, the Bureau cited concerns about accumulating debt, regulatory arbitrage, and data harvesting. In connection with the inquiry, the Bureau served a market monitoring order, as permitted under the Dodd–Frank Act, on five BNPL lenders: Affirm, Afterpay, Klarna, PayPal, and Zip. The order includes detailed questions about their business practices to help the Bureau "monitor for risks to consumers in the offering or provision of consumer financial products or services." The Bureau also published a blog posting on December 16, 2021, to discuss some of its consumer protection concerns for BNPL, including:

*Links to the announcements are available in the online version of *Outlook* at consumercomplianceoutlook.org.

- fees for BNPL;
- challenges in returning merchandise purchased with BNPL loans;
- fewer consumer protections for BNPL loans relative to credit cards; and
- the effect of BNPL loans on credit scores.

The Bureau later expanded its inquiry into BNPL to the public by publishing a request for comment in the *Federal Register* on January 24, 2022. The comment period ended on March 25, 2022.

The House Financial Services Committee conducted a hearing on November 2, 2021, titled "Buy Now, Pay More Later? Investigating Risks and Benefits of BNPL and Other Emerging Fintech Cash Flow Products." The committee's majority staff also released a memo about BNPL and the other products examined in the hearing.

The Bureau issues two reports on overdraft fees. On December 1, 2021, the Bureau released two reports on fees imposed for overdraft and nonsufficient funds (NSF). The first report (*Overdraft/NSF Fee Reliance Since 2015 – Evidence from Bank Call Reports*) analyzed banks' overdraft and NSF fee income based on call report data and estimated the overall market revenue of $15.47 billion in 2019, with banks over $1 billion earning around $11.97 billion, while smaller institutions earned approximately $3.5 billion. The second report (*Checking Account Overdraft at Financial Institutions Served by Core Processors*) analyzed overdraft data from core processor providers and found that 92.9 percent of smaller banks and 60.9 percent of credit unions had an overdraft program, in contrast to larger banks, where these programs are more common. The report also found that the average fee charged for an overdraft was 6 percent lower at credit unions and 11 percent lower at small banks relative to large banks.

On a related note, on February 10, 2022, the Bureau published a blog posting comparing overdraft fees across several different financial institutions.

Federal Reserve's Supervision Central Website

Effective supervision relies on strong collaboration between banking agencies and supervised institutions. Over the years, the need for better ways to exchange data outpaced the technology used for supervisory activities. To address this, the Federal Reserve launched Supervision Central, a centralized tool to facilitate secure data intake, sharing, and collaboration among supervisory staff, bank staff, and other agencies' staff for safety and soundness and consumer compliance activities at community and regional banking organizations supervised by the Federal Reserve.

Supervision Central is designed to reduce regulatory burden for supervised institutions by providing an easy way to submit documents and information to the Federal Reserve. Data submitted will be reusable across examinations with the goal of reducing the volume of duplicate information requests from the Federal Reserve by making documents previously provided more readily available to supervisory staff. Also, supervised institutions will no longer need to submit the same documents to multiple banking agencies for joint examinations and other supervisory activities because the agencies will be accessing the same documents. You can access the help site by visiting **www.supervisioncentral.org.**

On the Docket: Recent Federal Court Opinions*

FAIR CREDIT REPORTING ACT (FCRA)

Ninth Circuit affirms summary judgment of a FCRA claim against a consumer reporting agency (CRA) for reporting stale information because the plaintiff failed to show the CRA acted negligently or willfully. *Moran v. The Screening Pros, LLC,* 25 F.4th 722 (9th Cir., 2022). In 2010, when the plaintiff applied to lease an apartment, the landlord obtained his consumer report from The Screening Pros, a consumer reporting agency, which showed criminal charges had been filed against the plaintiff in 2000 that were dismissed in 2004. Section 605(a) of the FCRA (15 U.S.C. §1681c(a)) generally requires CRAs to remove negative information from consumer reports after specified time periods to prevent consumers being harmed by stale information. However, a plaintiff can only recover damages under the FCRA for a negligent or willful violation. The district court held that the plaintiff failed to show negligent or willful conduct and dismissed the case on summary judgment.

On appeal, the Ninth Circuit affirmed. The court held that a *negligence violation* requires a plaintiff to "show that the defendant acted pursuant to an objectively unreasonable interpretation of the statute," while a *willful violation* requires a plaintiff to show a knowing or a reckless violation of a standard. The court previously ruled the defendant should not have included the 2004 dismissal of the criminal charges in the plaintiff's consumer report in 2010. But the defendant submitted evidence that its interpretation was consistent with industry norms. In addition, the Federal Trade Commission's only guidance on the question at the time (although outdated) appeared to permit reporting the charge. Accordingly, the court found that, although a violation occurred, it was neither negligent nor willful and therefore affirmed the summary judgment.

FINTECH

The Conference of State Bank Supervisors (CSBS) withdraws its lawsuit against the Office of the Comptroller of the Currency (OCC) challenging the application of a fintech company to become a deposit-taking national bank without obtaining insurance from the Federal Deposit Insurance Corporation (FDIC). In 2018, the OCC issued a policy statement indicating it would accept applications for special purpose national bank charters for nonbank fintech companies under its chartering authority under the National Bank Act (NBA). This policy has been subject to various lawsuits, including one the CSBS filed. On January 13, 2022, the CSBS filed a notice with the U.S. District for the District of Columbia to voluntarily withdraw its lawsuit against the OCC concerning the application of Figure Technologies, a fintech company, for a special purpose national bank charter.

The lawsuit challenged the OCC's legal authority under the NBA to charter a full-service national bank without the entity obtaining deposit insurance from the FDIC. The CSBS is withdrawing the lawsuit because in December 2021, Figure Technologies amended its application to indicate it would apply to the FDIC for deposit insurance and to the Board of Governors of the Federal Reserve System to become a bank holding company under §3 of the Bank Holding Company Act. The CSBS stated the lawsuit was now moot because its concerns were addressed.

REGULATION E — ELECTRONIC FUND TRANSFER ACT (EFTA)

Ninth Circuit reverses the dismissal of a lawsuit for a consumer's liability for unauthorized transactions because the complaint plausibly alleged they would have occurred regardless of whether the consumer timely notified the bank. *Widjaja v. JPMorgan Chase Bank, N.A*., 21 F.4th 579 (9th Cir. 2021). The plaintiff alleged that identity thieves stole more than $500,000 from her checking account at Chase in a series of withdrawals. The second withdrawal of $29,000 on November 2, 2017, was flagged by the receiving bank as suspicious and returned to Chase. However, Chase did not notify the plaintiff of the incident or change her account credentials to prevent further unauthorized transactions.

The plaintiff alleged additional withdrawals were made between November 2017 and March 2019, but she did not report them to Chase until March 2019 because she alleged that she was traveling abroad and had "very limited or no" Internet access to check her bank statements. Chase reimbursed the plaintiff for some of the transactions but declined to reimburse her for $300,000 in losses because her notice of an unauthorized transaction was made more than 60 days after transmitting the periodic statement with the disputed transactions. Under the Electronic Fund Transfer Act (EFTA), if a consumer fails to report an unauthorized transfer to the bank within 60 days after the statement containing the unauthorized transfer is sent and the bank can establish that unauthorized transfers made after the 60-day period would not have occurred but for the consumer's failure to notify the bank of the earlier unauthorized transfer, consumers may face unlimited liability for unauthorized transfers occurring after the 60-day period. See 12 C.F.R. §1005.6(b)(3).

The district court held that the EFTA barred her claim as a matter of law and dismissed the case. On appeal, the Ninth Circuit court noted that under §1693g(a) of the EFTA, a consumer may only be held liable for unauthorized transfers occurring after the 60-day period if the bank establishes the transfers "would not have occurred but for the failure of the consumer" to report them within the time frames specified in the regulation and that the district court's analysis overlooked this requirement.

The court noted that "[w]hen notified by a consumer that an unauthorized transfer has taken place, most banks have procedures in place to prevent subsequent unauthorized transfers, such as freezing the consumer's account or changing the account number and password." Because Chase did not take these actions after becoming aware of the unauthorized withdrawal of $29,000 in November 2017, the plaintiff plausibly alleged a violation for purposes of surviving a motion to dismiss. On remand to the trial court, the plaintiff will still have the burden to prove that, even if she had timely notified Chase of the unauthorized transactions, Chase would not have prevented the additional ones from occurring.

STANDING

The Second Circuit, on reconsideration, dismisses a class-action lawsuit for failing to timely record a mortgage satisfaction because plaintiffs lacked standing. *Maddox v. Bank of N.Y. Mellon Tr. Co., N.A.,* 19 F.4th 58 (2d Cir. 2021). In 2000, the plaintiffs purchased a property secured by a mortgage loan, which was later assigned to Bank of New York (BNY) Mellon. In September 2014, the property was sold, but BNY Mellon did not record a mortgage satisfaction until September 22, 2015. New York law requires a creditor to record a mortgage satisfaction within 30 days of full repayment and provides statutory damages for violations. The plaintiff sought damages for all class members whose mortgage liens were not timely marked satisfied. BNY Mellon sought to dismiss the suit on standing grounds; the District Court denied the motion, and the Second Circuit affirmed that decision on appeal. But after the Supreme Court clarified in *TransUnion LLC v. Ramirez*, 141 S. Ct. 2190 (2021) that to have standing to sue in federal court plaintiffs must show that they suffered concrete injury, BNY asked the court to reconsider.

On reconsideration, the Second Circuit ordered the case dismissed for lack of standing. The court noted that the Supreme Court in *TransUnion* clearly stated "*no concrete harm; no standing*." The plaintiffs had sold their property without incident and did not allege reputational harm from someone else seeing the lien in the county's property records. The plaintiffs alleged the lien could have impacted their credit rating and made it more difficult to obtain financing if they needed it, but the court noted this was conjecture and this risk never materialized. Finally, the plaintiffs alleged emotional harm, but the court found the allegations implausible. The court noted that the plaintiffs could still seek damages in state court for failing to record the satisfaction.

* Links to the court opinions are available in the online version of *Outlook* at consumercomplianceoutlook.org.

REGULATORY CALENDAR

EFFECTIVE DATE OR PROPOSAL DATE†	IMPLEMENTING REGULATION	REGULATORY CHANGE
10/01/22	Reg. Z	Final rule to extend the sunset date for the temporary Government-Sponsored Enterprise (GSE) Qualified Mortgage (QM) loan definition Note: The GSEs announced in May 2021 that they can no longer purchase Patch GSE QM loans after June 30, 2021, despite the Consumer Finance Protection Bureau (Bureau)'s extension to October 1, 2022
04/01/22	Reg. Z	Final rule amending Regulation Z to facilitate the transition from the LIBOR interest rate index
01/01/22	CRA	Final rule of the Office of the Comptroller of the Currency to rescind its June 2020 CRA modernization rule
01/01/22	Regs. Z and M	Final rules establishing dollar thresholds for credit exempt from Regulations Z and M
01/01/22	Reg. Z	Final rule establishing a loan exemption threshold for appraisals of higher-priced mortgages for 2022
01/01/22	Reg. C	Final rule establishing 200 loans as the permanent Home Mortgage Disclosure Act data reporting a threshold for open-end lines of credit
11/30/21	Reg. F	Final rule that creates implementing regulations for the Fair Debt Collection Practices Act
09/01/21	Reg. B	The Bureau's §1071 rulemaking proposal for lenders to collect and report data on small business credit applications, including women and minority-owned businesses
08/12/21	Reg. Z	Interpretive rule: impact of the 2021 Juneteenth Holiday on certain closed-end mortgage requirements
07/19/21	N/A	Proposed Interagency Guidance on Third-Party Relationships: Risk Management

† Because proposed rules do not have an effective date, we have listed the *Federal Register* publication date.

REGULATORY CALENDAR

EFFECTIVE DATE OR PROPOSAL DATE†	IMPLEMENTING REGULATION	REGULATORY CHANGE
06/23/21	MLA	Bureau's interpretive rule for authority to conduct Military Lending Act (MLA) examinations
05/10/21	N/A	Federal Reserve Board's statement on the role of supervisory guidance
03/18/21	Reg. H	Agencies issue second proposed amendments to flood insurance questions and answers
03/16/21	Reg. B	Bureau issues interpretive rule that the scope of sex discrimination under the Equal Credit Opportunity Act includes sexual orientation and gender identity
03/01/21	Reg. Z	Final rule creating new QM category for Seasoned Loans
09/21/20	CRA/Reg. BB	Advanced notice of proposed rulemaking seeking comment on framework to modernize the Federal Reserve Board's implementing regulation for the Community Reinvestment Act
08/04/20	Reg. Z	Proposed rule under the Economic Growth, Regulatory Relief, and Consumer Protection Act to create a new exemption from escrow requirements for higher-priced mortgage loans
07/21/20	Reg. E	Final rule allowing insured institutions to estimate the exchange rate for a remittance transfer and increases exemption threshold from 100 to 500 remittance transfers per year
07/10/20	Reg. H	Proposed revisions to interagency questions and answers regarding flood insurance

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2022 Calendar of Events

May 10–11 **The Mortgage Market Research Conference**
Federal Reserve Bank of Philadelphia
Philadelphia, PA

June 21–24 **American Bankers Association Regulatory Compliance Conference**
Hyatt Regency Orlando
Orlando, FL

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