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CONSUMER COMPLIANCE OUTLOOK®

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OVERVIEW OF SPECIAL PURPOSE CREDIT PROGRAMS UNDER THE EQUAL CREDIT OPPORTUNITY ACT

BY KENNETH BENTON, PRINCIPAL CONSUMER REGULATIONS SPECIALIST, FEDERAL RESERVE BANK OF PHILADELPHIA

With the increased focus on racial economic disparities in recent years,[1] some financial institutions have contemplated creating tailored lending programs to help address this issue. But some institutions have expressed concerns whether a loan program targeting a protected class would violate the disparate treatment rules of the Equal Credit Opportunity Act (ECOA) and the Fair Housing Act (FHA).

These fair lending laws generally prohibit creditors from discriminating on a prohibited basis — including race — in credit and housing transactions.[2] Regulation B, ECOA's implementing regulation, also generally prohibits creditors from collecting information about race, color, religion, national origin, or sex to reduce the risk that creditors could use this information to discriminate on a prohibited basis.[3]

But Congress created a carveout in the ECOA to these requirements for Special Purpose Credit Programs (SPCPs), which allow creditors to consider prohibited-basis information in credit transactions to meet special social needs or to help an economically disadvantaged class of persons.[4] Provided that all the requirements for an SPCP are satisfied, a creditor may target applicants on a prohibited basis[5] and deny applicants who do not meet the eligibility requirements.[6]

Although SPCPs have been available since 1976 when they were added to the ECOA,[7] they have not been widely implemented.[8] This may reflect lenders' desire for greater clarity about the requirements for a compliant SPCP to avoid violating the ECOA and the FHA,[9] since fair lending violations have significant legal and reputational risks.

To address lenders' concerns, the Consumer Financial Protection Bureau (Bureau) issued an Advisory Opinion (AO) in 2021 that details and clarifies the requirements for an SPCP and provides explanatory examples.[10] Following this guidance, several federal agencies issued an interagency statement that encourages lenders to consider SPCPs,[11] and the Department of Housing and Urban Development (HUD) issued guidance to clarify that a compliant SPCP generally does not violate the FHA.[12]

Because of the renewed interest in SPCPs and the recent guidance, *Consumer Compliance Outlook* is publishing this article: 1) to discuss the requirements for establishing a compliant SPCP, 2) to provide examples of SPCPs that some financial institutions have implemented,

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3) to review the recent government-sponsored enterprises' (GSEs) SPCP plans, and 4) to provide an update on the Community Reinvestment Act (CRA) and SPCPs in the 2022 CRA rulemaking proposal.

SPCPs UNDER THE ECOA

The ECOA authorizes three different SPCPs:

- A credit assistance program expressly authorized by federal or state law for the benefit of an economically disadvantaged class of persons
- A credit assistance program administered by a nonprofit organization for its members or an economically disadvantaged class of persons, or
- A special purpose credit program offered by a profit-making organization to meet special social needs, according to the standards prescribed in the Bureau's regulations.[13]

The ECOA's legislative history shows that Congress focused on programs designed "to prefer members of economically disadvantaged classes'' and ''to increase access to the credit market by persons previously foreclosed from it."[14]

SPCP REQUIREMENTS OFFERED BY FOR-PROFIT INSTITUTIONS

Because *Outlook* focuses on outreach to financial institutions, this article reviews the requirements for SPCPs that for-profit institutions offer to meet special social needs. Regulation B specifies the following SPCP requirements that apply to for-profit financial institutions:

> **(i)** The program is established and administered pursuant to a written plan that identifies the class of persons that the program is designed to benefit and sets forth the procedures and standards for extending credit pursuant to the program; and
>
> **(ii)** The program is established and administered to extend credit to a class of persons who, under the organization's customary standards of creditworthiness, probably would not receive such credit or would receive it on less favorable terms than are ordinarily available to other applicants applying to the organization for a similar type and amount of credit.[15]

Here are the details of these requirements:

Written Plan

The written plan must:

- identify the class of persons the program is intended to benefit;
- specify the procedures and standards for extending credit under it; and
- list either its duration or when it will be reevaluated to determine whether to continue it.[16]

Class of Persons the Program Is Intended to Benefit

An SPCP must target a class of persons ''who would otherwise be denied credit or would receive it on less favorable terms,"[17] and the plan must explain if the class of persons will be required to demonstrate a financial need and/or share a common characteristic. The AO provides the following illustrative, but not exhaustive, examples of a class of persons an SPCP could target:

- minority residents of low- to moderate-income census tracts;
- residents of majority-Black census tracts;
- operators of small farms in rural counties;
- minority- or women-owned small business owners;
- consumers with limited English proficiency; or
- residents living on tribal lands.[18]

Procedures and Standards

The SPCP must include the procedures and standards for extending credit and be designed to increase the likelihood that either:

- a class of persons who would otherwise likely be denied credit will receive it under the program, or
- that a class of persons who would likely otherwise receive credit on less favorable terms will receive it on more favorable terms under the program.[19]

To satisfy this requirement, the creditor may:

- modify its existing loan standards;
- introduce a new product or service;
- adjust the terms and conditions or eligibility requirements for an existing product or service; or
- modify policies and procedures for loss mitigation programs, such as loan modifications.[20]

The AO includes an example of a creditor offering a new small business loan product for women-owned businesses that relaxes its regular loan standard of three years of industry experience to one year, if the creditor determined that its three-year requirement would likely prevent women-owned businesses from qualifying for small business credit.[21]

The written plan must also explain how the SPCP's policies and standards will increase credit availability for the class of persons the SPCP is intended to benefit.[22] If the targeted class shares a common characteristic, the plan may also discuss whether the creditor will be requesting and considering prohibited-basis information, such as race or nationality, which an SPCP may permissibly request.[23]

Program Duration/Reevaluation

The plan must specify its duration, which can be done by specifying how long it will last, by choosing a date to reevaluate if it is still needed, or by using a hybrid approach. The AO provides this example of the hybrid approach for the program's duration: It will end either on a specific date or when a preestablished origination volume has been reached, whichever occurs earlier. If the creditor extends the program beyond the plan's date, it must document the extension.

Description of Analysis

The Commentary for Regulation B specifies that a written plan ''must contain information that supports the need for the particular program.''[24] To that end, the plan must describe or incorporate the analysis determining the program is needed. A creditor can conduct a broad analysis using its own research or outside data, such as Home Mortgage Disclosure Act (HMDA) data, the Federal Reserve Board's small business credit survey, or other government or academic reports.

For example, a creditor could review the HMDA data of all lenders in its assessment area. If only a small number of residential mortgages were originated to Hispanic consumers, it could conduct further research to determine why. If the research revealed, for example, that applications were disproportionately denied because applicants' credit scores were below the minimum cutoff, the creditor could consider creating an SPCP targeting these consumers using alternative credit data to qualify them. Lenders can review the 2019 Interagency Statement on the Use of Alternative Data in Credit Underwriting and the Federal Reserve Board's Consumer Affairs letter 19-11 for more information.[25]

Nexus to the Organization's Customary Credit Standards

A key aspect of the written plan is establishing that "a class of persons would otherwise be denied credit or would receive it on less favorable terms" under the creditor's existing credit standards.[26] The plan must show a connection between the research or data showing the need for an SPCP and that a class of persons would not likely qualify under existing standards or would qualify on less favorable terms than those offered to other applicants.

To use the prior example, the creditor might find after reviewing its adverse action notices that its credit score minimum of 700 for purchase mortgage originations disproportionately resulted in denials of applications from Hispanic applicants, and that using alternative credit data would likely increase the number of approvals.

The AO included this additional example: A creditor identifies a class of applicants without enough savings to qualify for a mortgage loan (or qualify on less favorable terms) and will offer them down payment assistance funds under an SPCP. The plan could document that it previously denied mortgage applications to members of the targeted class because they had insufficient cash, so the SPCP would make them more likely to qualify.

REQUESTS FOR AND USE OF INFORMATION

As noted previously, creditors may be concerned that collecting prohibited basis information on a targeted group (e.g., Hispanics in low-income census tracts in Pennsylvania) could violate the ECOA and the FHA. The AO addresses this issue:

> If participants in a special purpose credit program … are required to possess one or more common characteristics (for example, race, national origin, or sex) and if the program otherwise satisfies the requirements of [Regulation B], ***a creditor may request and consider information regarding the common characteristic(s) in determining the applicant's eligibility for the program***.[27]

However, if the SPCP has not yet been established, a creditor cannot request demographic information that it is otherwise prohibited from collecting.[28] Instead, the creditor may use statistical methods to estimate demographic characteristics. Similarly, before the SPCP is established, the creditor may not collect demographic information for the preliminary analysis.

Once the SPCP is established, a creditor may collect information about common characteristic(s) to determine the applicant's eligibility for the program. The AO provides this example: A creditor's SPCP requires an applicant to reside in a low- to moderate-income census tract and be Black, Hispanic, or Asian. The creditor could request race or ethnicity information from applicants to confirm eligibility for this program.[29]

DISCRIMINATION AMONG MEMBERS OF THE TARGETED CLASS OF PERSONS PROHIBITED

While an SPCP may target a class of persons on a prohibited basis, *it cannot discriminate on a prohibited basis among members of that class*. For example, it could not charge different interest rates to members of the targeted class, based solely on their gender.[30]

NOTICE REQUIREMENTS FOR ACTION TAKEN

As noted previously, a creditor may deny an application because the applicant is not a member of the class of persons that the SPCP targets.[31] However, the creditor is still required to provide an adverse action notice to the applicant.[32]

SPCP EXAMPLES

Following the Bureau's guidance on the requirements for a compliant SPCP, HUD's guidance on the FHA and SPCPs, and the interagency statement, several banks have recently announced SPCPs. These include:

- eliminating a down payment requirement and closing costs for first-time home buyers in certain markets with large populations of Blacks and Hispanics.[33]
- allowing low down payments, eliminating mortgage insurance requirement, and increasing lender-paid assistance programs in majority Black and Hispanic census tracts in Los Angeles. The same lender has another SPCP to make it easier for small businesses owned by women, minorities, and veterans to qualify for loans by lowering its threshold for credit scores and other underwriting variables and by relying more heavily on cash flow analysis, an alternative credit data tool.[34]
- identifying existing minority mortgage home borrowers with the bank who would benefit from refinancing their loan at a lower rate.[35]
- providing a $5,000 lender credit and more flexible underwriting standards for mortgage loans in Black and Hispanic communities the bank serves.[36]

SPCPs AND THE COMMUNITY REINVESTMENT ACT

The Community Reinvestment Act (CRA) does not currently address whether an SPCP loan could qualify for CRA credit. However, in the CRA interagency rulemaking proposal issued in June 2022, the agencies solicited comment on this issue in Question 106: "Should special purpose credit programs meeting the credit needs of a bank's assessment areas be included in the regulation as an example of loan product or program that facilitates home mortgage and consumer lending for low- and moderate-income individuals?"[37]

SPCPs and the GSEs

Freddie Mac and Fannie Mae, the two government-sponsored enterprises, recently published their plans to develop and implement SPCPs, including purchasing loans from lenders issued under an SPCP.

Freddie Mac

Freddie Mac announced its "commitment to fully explore the use of the Special Purpose Credit Program framework to expand access to mortgage funding for traditionally

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Special Purpose Credit Program Requirements

Written Plan Requirements:	• identify the class of persons the program is intended to benefit, • specify the procedures and standards for extending credit under it, and • list either the SPCP's duration or when it will be reevaluated to determine whether to continue it.
Class of Persons the Program Intends to Benefit	The SPCP must target a class of persons ''who would otherwise be denied credit or would receive it on less favorable terms" and explain if the targeted class will be required to demonstrate a financial need and/or share a common characteristic. Examples: • Minority residents of low- to moderate-income census tracts • Residents of majority-Black census tracts • Operators of small farms in rural counties • Minority- or women-owned small business owners • Consumers with limited English proficiency or residents living on tribal lands
Procedures and Standards	Specify procedures and standards for extending credit designed to increase chances that: • a class of persons who would otherwise likely be denied credit will receive it under the program, or • a class of persons who would likely otherwise receive credit on less favorable terms will receive it on more favorable terms under the program. A creditor can: • modify its existing loan standards; • introduce a new product or service; • adjust the terms/conditions for existing product/service; or • modify policies and procedures for loss mitigation programs.
Program Duration/ Reevaluation	The plan must specify the SPCP's duration or when it will reevaluate whether to continue it.
Description of Analysis	Describe the analysis determining the need for program using its own research or outside data.
Nexus to the Organization's Customary Credit Standards	Plan must show connection between the need for an SPCP with a class of persons not likely to qualify under creditor's existing standards or qualifying on less favorable terms.
Requests for and Use of Information	If the SPCP requires a common characteristic (such as race) and the program otherwise satisfies the requirements for an SPCP, a creditor may request data on common characteristics. See Comment 8(c)-1. But if the SPCP is not yet established, a creditor cannot request information on race, color, religion, national origin, or sex. See §1002.5(b).

underserved minority communities."[38] This includes:

- purchasing SPCP loans
- offering a Freddie Mac SPCP, and
- developing a geotargeted approach to SPCPs, such as targeting majority–minority census tracts.[39]

Fannie Mae

Fannie Mae announced in its Equitable Housing Finance Plan[40] that it is planning the following SPCP activities:

- Announcing its "objective to make our purchase of SPCP loans as routine as any other loans we currently buy."[41]
- Launching three-to-five SPCP pilots that include:
  - expanding its down payment assistance program;
  - exploring ways to reduce hurdles for lenders to participate in SPCPs;
  - creating SPCP pilots to reduce borrower closing costs for Black home buyers via appraisal products, appraisal reimbursements, and/or title products; and
  - testing add-on features for SPCP pilots aimed at strengthening borrower stability to address unexpected expenses or temporary disruptions to income.

THE FAIR HOUSING ACT AND SPCPs

HUD's Office of General Counsel Guidance

As noted previously, SPCPs have not been widely implemented despite their availability since 1976. This reflects two possible concerns: 1) creditors want greater clarity about the requirements under §1002.8 for implementing a compliant SPCP to ensure they do not violate the ECOA, and 2) creditors are uncertain if SPCPs comply with the Fair Housing Act, which prohibits discrimination in housing on a prohibited basis.[42] The concern is that while the ECOA specifically permits SPCPs, the FHA is silent on this issue.

HUD issued an Advisory Opinion in December 2021 to specifically clarify that the FHA generally does not prohibit an SPCP that complies with the ECOA.[43] In support, the opinion noted the rule of construction that similar statutes should be interpreted similarly. Since both the ECOA and the FHA are laws prohibiting "certain discriminatory conduct and encouraging affirmative conduct to address long unmet needs and disparities," the opinion concluded they should be interpreted harmoniously. The opinion also noted that the U.S. Department of Justice, which is charged with enforcing both laws, has approved the use of SPCPs to remediate discrimination in enforcement actions for violations of both laws. The opinion therefore concluded that:

> While the [FHA] and ECOA regulate overlapping but different types of credit activity and entities, the statutes are complementary and should generally be harmonized. Accordingly, a nonprofit organization's Special Purpose Credit Program established to serve an economically disadvantaged class of persons or a for-profit institution's Special Purpose Credit Program designed and implemented in compliance with ECOA and Regulation B generally do not violate the Act.[44]

After HUD's general counsel confirmed that the SPCPs do not generally violate the FHA, HUD's Office of Fair Housing and Equal Opportunity (FHEO) issued guidance encouraging lenders to use SPCPs:

> With those legal concerns addressed, FHEO encourages lenders to seriously consider establishing Special Purpose Credit Programs that are consistent with the antidiscrimination and affirmative provisions of the Equal Credit Opportunity Act, Regulation B, and the Fair Housing Act. Such programs, if constructed thoughtfully and in accordance with the Bureau's regulations and guidance, can be a significant step towards bridging the racial and ethnic homeownership and wealth gaps that exist throughout the United States.[45]

THE INTERAGENCY STATEMENT ON SPCPs

After the Bureau and HUD issued their SPCP guidance, the federal banking agencies, Bureau, and other federal agencies issued an interagency statement encouraging the use of SPCPs: "As creditors consider how they may expand access to credit to better address special social needs, the agencies encourage creditors to explore opportunities to develop special purpose credit programs consistent with ECOA and Regulation B requirements as well as applicable safe and sound lending principles."[46]

CONCLUSION

SPCPs provide a framework for financial institutions to create credit programs to help address special social needs while complying with federal fair lending laws. SPCPs have not been widely implemented because of creditors' regulatory concerns. Now that the Bureau and HUD have issued guidance addressing these specific concerns, and an interagency statement has been issued encouraging creditors to consider offering SPCPs, creditors may consider revisiting these programs. While regulators cannot approve or provide a safe harbor for any particular program, we welcome you to raise specific questions and concerns with your primary regulator. ■

Endnotes*

1 Aditya Aladangady and Akila Forde, "Wealth Inequality and the Racial Wealth Gap," Federal Reserve Board, October 21, 2021; Ana H. Kent, Nikki Lanier, David F. Perkis, and Claire James, "Examining Racial Wealth Inequality," Federal Reserve Bank of St. Louis, March 2022; Benjamin Harris and Sydney Schreiner Wertz, "Racial Differences in Economic Security: The Racial Wealth Gap," U.S. Department of the Treasury, September 15, 2022.

2 See ECOA: 15 U.S.C. §1691(a); 12 C.F.R. §1002.4(a); FHA: 42 U.S.C. §§3604-3606; 24 C.F.R. Part 100.

3 See 12 C.F.R. §1002.5(b). The preamble to the *Federal Register* notice clarified this requirement: "[I]f creditors cannot inquire about or note applicants' personal characteristics, such as national origin or race, they are less likely unlawfully to consider the information in connection with a credit transaction." See 68 *Federal Register* 13144, 13147 (March 18, 2003).

4 See 12 U.S.C. §1691(c); 12 C.F.R. §1002.8(b)(2).

5 See Comment 8(c)-1: "This section permits a creditor to request and consider certain information that would otherwise be prohibited by §§1002.5 and 1002.6 to determine an applicant's eligibility for a particular program."

6 See 15 U.S.C. §1691(c): "It is not a violation of this section for a creditor to refuse to extend credit offered pursuant to … [an SPCP] *if such refusal is required by or made pursuant to such program*." (Emphasis added); S. Rept. 94–589, 94th Congress, 2nd Session, reprinted in 1976 U.S.C.C.A.N. 403, 408. "[Subsection 701(c) makes it clear that denials of credit to persons ineligible for those programs does not violate this Act."

7 See Equal Credit Opportunity Act Amendments of 1976, Pub. L. 94-23, 90 Stat. 251, March 23, 1976.

8 See "FHEO's Statement by HUD's Office of Fair Housing and Equal Opportunity on Special Purpose Credit Programs as a Remedy for Disparities in Access to Homeownership," December 7, 2021: "But very few [SPCPS] have been established [since 1976] to create homeownership opportunities for affected communities."

9 See Endnote 8, p. 2–3: "When asked why they have not previously established Special Purpose Credit Programs, some lenders told HUD and other federal agencies that they are willing to establish such Programs to improve homeownership opportunities for racial and ethnic groups who have been underserved historically, but that they are worried that those Programs may run afoul of the Fair Housing Act and other federal anti-discrimination laws."

10 See 86 *Federal Register* 3762, 3763 (January 15, 2021).

11 See "Interagency Statement on Special Purpose Credit Programs Under the Equal Credit Opportunity Act and Regulation B," February 22, 2022.

12 Damon Smith, Office of General Counsel Guidance on the Fair Housing Act's Treatment of Certain Special Purpose Credit Programs That Are Designed and Implemented in Compliance with the Equal Credit Opportunity Act and Regulation, December 6, 2021.

13 See 12 U.S.C. §1691(c): "It is not a violation of this section for a creditor to refuse to extend credit offered pursuant to … [an SPCP] *if such refusal is required by or made pursuant to such program*." (Emphasis added).

14 See Senate Report 94–589, 1976 U.S.C.C.A.N. at 409.

15 See 12 C.F.R. §1002.8(a)(3).

16 See 12 C.F.R. §1002.8(a)(3); 86 *Federal Register* at 3764-65.

17 See Comment 8(a)-5.

18 See 86 *Federal Register* at 3765.

19 See 12 C.F.R. §1002.8(a)(3).

20 See 87 *Federal Register* at 3765.

21 See 87 *Federal Register* at 3765.

22 See 87 *Federal Register* at 3765.

23 See Comment 8(c)-1.

24 See Comment 8(a)-5.

25 See https://www.federalreserve.gov/supervisionreg/caletters/caltr1911.htm/.

26 See Comment 8(a)-5.

27 See 86 *Federal Register* at 3764.

28 See 86 *Federal Register* at 3766.

29 See 86 *Federal Register* at 3764.

30 See 12 C.F.R. §1002.8(b)(2). *See United States v. Am. Future Sys., Inc.*, 743 F.2d 169, 175 (3d Cir. 1984) (finding lender's SPCP violated ECOA because while it permissibly targeted a group of borrowers based on their age, it discriminated on a prohibited basis *among members of that group*).

31 See 15 U.S.C. §1691(c).

32 See Comment 8(b)-1: "A creditor that rejects an application because the applicant does not meet the eligibility requirements (common characteristic or financial need, for example) must nevertheless notify the applicant of action taken as required by §1002.9."

33 See "Bank of America Introduces Community Affordable Loan Solution to Expand Homeownership Opportunities in Black/African American and Hispanic-Latino Communities," August 30, 2022.

34 See David Benoit and AnnaMaria Andriotisc, "Citigroup Joins Industry Effort to Lend to People Without Credit Scores," *Wall Street Journal,* September 3, 2022; see also "The Forum File, 2022 Edition #4," September 7, 2022, discussing Citi's SPCPs. The use of cash flow analysis is discussed on p. 2 of the 2019 *Interagency Statement on the Use of Alternative Data in Credit Underwriting:* "The evaluation of a borrower's income and expenses to help determine repayment capacity is a well-established part of the underwriting process. Improving the measurement of income and expenses through cash flow evaluation may be particularly beneficial for consumers who demonstrate reliable income patterns over time from a variety of sources rather than a single job. Cash flow data are specific

Endnotes Continued*

to the borrower and generally derived from reliable sources, such as bank account records, which may help ensure the data's accuracy."

35 See "Wells Fargo Expands Efforts to Advance Racial Equity in Homeownership," April 13, 2022.

36 See "TD Bank Introduces New Mortgage Loan Product Designed for Minority Communities," March 2, 2022.

37 See 87 *Federal Register* 33884, 33968 (June 3, 2022).

38 See "Freddie Mac Announces Landmark Equitable Housing Finance Plan," June 8, 2022.

39 See *Freddie Mac Equitable Housing Plan,* p. 17.

40 See *Fannie Mae Equitable Housing Finance Plan*, p. 10.

41 See *Fannie Mae Equitable Housing Finance Plan*, p. 10.

42 See Endnote 11, Brad Finkelstein, "What's Next for Special Purpose Credit Programs?" *National Mortgage News*, December 10, 2021.

43 See Endnote 12.

44 See Endnote 12.

45 See Endnote 8, p.3.

46 See CA letter 22-2: Interagency Statement on Special Purpose Credit Programs Under the Equal Credit Opportunity Act and Regulation B, February 22, 2022, p. 2.

* 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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Federal Reserve Board Consumer Affairs Letters for 2022 and 2021

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. When the same issue is also addressed in a Supervision and Regulation (SR) letter, the SR letter is also noted.

CA 22-10 / SR 22-10	Inactive Supervisory Guidance
CA 22-9	Revised Federal Debt Collection Practices Act Examination Procedures
CA 22-8 / SR 22-9	FedEZFile™ and FedEZFile Fluent™ to be Released for Filing Applications with the Federal Reserve
CA 22-7 / SR 22-7	Policy Statement on Whistleblower Claims
CA 22-6 / SR 22-6	Engagement in Crypto-Asset-Related Activities by Federal Reserve-Supervised Banking Organizations
CA 22-5	Standard Information Request (SIR) Process
CA 22-4	Revised "A Guide to HMDA Reporting: Getting It Right!"
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 Board of Governors of the Federal Reserve System (Board) issues a final rule to amend Regulation II to clarify the prohibition on network exclusivity. On October 11, 2022, the Board issued a final rule amending Regulation II (12 C.F.R., part 235), the Board's implementing regulation for §920 of the Electronic Fund Transfer Act (EFTA). The Dodd–Frank Act added §920 (commonly known as the Durbin Amendment) to the EFTA to regulate interchange fees for electronic debit card transactions and the networks available to process them with the goal of reducing the cost of transaction fees for merchants.

Section 920(b)(1)(B) of the EFTA directed the Board to issue regulations prohibiting issuers or networks from inhibiting the ability of a merchant or its acquirer to choose among the available networks to process a debit card transaction. Without this restriction, merchants or their acquirers might not be able to select a network with lower fees. Section 902(b)(1)(A) of the EFTA requires issuers to provide at least two unaffiliated payment card networks to process electronic debit transactions and prohibits issuers from inhibiting merchants' ability to direct the network through which a transaction is routed.

On July 20, 2011, the Board issued a final rule to implement §920 of the EFTA, including a prohibition on network exclusivity in 12 C.F.R. §235.7(a). However, the technology to process card-not-present (CNP) transactions was not yet widely deployed in 2011. Since then, most networks have introduced the technical capability to process these transactions. Additionally, the volume of CNP transactions has increased from 10 percent of all debit card transactions in 2011 to 23 percent in 2019.

In analyzing the market since enacting the 2011 rule, the Board found that some issuers were not providing two unaffiliated networks to process CNP transactions. The amendment is designed to address this issue by clarifying that issuers must provide at least two unaffiliated networks through which CNP transactions can be processed. The rule also includes restrictions in §235.7(a) to prevent issuers from circumventing these requirements. The Board explained that certain issuers are actively disabling or failing to enable the CNP capabilities of one or more enabled networks, resulting in fewer than two unaffiliated networks to process CNP transactions. The rule is effective July 1, 2023.

Fannie Mae launches initiative to accelerate multifamily positive rent reporting to help borrowers build credit. Under its Multifamily Positive Rent Payment Reporting pilot program, Fannie Mae is partnering with three fintech providers to collect renter payment history from multifamily property owners and landlords and transmit such information to the three national consumer reporting agencies (Equifax, Experian, and TransUnion). The credit bureaus will include this positive rent payment history in the consumer's credit report. Fannie Mae noted that about 20 percent of the U.S. population has little or no credit history, and rent payments are generally not reported to the credit bureaus. Fannie Mae also noted that sufficient credit history helps renters increase their credit scores, which in turn can improve access to a broader range of housing and the ability to qualify for credit products. For the first year of the program, Fannie Mae will pay the designated vendors' fees charged to the property owners for collecting and transmitting the data.

The Consumer Financial Protection Bureau (Bureau) issued Circular 2022-07 concerning consumers' disputes of their credit report. On November 10, 2022, the Bureau issued Circular 2022-07 to provide guidance on the duties of consumer reporting agencies (CRAs) and furnishers to investigate consumer disputes of information in their credit report. Because consumer credit reports can affect applications for credit, leasing, employment, and insurance, §611 of the Fair Credit Reporting Act (FCRA) requires consumer reporting agencies, as well as furnishers of credit report information, to investigate consumers' disputes of information in their report.

Despite this requirement, the Bureau found that credit report errors and the challenges in correcting them continue to be an issue. The Bureau received more than 500,000 complaints about credit or consumer reporting during the first nine months of 2021, with errors topping the list of complaints. The Bureau issued this circular to provide guidance to agencies charged with enforcing federal consumer protection laws and help promote compliance with §611. The circular provides guidance on two questions:

1. *Are consumer reporting agencies and the entities that furnish information to them (furnishers) permitted under the Fair Credit Reporting Act (FCRA) to impose obstacles that deter submission of disputes?*

   No. Consumer reporting agencies and furnishers are liable under the FCRA if they fail to investigate any dispute that meets the statutory and regulatory requirements, as described in more detail below. Enforcers may bring claims if consumer reporting agencies and furnishers limit consumers' dispute rights by requiring any specific format or by requiring any specific attachment such as a copy of a police report or consumer report beyond what the statute and regulations permit.

2. *Do consumer reporting agencies need to forward consumer-provided documents attached to a dispute to furnishers?*

   It depends. Enforcers may bring a claim if a consumer reporting agency fails to promptly provide the furnisher with "all relevant information" regarding the dispute that the consumer reporting agency receives from the consumer. While there is not an affirmative requirement to specifically provide original copies of documentation submitted by consumers, it would be difficult for a consumer reporting agency to prove it provided all relevant information if it fails to forward even an electronic image of documents that constitute a primary source of evidence.

Bureau issues outline of its approach to the §1033 rulemaking. On October 27, 2022, the Bureau released a summary of the outline of proposals it is considering to regulate consumers' right to access their personal financial data. Section 1033(a) of the Dodd–Frank Act authorizes the Bureau to issue regulations requiring financial institutions to provide account data to consumers upon request. The rulemaking will affect the growing use of this data by fintech companies and others. For example, consumers can sign up with data aggregators to collect and aggregate their financial account information so consumers can see their financial picture in one place.

Similarly, algorithms have been developed that analyze consumer bank account transaction data to evaluate consumers' creditworthiness. But before the Bureau can issue regulations to implement §1033, it is required under the Small Business Regulatory Enforcement Fairness Act (SBREFA) to consult with a panel of small businesses representatives about the likely impact of the regulations on small entities. In October, the Bureau released an outline of proposals it is considering for the §1033 rulemaking. The proposals would address the following topics:

- the data providers who would be subject to the rule
- the recipients of information
- the types of information that would need to be available
- how and when information would need to be available
- third-party obligations
- record-retention obligations, and
- implementation period

Following the conclusion of the SBREFA process, the Bureau can begin drafting a rulemaking proposal.

The Board expects to launch its FedNow payment service in 2023. On August 29, 2022, the Board announced that it expects to launch its FedNow payment service between May and July 2023. FedNow is the Federal Reserve's service for participating financial institutions that will allow consumers and businesses to instantly transfer payments at any time on any day. For example, a consumer could initiate a payment to a repairman from the consumer's bank account to the repairman's bank account at another institution that would be received instantly.

Currently, payment transfers through the Automated Clearing House typically settle within one-to-three business days. Payment recipients will have full access to the funds immediately, providing greater flexibility to manage time-sensitive payments. More than 120 organizations are now participating in the pilot program. This announcement follows the June 6, 2022, final rule the Board issued to provide the legal framework for FedNow.

Board issues guidance to Federal Reserve-Supervised Banking Organizations Engaging in Crypto-Asset-Related Activities. On August 16, 2022, the Board published Consumer Affairs letter 22-6/Supervision Regulation letter 22-6 to provide guidance on the Board's expectations for the institutions it supervises regarding crypto-asset activities. The letter notes that the emerging cryptosector provides opportunities for financial institutions but also poses risks, including compliance risk. "Crypto-assets pose significant consumer risks such as those related to price volatility, misinformation, fraud, and theft or loss of assets. In addition, banking organizations engaging in crypto-asset-related activities face potential legal and consumer compliance risks stemming from a range of issues, including, for example, uncertainty regarding the legal status of many crypto-assets." The letter also discusses risks in technology and operations, anti-money laundering, and financial stability.

The letter encourages any Federal Reserve-supervised banking organization engaging or seeking to engage in crypto-asset–related activities to notify its lead supervisory contact at the Federal Reserve and to have in place adequate systems, risk management, and controls to conduct such activities in a safe and sound manner and consistent with applicable laws. Supervised institutions must also determine, before engaging in a crypto-asset–related activity, that it is legally permissible and whether any filings are required under applicable federal or state laws.

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

On the Docket: Recent Federal Court Opinions*

Fifth Circuit holds that the Consumer Financial Protection Bureau's funding structure is unconstitutional and vacates the payday lending rule. *Community Financial Services Ass'n of Am. v. CFPB*, 51 F.4th 616 (5th Cir. 2022). In 2017, the Consumer Financial Protection Bureau (Bureau) issued a final rule to impose underwriting requirements and payment restrictions on payday, vehicle title, and certain high-cost loans using its authority to regulate unfair, deceptive, or abusive acts or practices. The Bureau later rescinded the underwriting requirements but retained the provision prohibiting a lender from attempting to initiate a payment transfer for covered loans after two previous consecutive failed attempts, unless the lender obtains the consumer's new and specific authorization. Two trade groups filed a lawsuit alleging this provision was invalid because the Bureau's structure of a sole director and funding outside the congressional appropriations process is unconstitutional and because the final rule exceeded its authority and violated the Administrative Procedure Act (APA). The court upheld the Bureau's finding that initiating a payment transfer was unfair after two failed, consecutive attempts and also rejected arguments the rulemaking was arbitrary and capricious under the APA. However, the court found the Bureau's funding structure was unconstitutional.

The appropriations clause of the Constitution provides: "No money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law …" The Dodd–Frank Act funds the Bureau outside of the appropriation process by directing the Federal Reserve Board (Board) to pay the Bureau's annual budget request provided it does not exceed 12 percent of the Board's operating expenses. The court determined this funding mechanism, which the court stated was double-insulated because the Board is also funded outside the appropriations process, deprives Congress of the power of the purse and thus violates the separation of powers doctrine and the appropriations clause. While the court acknowledged other federal regulatory agencies are funded outside of the appropriations process, it distinguished the Bureau because of its unique powers, including a single director answerable to the President and broad rulemaking and enforcement authority. The court also noted that the Federal Reserve, unlike the Bureau, is still "tethered" to the Treasury, based on a requirement to remit funds above a statutory limit. Because the court found the Bureau's funding structure was unconstitutional, it vacated the payday lending rule. In November 2022, the Bureau petitioned the Supreme Court to review this decision, which conflicts with other federal court cases on this issue.

Second Circuit holds the National Bank Act preempts a New York law requiring that interest be paid on residential mortgage escrow accounts. *Cantero v. Bank of America*, 49 F.4th 121 (2d Cir. 2022). At issue in this case was the New York General Obligations Law (NY GOL) §5-601 that required lenders to pay a minimum of 2 percent interest on mortgage escrow accounts. Two separate class-action lawsuits alleged Bank of America (BOA) violated this New York law by not paying interest on the plaintiffs' escrow accounts. BOA filed a motion to dismiss, arguing the National Bank Act (NBA) preempts NY GOL §5-601 for national banks, which the lower court denied.

On appeal, the Second Circuit reversed and remanded the case finding that the NBA preempts NY GOL §5-601 because it exerts control over the power of national banks to create and fund mortgage escrow accounts. The court noted its conclusion is consistent with prior statements of New York bank regulators stating that NY GOL §5-601 is preempted, as well as the Office of the Comptroller of the Currency, which had issued an administrative rule in 2004 purporting to preempt state interest on escrow account laws. The court also found that a Dodd–Frank Act provision requiring mandatory escrows for higher-priced mortgage loans mortgages — and allowing such accounts to be subject to state escrow interest laws — did not mean that Congress intended to subject all mortgage lenders to state escrow interest laws.

Eighth Circuit affirms dismissal of Fair Credit Reporting Act lawsuit because plaintiff failed to establish damages. *Peterson v. Equifax Info. Services,* 44 F.4th 1124 (8th Cir. 2022). The plaintiff filed a Chapter 7 bankruptcy in March 2019 and obtained a discharge order several months later. Her bankruptcy included a credit card debt of $2,349. On August 30, 2019, the plaintiff obtained her Experian credit report, which showed her bankruptcy and discharge but still listed the credit card debt with an outstanding balance of $2,481 that was 90 days late. In October 2019, Experian updated her report to list the debt as discharged with a zero balance.

The lawsuit alleged Experian violated §607(b) of the Fair Credit Reporting Act (FCRA) by not timely updating her report, which caused her credit card application to be denied. The district court dismissed the lawsuit because she failed to establish any damages. On appeal, the Eighth Circuit affirmed. The court noted she testified at deposition that her credit card application was denied because of the bankruptcy. But when Experian filed a motion for summary judgment, she submitted an affidavit indicating her application was denied because of the erroneous information in her credit report. The court indicated a litigant cannot contradict prior sworn testimony with a subsequent contradictory affidavit. "If testimony under oath. …can be abandoned many months later by the filing of an affidavit, probably no cases would be appropriate for summary judgment."

The court also noted that she applied for a credit card again with the same issuer after her report was corrected, but her application was still denied. The plaintiff also alleged she suffered emotional distress, but the court said she failed to produce evidence of a genuine injury, such as a physical injury, medical treatment for psychological or emotional injury, or witnesses to corroborate emotional distress. The court therefore affirmed the lower court's dismissal of the case.

Sixth Circuit reviews standards for reasonable procedures to ensure accuracy of consumer reports. *Hammoud v. Experian Information Services, LLC,* 52 F.4th 669 (6th Cir. 2022). Ahmed Hammoud filed for Chapter 7 bankruptcy in 2009, and his father, Mohamad Hammoud (also known as Ahmed Mohamad Hammoud) filed for bankruptcy with his wife in 2010. The father's petition inadvertently used the son's Social Security number (SSN).

LexisNexis, a data collector, reported the bankruptcies to Experian. Because Experian's systems rely on SSNs, both bankruptcies were populated in the son's credit report history. The error was corrected with the bankruptcy court the next day, but it remained on the son's credit report for nine years. When the son attempted to refinance his mortgage loan in 2019, he learned that his credit report listed both bankruptcies.

On August 13, 2019, he disputed the second bankruptcy, and Experian removed it on August 28, 2019. The son's lawsuit alleged Experian violated §607(b) of the FCRA by including inaccurate information in his credit report from LexisNexis. The court noted that consumer reporting agencies are permitted to gather information from reliable third parties. LexisNexis is known to be reliable, and Experian periodically audits the information LexisNexis provides.

The son also argued that Experian should have reviewed the docket entries to see that the father's SSN on his bankruptcy had been updated. But the court held that "Section 1681e(b) does not require credit reporting agencies to investigate information to that degree, unless and until the consumer has alerted it to an inaccuracy." Once the son disputed the information, his credit report was promptly corrected. Accordingly, the court concluded that "Experian's processes strike the right balance between ensuring accuracy and avoiding 'an enormous burden' on consumer credit reporting agencies."

Seventh Circuit holds that a bank's account agreement permitted it to use the available balance method to calculate nonsufficient funds fees. *Page v. Alliant Credit Union,* 52 F.4th 340 (7th Cir. 2022). The plaintiff's class-action lawsuit alleged a credit union violated the account agreement by using the available balance, instead of the ledger balance, to determine if her account was overdrawn and subject a nonsufficient funds (NSF) fee for a debit transaction. The ledger balance is based on the balance when a transaction is submitted but does *not* consider authorized transactions that have not yet settled, while the available balance includes holds on deposits and transactions that have been authorized but not yet settled. The lawsuit alleged multiple NSF fees were improperly charged for the same transaction because her account had sufficient funds based on the ledger balance. The lower court dismissed the case, which the Seventh Circuit affirmed on appeal.

The plaintiff asserted that the agreement's use of different phrases in describing withdrawal restrictions (sufficient available funds) and fee provisions (insufficient funds) meant the available balance only applied to the withdrawal restrictions, while the ledger balance applied for purposes of assessing fees. However, the court noted that the agreement permits a fee when it restricts withdrawals in stating that "*Checks or other transfer or payment orders which are drawn against insufficient funds may be subject to a service charge as set forth in the Fee Schedule.*" (Emphasis in original). The court stated that the contract should be construed based on how a reasonable person would understand it and that it was implausible for a reasonable person to think that the agreement used two different methods of calculating the account balance in consecutive sections without the agreement expressly saying so.

The plaintiff also argued it was ambiguous whether her agreement disclosed the use of the available balance method because other institutions more clearly disclose its use in their account agreements. But the court disagreed, finding "that some institutions disclosed that they used the available balance method differently or more clearly does not prove that the Agreement promised to use the ledger-balance method or that the Agreement is ambiguous."

Finally, the plaintiff argued that the agreement did not permit multiple NSF fees when one transaction is represented multiple times. However, the court noted the agreement refers to "checks, ACH debits, debit card transactions, fees or other posted items," which showed that items can include ACH debits where a payee, rather than the member, debits the member's account. Consequently, the court held that the fee schedule permits a fee each time a payee attempts to make an ACH debit from an account with insufficient funds and the district court correctly dismissed the plaintiff's multiple-fees theory.

* 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
01/01/23	Reg. Z	Final rule establishing loan exemption threshold for appraisals of higher-priced mortgages for 2022
01/01/23	Regs. M and Z	Final rules establishing dollar thresholds for credit exempt from Regulations M and Z
07/25/22	Reg. V	Final rule prohibiting furnishing consumer reports containing adverse information in cases of human trafficking
06/03/22	Reg. BB	Agencies issue rulemaking proposal to modernize their implementing regulations for the Community Reinvestment Act
05/31/22	Reg. H	Agencies release revised interagency questions and answers regarding flood insurance
04/13/22	N/A	Agencies propose changes to their Uniform Rules of Practice and Procedure
04/01/22	Reg. Z	Final rule amending Regulation Z to facilitate the transition from the LIBOR interest rate index

REGULATORY CALENDAR

EFFECTIVE DATE OR PROPOSAL DATE†	IMPLEMENTING REGULATION	REGULATORY CHANGE
01/01/22	Reg. C	Final rule establishing 200 loans as the permanent Home Mortgage Disclosure Act data reporting threshold for open-end lines of credit
11/30/21	FDCPA	Final rule creating implementing regulations for the Fair Debt Collection Practices Act
09/01/21	Reg. B	Rulemaking proposal under §1071 of the Dodd–Frank Act for data collection and reporting of 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 and risk management
06/23/21	MLA	Consumer Financial Protection Bureau's interpretive rule for authority to conduct Military Lending Act examinations
05/10/21	N/A	Federal Reserve Board's statement on the role of supervisory guidance

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

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