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Re: Proposed CDFI Program–Certification Application and Annual Reporting

I. Introduction and Overview

The **Center for Responsible Lending**, **Self-Help Credit Union**, **Self-Help Federal Credit Union**, and **Self-Help Ventures Fund**, the latter three all CDFIs and all four related to the Center for Community Self-Help (collectively, Self-Help), appreciate the opportunity to comment on the CDFI Fund (Fund)'s proposed revisions to the CDFI certification and reporting requirements. For 40 years, Self-Help has created asset-building opportunities for low-income individuals, rural communities, women, and families of color. In total, Self-Help has provided over $9 billion in financing to 172,000 homebuyers, small businesses, and nonprofit organizations and serves more than 154,000 mostly low-income families through 62 credit union branches in North Carolina, California, Florida, Illinois, South Carolina, Virginia, and Wisconsin.

We welcome the Fund's efforts to more vigorously ensure that the primary mission of any CDFI is to promote community development. To that end, **we urge the Fund to establish lending standards that function as clear, bright-line eligibility requirements for CDFI certification or renewal:**

(1) **a fee-inclusive annual percentage rate (APR) limit of 36%, computed consistent with the current Military Lending Act regulations (or lower if required by state law)**;[1] and

(2) **for any mortgages offered, product protections consistent with the qualified mortgage (QM) statutory protections**: (a) no negative amortization, interest-only payments, or balloon payments; (b) adjustable rate mortgages underwritten at the maximum rate in the first five years; (c) original maximum term of 30 years; and 4) total points and fees generally not exceeding three percent of the loan amount. These product protections will help ensure responsible mortgage lending while allowing innovation in underwriting that may benefit communities that CDFIs serve.

We further urge the Fund to **require that lenders assess borrowers' ability-to-repay** and **monitor other lending metrics like defaults, refinancings, and debt collection practices**. For mortgage loans, although CDFIs are exempt by regulation from the ability-to-repay provisions of the Dodd-Frank Act, CDFIs should still demonstrate that they consider and verify borrower debts, income, and assets.

Moreover, we urge the Fund to **evaluate an institution's fair lending record** in advance of certification, particularly compliance with the Equal Credit Opportunity Act and Fair Housing Act.

In addition, we urge the Fund to **establish an eligibility requirement that CDFIs charge no more than six overdraft fees in a rolling 12 months**, consistent with the FDIC's 2010 guidance addressing overdraft programs.

We also strongly support the Fund's proposal to **require that the primary mission test be applied as a whole to non-depository parents, affiliates, and subsidiaries engaged in financing.**

We support **the removal of geographic boundaries on most Target Market designations, while emphasizing that the eligibility requirements are critical to ensuring that CDFIs operating on any scale are promoting rather than eroding community development.** We further urge the Fund to **monitor the extent to which CDFIs with national Target Markets are responsibly reaching borrowers of color.**

Finally, we urge the Fund to **collect more robust race and ethnicity data with respect to CDFIs and the borrowers and communities they serve, as well as transaction level data for all CDFIs.**

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[1] As discussed in Section III, we also urge the Fund to require that non-bank CDFIs partnering with banks abide by the interest rate limits in the state where the borrower resides. And we encourage an exception from rate limits for federal credit unions whose only product exceeding this rate is the payday alternative loan (PAL).

CDFIs are uniquely suited to promote community development and expand financial inclusion. Too often, however, we see "financial inclusion" as the central purported justification for permitting irresponsible lending practices, unreasonably high rates, and erosion of longstanding consumer protections and fair lending requirements. It is becoming difficult to keep track of all the affirmatively harmful regulatory actions taken in recent years in the name of "access to credit" and "financial inclusion" – which in reality exacerbate *exclusion*. At present, we are particularly concerned about a growing push to "promote financial inclusion" by online consumer lenders that charge high interest rates, some of which scheming with banks to evade state interest rate limits – an essential protection against predatory lending.[2] At least one CDFI is charging rates as high as 190% APR. Moreover, in the mortgage space, we are concerned that some CDFI mortgage lenders are using the certification not to promote community development but to avoid the sensible underwriting requirements that apply to most non-CDFI lenders.

High-cost and/or unaffordable indebtedness and default inflict misery of all kinds on borrowers and their families,[3] ultimately leaving them worse off than when they started. Communities of color are targeted and disproportionately harmed by such lending, which exploits and fuels the racial wealth gap.[4]

We urge the Fund to put its imprimatur only on lending practices that, in the spirit of the CDFI mission, carry reasonable interest rates and promote asset building rather than saddling consumers with high-cost, harmful debt.

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[2] The OCC and the FDIC are taking a lead role in this effort despite their lack of authority to regulate non-banks. The OCC's fintech charter would enable non-banks to ignore state rate caps. It has been successfully challenged by New York in Federal District Court, though the OCC is appealing the decision to the Second Circuit. Both the OCC and FDIC recently issued final rules providing that non-bank assignees of bank loans can ignore state interest rate caps and continue charging whatever interest the bank charged. These rules are being challenged in court by a number of State Attorneys General. The OCC also last week finalized a rule that would enable non-banks to ignore state rate caps by laundering loans through banks. The rule attacks the centuries-old anti-evasion doctrine by providing that the "true lender" in a rent-a-bank scheme is the bank, so long as the bank's name is on the loan document. *See* Comments on the OCC's proposal to gut the true lender doctrine from a coalition of national consumer and civil rights groups, filed Sept. 3, 2020, at https://www.responsiblelending.org/research-publication/comment-occ-rule-would-allow-payday-lenders-use-rent-bank-schemes-evade-state.

[3] For discussion of financial impacts as well as growing research documenting health impacts of the high-cost debt treadmill, *see* Comments from CRL, NCLC and additional consumer and civil rights groups to the OCC at 39-42, filed Sept. 3, 2020, at https://www.responsiblelending.org/research-publication/comment-occ-rule-would-allow-payday-lenders-use-rent-bank-schemes-evade-state.

[4] *Id.* at 43-44.

II. Some CDFIs' current practices provide examples of what the CDFI Fund should clearly not support.

Consumer lending

Several CDFIs are engaged in lending at high rates and/or abusive debt collection practices. We provide these as clear examples of what the CDFI Fund should not permit. But we emphasize that many programs far less irresponsible than these outliers still would not satisfy the standards that CDFIs should uphold.

Fig Loans, which describes itself as the "first fintech" to receive CDFI certification, discloses an "example" APR of an extraordinary 190%.[5] The terms of its "Fig Loan" product range from $300-$750, from 4 to 6 months.[6] Fig Loans touts that it "provide[s] credit building alternatives to payday loans," and proudly shows the CDFI seal on its website. (See Appendix for a screenshot of the CDFI seal sharing a screen with a 190% APR loan.) There is no universe in which an entity charging 190% APR should have the imprimatur of the CDFI Fund.

Aura (formerly Insikt/Lendify) makes high-rate loans through finders. Aura charged between 40% and 69.99% APR on three-fourths of its loans in 2017.[7] Available loan performance data raise serious questions about the affordability of Aura loans. In 2017, 57% of Aura's average loans outstanding incurred a late fee, and those that were charged late fees incurred, on average, 4.5 late fees each. Aura charged off over 5,200 loans during 2017, or 15.8% of its average number of loans outstanding. Aura securitizes loans it brands as "social impact bonds."[8] Aura has also lobbied to weaken state usury laws – in California, Florida, and New York, for example – by pushing for exceptions that would allow it to lend at higher rates than the laws allow.

Aura's finder model also skirts broker laws in a number of states and encourages unaffordable lending. Aura pays these finders for marketing, brokering, and loan servicing. But these finders, though acting as brokers, are not licensed or regulated as brokers, even as they have access to a borrower's social security number, credit report, and other personal information. Aura also has pushed for laws that would enable it to pay finders more for larger loans than for smaller ones – a strong incentive for brokers to push borrowers into larger, less affordable loans.

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[5] https://www.figloans.com/.

[6] *Id.*

[7] Aura's 2018 report, reporting on 2017 loans, to the California Department of Business Oversight, on file with CRL. These loans were all under $2,500, with most in the $500-$1,999 range, and with an average contracted term of 12 months.

[8] https://myaura.com/invest

Oportun, another CDFI, also has a history of charging high rates up to 69.99%. While its refinance rates are not available, 80% of its dollars loaned go to repeat customers.[9] Its late fees also signal unaffordability: In 2018, it collected late fees on roughly 75% of its loans.[10] Oportun has recently made headlines for grossly abusive debt collection practices.[11] ProPublica investigated Oportun's sue-to-intimidate method, finding that the company filed 47,000 suits across Texas over the last four years, making it the state's most litigious personal loan company. Oportun has filed over 5,000 suits in Texas since the start of the pandemic. The Guardian found that Oportun accounted for at least 15% of small claims filings in California from mid-2017 to mid-2018 and had filed 14,000 suits in the state during the first half of 2020.[12] The company drops suits in the rare cases where borrowers obtain lawyers, signaling it sues only to intimidate and/or collect default judgments. Oportun lends primarily to the Latino community, where its litigation tactics are prone to evoke pronounced fear in light of fear of immigration enforcement.[13]

Following media inquiries into its litigation practices, Oportun announced it would lower its maximum APR to a fee-inclusive 36%; drop its pending lawsuits; suspend new filings for the time being; and reduce its filing rate going forward by 60%.[14] Even if meets that target, Oportun would be the fifth most litigious debt collector in Texas – showing that interest rate alone does not guarantee affordability.[15]

Some CDFI banks and credit unions also engage in abusive checking account overdraft practices, which we discuss in Section VII below.

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[9] Kiah Collier, Ren Larson and Perla Trevizo, *The Loan Company That Sued Thousands of Low-Income Latinos During the Pandemic*, ProPublica, Aug. 31, 2020, https://www.propublica.org/article/the-loan-company-that-sued-thousands-of-low-income-latinos-during-the-pandemic#:~:text=A%20monthslong%20investigation%20revealed%20that,%E2%80%94%20even%20amid%20COVID%2D19 (ProPublica, Aug. 2020).

[10] Raheem Hosseini, *Exclusive: the litigious debt collectors targeting Latinos during a pandemic*, The Guardian, Aug. 2, 2020, https://www.theguardian.com/us-news/2020/aug/02/oportun-loans-lawsuits-latino-small-claims-californi (The Guardian, Aug. 2020).

[11] *See* ProPublica, Aug. 2020 and The Guardian, Aug. 2020 for in-depth descriptions of Oportun's practices, including accounts of the impact of these practices on the financially distressed Latino borrowers featured.

[12] The Guardian, Aug. 2020.

[13] ProPublica found that of 467 lawsuits reviewed in Texas, fewer than half included the defendant's Social Security number. ProPublica, Aug. 2020.

[14] Oportun Statement, *Oportun to cap new loan originations at an "all-in" 36% APR*, July 28, 2020, https://oportun.com/about/press/oportun-to-cap-new-loan-originations-at-an-all-in-36-apr/.

[15] ProPublica, Aug. 2020.

Mortgage

We are concerned that some financial institutions seek CDFI certification to skirt mortgage requirements. For example, after the CFPB's Ability-to-Repay/Qualified Mortgage regulation was published in January 2013 and became effective in January 2014, there was a large uptick in depositories obtaining CDFI certification. The Fund maintains a list of CDFIs and the date they were certified. Out of 147 CDFIs categorized as banks/thrifts, at least 75 became certified in the last quarter of 2013 or 2014. Likewise, of CDFIs categorized as bank holding companies or depository institution holding companies, a large percentage of them gained certification in 2013 or 2014. It does not seem to be a coincidence that this increase occurred immediately after CFPB determined CDFIs were exempt from the Ability-to-Repay/Qualified Mortgage regulation. This does not by itself, of course, mean that CDFIs are engaging in irresponsible practices. But it suggests that additional tightening would be helpful to ensure that bad actors are not given room to thrive.

Additionally, we have observed a CDFI state that it offers mortgages that require little to no income verification or will rely on a borrower-prepared profit and loss statement to document income. If a lender is indeed relying on a statement by the borrower as proof of income, without more, this could indicate a stated income/no doc loan. These dangerous loans were done during the boom leading up to the housing crisis. It is critical to ensure that CDFIs do not permit a resurgence of this practice. Despite their exemption from the CFPB's ATR regulation, CDFI mortgage lenders should still demonstrate that they utilize sound underwriting practices – specifically, that they considered and verified borrower debts, income, and assets.

III. CDFI designation should be reserved for lenders not offering loans exceeding a fee-inclusive 36% APR (or lower state limits under state law).

Interest rate limits are the single most effective way to prevent predatory lending. For CDFIs to meet their statutory objective to promote community development, they must operate within reasonable interest rate limits.

For small loans, the 36% fee-inclusive rate cap under the Military Lending Act (MLA) (MAPR) that protects servicemembers and their dependents is a widely accepted dividing line between reasonably priced loans and high-cost ones.[16] For larger loans, most states impose lower rate limits: a median of 31% APR including fees for a $2,000 loan and a median of 25% APR for a $10,000 loan.[17] CDFIs should be encouraged to keep rates at these limits or well below on these

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[16] *See* Lauren Saunders, *Why 36%? The History, Use, and Purpose of the 36% Interest Rate Cap*, NCLC (April 2013), https://www.nclc.org/images/pdf/pr-reports/why36pct.pdf.

[17] NCLC, *State Annual Percentage Rate (APR) Caps for $500, $2,000 and $10,000 Installment Loans* (2019), https://www.nclc.org/images/pdf/high_cost_small_loans/fact-sheet-apr-caps-for-installment-loans.pdf.

larger loans.[18] But a fee-inclusive 36% APR eligibility requirement provides a clear, bright-line standard, rooted in federal precedent. It is also a threshold that all lenders are already required by federal law to know whether or not their consumer loans exceed, so establishing it as an eligibility threshold should not create significant additional administrative burden.

A bright line requirement is far preferable to the Fund's current proposal to make the interest rate a benchmark that triggers higher scrutiny. First, a bright line limit of 36% MAPR is appropriate to fulfill the statutory objective. It makes little sense to provide a federal imprimatur, and often subsidy, for lenders making loans so expensive that Congress has prohibited them for our nation's servicemembers or that are illegal in most states. An exception should be provided for federal credit unions whose only product that exceeds these rates is payday alternative loans (PALs). By federal regulation, PAL pricing is limited; its features are clearly prescribed; and its frequency is limited to six in a twelve-month period, all of which serve to make PALs far less likely to inflict harm on borrowers than other loans exceeding a 36% MAPR.

Moreover, a clear eligibility requirement avoids charging the Fund with policing whether or not lenders that, by definition, are operating far outside the norms of propriety in lending, may nonetheless merit CDFI certification. As we fail to think of such an entity, expending Fund resources on this task is both unnecessary and inefficient.

The notion that higher-cost loans should be allowed because they expand financial inclusion, or otherwise promote community development, is not supportable. So-called "fintechs" offering online installment loans at high rates are among the loudest pushing for schemes to avoid state interest rate caps in the name of "access to credit." These lenders, using "soaring rhetoric,"[19] portray their loans as better alternatives to payday loans, but their loans often lead to similar problems. They often carry extremely high rates, with repayment still tied to payday, with little regard for the borrower's ability to repay while meeting other expenses – all part of a business model where lenders can profit despite high borrower defaults.

Data show time and again that high-cost credit, like that offered by many of these so-called "fintechs" – and some CDFIs, discussed in Section II above – does not drive out other, higher-

[18] In our recent comments to the Fund on its Small Dollar Loan Program, we urged the following limits on that program, which CDFIs should be encouraged to adhere to across the board, to the extent state laws permit such rates:

- For loans up to $1,000, a fee-inclusive 36% under the MLA;
- For loans $1,001 to $2,500, a fee-inclusive 31% (calculated consistent with the MLA);
- For loans above $2,500, a fee-inclusive 25% (calculated consistent with the MLA).

[19] *See* Christopher K. Odinet, *Predatory Fintech and the Politics of Banking* 19, 20, 22-28 (Iowa Law Review (2021 Forthcoming)) (Aug. 2020), https://papers.ssrn.com/sol3/Papers.cfm?abstract_id=3677283.

cost unaffordable credit. It simply piles more unaffordable credit onto already financially vulnerable borrowers.[20]

Harm caused by high-rate loans extends far beyond the higher cost itself. High-cost lending turns incentives on their head, so that lenders succeed when borrowers fail – that is, lenders can easily profit even when large portions of borrowers default.[21] Once even small portions of principal are paid down, lenders aggressively push refinances to borrowers to keep them on a high-cost debt treadmill.[22] Even with these high refinance rates, defaults on high-cost loans are extraordinarily high. Elevate, a lender whose loans average 122% APR,[23] describes its mission as "Good Today, Better Tomorrow."[24] But Elevate has net charge-offs as a percentage of revenues of 50%.[25]

High-cost lenders peddling unaffordable loans cause particular harm to communities of color,[26] often in the same geographic areas that experienced redlining. Storefront high-cost lenders have long targeted borrowers of color, more likely to locate stores even in more affluent communities of color than in less affluent white communities.[27] Online high-cost lenders may

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[20] *See* Comments of CRL, NCLC and other consumer and civil rights groups on the FDIC's Request for Information on Small-Dollar Lending at 5-8, Jan. 22, 2019, https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-fdic-smalldollar-rfi-22jan2019.pdf.

[21] *See generally*, NCLC, *Misaligned Incentives: Why High-Rate Installment Lenders Want Borrowers Who Will Default* (July 2016), https://www.nclc.org/issues/misaligned-incentives.html.

[22] The CFPB found that for online payday installment loans (the channel for most new "fintech" loans) refinance rates were very high. CFPB Supplemental Findings on payday, payday installment, and vehicle title loans (June 2, 2016) at 15 (35% for storefront, 22% for online); *see also* Elevate Credit, Inc., Form 10K, 2019, https://www.sec.gov/Archives/edgar/data/1651094/000165109420000010/elevate10-kx2019.htm, at 15 (noting "[a]pproximately 55% of Rise installment customers in good standing had refinanced or taken out a subsequent loan as of December 31, 2019, with 40% of the outstanding Rise installment loan balances on that date consisting of new customer loans and 60% related to returning customer loans."). While mainstream lenders also often have substantial rates of refinancings, those lenders also charge rates that permit reasonable amortization of loan balances.

[23] Elevate Form 10K, 2019, at 75.

[24] Elevate Form 10K, 2019, at 6; *see also* Elevate's website at https://www.elevate.com/company.html.

[25] Elevate Form 10K, 2019, at 75; CFPB Supplemental Findings on payday, payday installment, and vehicle title loans (June 2, 2016) at 9 (the CFPB found that 55% of online loan sequences ended in default).

[26] *See* CFPB Payday Rule, 82 Fed. Reg. at 54556-57 (African Americans are payday borrowers at three times the rate, and Hispanics at twice the rate, of non-Hispanic whites (citing 2015 FDIC National Survey of Unbanked and Underbanked Households (calculations using custom data tool)). Vehicle title borrowers are also disproportionately African American and Hispanic. *Id*.)

[27] Li, et al., *Predatory Profiling: The Role of Race and Ethnicity in the Location of Payday Lenders in California,* Center for Responsible Lending (2009), http://www.responsiblelending.org/payday-lending/research-

focus more on subprime credit score than geography, although we understand that some lenders use zip codes to target online marketing. But historical discrimination against communities of color is also reflected in credit scores.[28] Lenders that focus on borrowers with subprime credit scores will inevitably disproportionately target borrowers of color. The algorithms and big data that "fintech" lenders use may also result in disparate impacts on these communities.[29]

Moreover, when online lenders promote their models as expanding economic inclusion, this often puts borrowers of color among their target borrowers. Communities of color have historically been disproportionately left out of the traditional banking system, a disparity that persists today. Some defend the high-cost "fintech" loans as bringing communities of color into the economic mainstream.[30] But high-cost loans, particularly with their high association with lost bank accounts,[31] drive borrowers out of the banking system and exacerbate this disparity. By sustaining and exacerbating an existing precarious financial situation, high-cost lending reinforces and magnifies existing income and wealth gaps – legacies of continuing discrimination – and perpetuates discrimination today.

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analysis/predatory-profiling.pdf; Brandon Coleman and Delvin Davis, *Perfect Storm: Payday Lenders Harm Florida Consumers Despite State Law*, Center for Responsible Lending at 7, Chart 2 (March 2016); Delvin Davis and Lisa Stifler, *Power Steering: Payday Lenders Targeting Vulnerable Michigan Communities*, Center for Responsible Lending (Aug. 2018), https://www.responsiblelending.org/research-publication/power-steering-payday-lenders-targeting-vulnerable-michigan-communities; Delvin Davis, *Mile High Money: Payday Stores Target Colorado Communities of Color*, Center for Responsible Lending (Aug. 2017; amended Feb. 2018), https://www.responsiblelending.org/research-publication/mile-high-money-payday-stores-target-colorado-communities-color.

[28] *See* Chi Chi Wu, *Past Imperfect: How Credit Scores and Other Analytics "Bake In" and Perpetuate Past Discrimination*, National Consumer Law Center (May 2016), https://www.nclc.org/images/pdf/credit_discrimination/Past_Imperfect050616.pdf.

[29] *See* Testimony of Chi Chi Wu, National Consumer Law Center, Before the U.S. House Committee on Financial Services Task Force on Financial Technology Regarding "Examining the Use of Alternative Data in Underwriting and Credit Scoring to Expand Access to Credit" (July 25, 2019); Carol A. Evans, *Keeping Fintech Fair: Thinking about Fair Lending and UDAP* Risks, Consumer Compliance Outlook (2017), https://consumercomplianceoutlook.org/2017/second-issue/keeping-fintech-fair-thinking-about-fair-lending-and-udap-risks/; *see also* Christopher K. Odinet, *Predatory Fintech and the Politics of Banking* 19-20 (Iowa Law Review (2021 Forthcoming) (Aug. 2020), https://papers.ssrn.com/sol3/Papers.cfm?abstract_id=3677283.

[30] *See* Remarks of Acting Comptroller of the Currency Brian Brooks to the Online Lending Policy Institute, June 11, 2020, https://www.youtube.com/watch?v=Ae_SoZeRbxM, at 33:00 (stating "I want to make poor people rich" while addressing financial inclusion, in a conversation where he also states that his personal belief is that "price controls generally create shortages" and that "if we believe in market pricing for hamburgers, for jeans, for automobiles, I'm not sure why we don't believe in market rates for money, it's another commodity, and we want it to flow freely").

[31] CFPB found that about half of borrowers with online payday or other high-cost online loans paid a nonsufficient funds (NSF) or overdraft fee. These borrowers paid an average of $185 in such fees, while 10% paid at least $432. It further found that 36% of borrowers with a bounced payday payment later had their checking accounts closed involuntarily by the bank. CFPB Online Payday Loan Payments at 3-4, 22 (April 2016).

Thus, interest rate limits are an essential component of responsible lending because they better align lender incentives with borrower incentives by making it more difficult for a lender to build a business model with high defaults; they enable borrowers to make progress on paying down principal; and they make the loan cost reasonable for the borrower.

We also urge the Fund to require that non-bank CDFIs partnering with banks abide by the interest rate limits in the state where the borrower resides. We caution the Fund to be alert to potential "rent-a-bank" schemes, where non-bank CDFIs may seek to scheme with banks to take advantage of banks' preemption privileges in order to evade state laws that prohibit high interest rates.[32] If rates in these arrangements are not required to comply with the state law where the borrower resides, then non-bank CDFIs will be able to launder their loans through a bank to evade state rate caps.[33]

While interest rates limits are critical, lenders can still make unaffordable loans even operating under reasonable rate limits – through coercive payment collection devices, loan flipping, and aggressive debt collection, including legal actions and garnishment. So an upfront ability-to-repay determination and protections from other harmful practices are also essential.

IV. CDFIs should be required to lend based on the borrower's ability-to-repay.

We were pleased to see the Fund's advisement that loans should be made based on the borrower's ability to repay.[34] Indeed, lending based on a borrower's ability to repay – while meeting other expenses, without needing to refinance/reborrow, and without relying on collateral – is a fundamental tenet of responsible lending.[35] Thus, a meaningful ability-to-repay

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[32] Comments on the OCC's proposal to gut the true lender doctrine from a coalition of national consumer and civil rights groups, filed Sept. 3, 2020, at https://www.responsiblelending.org/research-publication/comment-occ-rule-would-allow-payday-lenders-use-rent-bank-schemes-evade-state.

[33] For detailed discussion of our concerns about rent-a-bank schemes, *see id.*

[34] Proposed Application at 30.

[35] HOEPA statutory language since 1994 requires that repayment ability include "current and expected income, *current obligations*, and employment." 15 U.S.C. 1639(h): ". . . A creditor shall not engage in a pattern or practice of extending credit to consumers under [high-cost] mortgages . . . *based on the consumers' collateral* without regard to the consumers' repayment ability, including the consumers' current and expected income*, current obligations*, and employment" (emphasis added).

The 2000 OCC Advisory Letter on Abusive Lending Practices discusses equity stripping as "*reliance on . . . collateral, rather than the borrower's independent ability to repay*. . . ."OCC Advisory Letter on Abusive Lending Practices, AL 2000-7 (June 25, 2000), *available at* http://www.occ.gov/static/news-issuances/memos-advisory-letters/2000/advisory-letter-2000-7.pdf (emphasis added).

The 2001 Interagency Subprime Guidance provides that abusive lending practices occur when "the lender structures a loan to a borrower who has little or no ability to repay the loan *from sources other than the collateral pledged."* Interagency Expanded Guidance or Subprime Lending Programs, FIL 9-2001, January 31, 2001. The FDIC's 2005 payday loan guidelines also notes that it clarifies previously issued guidance, including the 2001 Expanded

determination considers both the borrower's income and expenses. Responsible underwriting is especially important when, like with most online loans today, a lender has access to the borrower's checking account and can repay itself automatically out of the account before a borrower can pay other essential expenses.

Payment-to-income (PTI) ratios cannot substitute for underwriting. Consider a family of four living just below the federal poverty level of $24,300 annually or $2,025 monthly. A 5% PTI standard would unrealistically assume that the borrower has $101 in extra cash each month, or $1,215 annually, that they can spare toward service of additional debt. Yet, by definition, the poverty level is the level below which a family already has insufficient income. Even at somewhat higher income levels, it is far-fetched to categorically assume that a borrower who is already struggling financially has an extra 5% of her income available to put towards a new debt.

The Fund should also monitor default rates (noted below) because high default rates signal unaffordability. But low default rates alone do not mean borrowers have the ability to repay. Refinances mask unaffordability. And when a lender has a repayment mechanism, like electronic access to the account, the lender will often collect payment even when the borrower

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Subprime Guidance; the 2001 Expanded Subprime Guidance also contemplates equity stripping outside the context of mortgage lending, noting that lenders may make a loan to a borrower who has little or no ability to repay other than from the collateral pledged, then take possession of the borrower's home or automobile upon default.

The FDIC's 2005 payday loan guidelines describe concerns with "payday loans to individuals who do not have the ability to repay, or that may result in repeated renewals or extensions and fee payments over a relatively short span of weeks." FDIC Guidelines for Payday Lending (revised Nov. 2015), https://www.fdic.gov/news/financial-institution-letters/2005/fil1405a.html#:~:text=Provide%20that%20no%20more%20than,during%20the%20previous%2012%20months.

The Federal Reserve's 2009 HOEPA rules required verification of income, assets *and obligations* for both high-cost and higher-priced loans. They also note that "[l]ending without regard to repayment ability . . . facilitates an abusive strategy of 'flipping' borrowers in a succession of refinancings." Federal Reserve System, Truth in Lending, Regulation Z; Final Rule, 73 Fed. Reg. 44522, 44542, 445446. (July 30, 2008).

The Wall Street Reform Act, 2010, for all residential mortgages, requires "a reasonable and good faith determination based on verified and documented information," 15 U.S.C. § 1639c(a)(1), including, among other items, expected income, *current obligations*, *debt-to-income ratio or residual income*, and other financial resources other than the consumer's equity. 15 U.S.C. § 1639c(a)(3).

The regulations implementing the ability-to-repay provision of the Credit CARD Act of 2009 also require credit card issuers to consider "the consumer's current obligations." 12 C.F.R. § 1026.51(a)(1)(i).

NCUA's PAL program provides the following: "[T]he FCU must consider the borrower's *entire financial position*, *including debt burden*, and make an informed judgment consistent with responsible lending principles regarding whether to extend a PALs loan to a borrower. Accordingly, the FCU should conduct some inquiry into whether the borrower can manage to repay the PALs loan *without the need for additional PALs loans or traditional payday loans*." 84 Fed. Reg. 51942, 51946 (Oct. 1, 2019) (emphasis added).

The recent Interagency Lending Principles for Offering Responsible Small-Dollar Loans from the Federal Reserve, FDIC, NCUA, and OCC, states that characteristics of "responsible programs" include successful repayment "in accordance with original terms," and minimizing "cycles of debt due to rollovers or reborrowing." https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20200520a1.pdf.

cannot afford the loan. Thus, review of default rates does not substitute for an upfront ability-to-repay determination.

V. Additional structural and procedural safeguards on consumer loans are important to protect borrowers.

We appreciate the series of questions on the proposed application that appear aimed at assessing the risk and harm of loans made above 36%,[36] as well as those related to troubled loans and debt collection. Generally, protections along the lines of those contemplated by these questions are sensible regardless of interest rate.

We urge the Fund to require that all CDFIs adhere to the following:

- **For consumer loans, equal, fully amortizing installments due at equal intervals**. CDFI loans should carry a traditional responsible loan structure with no balloon payments or other surprises for borrowers.

- **No forced arbitration clause or class action ban.** These contractual provisions promote irresponsible lending by sheltering lenders from accountability for violating the law. CDFIs should not be permitted to include these in their loan contracts.

- **No sale of defaulted debt.** Debt buyers are notorious for their abusive debt collection practices.

- **No coerced automated repayment.** Regulation E makes it illegal for lenders to require installment loan borrowers to repay by preauthorized electronic fund transfer (EFT). But some lenders coerce automated repayment by, for example, delaying loan disbursement for borrowers who do not agree to automatic repayment; making it unreasonably onerous to sign up for manual payment; charging fees for manual payment that have no relationship to the cost of processing those payments; or requiring repayment by remotely created check if the borrower does not agree to an EFT.

We further urge that the Fund collect data on, monitor, and encourage the following:

- **Reasonable refinance and default rates, as excessive rates signal unaffordable lending.** High refinance rates are a hallmark feature of unaffordable loan programs. Refinancing can mask defaults or lengthen the debt trap, and upfront fees provide lenders added incentives to push refinances. High default rates also signal unaffordable lending.

[36] Proposed Application at 39-40.

- **Monitoring of any add-ons.** Add-ons like credit insurance can dramatically drive up the cost of loans, incentivize lenders to push refinances, and often provide little-to-no value for borrowers. A 36% MAPR limit for eligibility would go a long way toward addressing this problem. If this benchmark were not made a bright-line eligibility requirement, add-ons would require closer monitoring.

- **Minimum and maximum loan terms.** Minimum loan terms promote affordable installment payments. Maximum loan terms help to ensure that relatively small payments, repaid over a very long period of time, don't end up costing borrowers an unreasonable amount in interest relative to principal borrowed.

- **Workout program.** Lenders should offer and prominently disclose reasonable accommodations to struggling borrowers before pursuing other debt collection avenues.

- **Savings features on small consumer loans should be encouraged.** Savings features promote a more stable financial future. The cushion they build also makes borrowers less vulnerable to predatory lenders going forward. The savings component can be built into the regularly-scheduled payments on a loan – provided that the resulting payment is still affordable – or, at a minimum, loans can be structured so that, subject to the consumer's consent, payments continue for a period of time after the loan is repaid with all of the payments going into a savings vehicle.

- **Responsible debt collection practices, including not over-relying on lawsuits to collect debt.** Aggressive debt collection practices are another sign of unaffordable lending. In addition to not selling debt to debt buyers, which we suggest prohibiting above, lenders should not over-rely on lawsuits to collect debt – another sign of unaffordable lending; see, for example, discussion of Oportun's practices in Section II above. Lawsuits to collect unaffordable debt often lead to legal nightmares for borrowers, including wage or bank account garnishment and compounding fees.

VI. The Fund should require CDFIs to adhere to the Qualified Mortgage (QM) product protections.

Although CDFIs are exempt from the Ability-to-Repay/Qualified Mortgage rule (ATR/QM rule), that does not imply that CDFIs should be permitted to disregard affordability and the ability of borrowers to repay a mortgage loan. Indeed, considering that CDFIs are mission-based organizations with a particular aim to ensure access to underserved borrowers, arguably it is even more vital for the Fund to ensure that CDFIs are offering quality mortgage products that facilitate wealth-building. We recognize that the majority of entities applying for CDFI certification are truly mission-driven entities. However, as discussed in Section II, there is a genuine risk that some institutions have pursued and will pursue CDFI certification to skirt certain requirements, including complying with the ATR/QM rule. It is critical to ensure that the

certification process is robust. When it comes to mortgages from CDFIs, the CFPB relies on the Fund to serve as a gatekeeper. The CFPB's preamble to the ATR/QM final rule references the Fund's certification process, stating: "[G]overnment approval and oversight associated with [the CDFI and other] designations ensures that there is little risk that consumers would be subject to abusive lending practices."[37]

Thus, the CDFI Fund should adopt an objective gating requirement to help ensure that CDFIs are offering responsible mortgage products. We recommend that the gating requirement be that certified CDFIs must abide by the QM product protections. These protections are 1) the loan cannot have negative amortization, interest-only payments, or balloon payments; 2) ARMs must be underwritten at the maximum rate in the first five years; 3) the original mortgage term must be 30 years or less; and 4) total points and fees generally cannot exceed 3 percent of the loan amount. In addition, lenders should be able to demonstrate that they considered and verified borrower debts, income, and assets.

The QM statutory product protections provide for the most transparent and sustainable mortgages. On the contrary, non-QM mortgages may build in payment shock and high fees. In fact, non-QM loans provide for artificial and temporary affordability through product structures that inherently cause payments to rise to unaffordable levels when they begin amortizing or teaser rates expire – the precise opposite what legitimate CDFIs should offer their borrowers. While there may be room for product innovation in the non-QM space that complies with fair lending laws, non-QM is generally the province of jumbo loans and specialized products for wealthier borrowers – not the borrowers CDFIs are mission-bound to serve. CDFIs should not be permitted to devise complex products that ostensibly permit underserved borrowers to access homeownership through lower initial payments, yet in reality, are prone to cause harm for underserved communities by product design.

The importance of safe product protections is illustrated by recent history. During the subprime lending boom, lenders steered millions of families into abusive loans that were not sustainable and that were inconsistent with the QM product protections, even as those borrowers would have qualified for safer and more affordable credit. Leading up to the crisis, these dangerous niche products that lenders mass-marketed included interest-only loans, ARM loans that combined "teaser" rates with subsequent large jumps in payments, negative amortization loans, and loans made with limited or no documentation of the borrower's income or assets.[38] Studies have shown that these products in and of themselves caused about half of the increased risk in mortgage lending that led to the Great Recession.[39]

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[37] 78 Fed. Reg. 35429, 35564 (June 12, 2013).

[38] Financial Crisis Inquiry Commission, *The Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States*, at pp. 104-111 (2011), https://www.govinfo.gov/content/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf.

[39] Morris A. Davis, William D. Larson, Stephen D. Oliner, and Benjamin R. Smith, *A Quarter Century of Mortgage Risk*, FHFA Staff Working Paper 19-02, at p. 35, October 2019 (revised) January 2019 (original) (finding that "risky

These abusive products were disproportionately targeted to communities of color. Roughly half of all mortgages made to Black and Latino families during the run-up to the crisis were subprime loans, which included patently unsustainable terms.[40] Evidence shows that many of those borrowers were steered into toxic mortgages even when they qualified for safer and more responsible loans with cheaper costs.[41] As a consequence of these lending practices, Black and Latino families lost over $1 trillion dollars in wealth during the crisis.[42]

In response to these abuses, the Dodd-Frank Act established rules ensuring that borrowers have a reasonable ability to repay their mortgage loans at consummation and requiring full

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product features accounted for more than half of the rise in risk during the boom years", defining "risky product features" as those ineligible for QM status). The definition of "risky product features" is conservative because it does not include many loans that would also be ineligible for QM status. Namely, the definition excludes the 22% of subprime loans that were 30-year ARMs (40% of subprime loans were) and that were fully documented (60% of subprime loans were, and 40% times 56% equals 22%). These loans would not have been QM because they almost certainly were not underwritten at the maximum interest rate for the first five years of the loan and a high percentage had prepayment penalties and did not escrow for taxes and insurance. Prepayment penalties are prohibited and escrows are required for loans over 1.5% over APOR by Dodd-Frank. For characteristics of subprime loans, see Testimony of Eric Stein before the U.S. Senate Committee on Banking, Housing and Urban Affairs, *Turmoil in the U.S. Credit Markets: The Genesis of the Current Economic Crisis*, Center for Responsible Lending (October 16, 2008) at pp. 11-14, 34-39, https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/senate-testimony-10-16-08-hearing-stein-final.pdf. *See also* Lei Ding, Roberto Quercia, Wei Li, and Janneke Ratcliffe, *Risky Borrowers or Risky Mortgages Disaggregating Effects Using Propensity Score Models*, at pp. 245-277, Journal of Real Estate Research: Vol. 33, No. 2 (2011).

[40] Federal Reserve researchers, using data from 2004 through 2008, have reported that higher-rate conventional mortgages were disproportionately distributed to borrowers of color, including African-American, Latino, American Indians, Alaskan Natives, Native Hawaiians, Pacific Islanders, and Hispanic borrowers. *See* R.B. Avery, K.P. Brevoort, and G.B. Canner, *Higher-Priced Home Lending and the 2005 HMDA Data*, Federal Reserve Bulletin (September 2006), http://www.federalreserve.gov/pubs/bulletin/2006/hmda/bull06hmda.pdf. For example, in 2006, among consumers who received conventional mortgages for single-family homes, roughly half of African-American (53.7 percent) and Hispanic borrowers (46.5 percent) received a higher-rate mortgage compared to about one-fifth of non-Hispanic white borrowers (17.7 percent). According to the researchers, "[F]or higher-priced conventional first-lien loans for an owner-occupied site-built home, the mean APR spreads were about 5 percentage points above the yields on comparable Treasury securities both for purchase loans and refinancings". R.B. Avery, K.P. Brevoort, and G.B. Canner, *The 2006 HMDA Data*, at p. A88, Federal Reserve Bulletin (December 2007), http://www.federalreserve.gov/pubs/bulletin/2007/pdf/hmda06final.pdf. For a discussion of the unsustainable subprime lending terms and practices, see Testimony of Eric Stein before the U.S. Senate Committee on Banking, Housing and Urban Affairs, ibid.

[41] Rick Brooks and Ruth Simon, *Subprime Debacle Traps Even Very Credit-Worthy*, Wall Street Journal, December 2007, https://www.wsj.com/articles/SB119662974358911035; *see* Debbie Gruenstein Bocian, Keith Ernst and Wei Lee, *Race, Ethnicity and Subprime Loan Pricing*, Center for Responsible Lending, Journal of Economics and Business, at pp. 110-124, Vol. 60, Issues 1-2, January-February 2008.

[42] Debbie Gruenstein Bocian, Peter Smith, and Wei Li, *Collateral Damage: The Spillover Costs of Foreclosures*, Center for Responsible Lending, at p. 2 (Oct. 24, 2012), https://www.responsiblelending.org/mortgage-lending/research-analysis/collateral-damage.pdf.

documentation of income and assets. Given the CDFI exemption from ATR/QM, it is essential to ensure that CDFIs are providing sustainable mortgages. The QM statutory product protections would serve as the threshold to ensure that CDFIs are not able to offer products that disregard ability to repay, have built-in payment shock, or impose excessive fees.

If CDFIs abide by safe product protections, it is appropriate for CDFIs to be exempt from the affordability limits that CFPB may apply to other creditors, such as the current strict DTI limit; applied to CDFIs, these limits may unreasonably constrict access to credit, and exempting them is consistent with the portfolio exemption for small creditors.[43] As CFPB states in the preamble to the ATR/QM final rule, "ability-to-repay requirements generally differ from the unique underwriting criteria which are related to the characteristics of the consumers served by [CDFIs]."[44] The affordability requirements "primarily consist of quantitative underwriting considerations," such as the consumer's DTI ratio.[45] Conversely, CDFIs engage in a more qualitative underwriting process that considers compensating factors. Given that many CDFIs focus on mission-based lending, roots in the community, and knowledge of their borrowers, it is reasonable for CDFIs to deviate from the specific affordability requirements of the ATR/QM rule in order to responsibly increase access to credit. Still, CDFIs should ensure that their practices are responsible by abiding by the QM product protections and demonstrating that they consider and verify borrower debts, income, and assets when underwriting a loan.

Furthermore, requiring CDFIs to abide by the product protections would not inhibit innovation in underwriting, such as relying on qualitative compensating factors, alternative data, or alternative credit models to qualify borrowers. CDFIs need not strictly adhere to mainstream underwriting criteria. In fact, as the CFPB stated in the ATR/QM final rule, CDFIs that provide mortgage loans generally employ underwriting guidelines tailored to the needs of LMI consumers. Unlike creditors that rely on industry-wide underwriting guidelines, which generally do not account for the unique credit characteristics of LMI consumers, CDFIs "typically engage in a lengthy underwriting process that is specifically tailored to the needs of these consumers by incorporating a variety of compensating factors."[46] This enables more inclusive access to credit for borrowers underserved by traditional underwriting and credit scoring mechanisms. Yet, alternative structures must still be subject to fair lending compliance reviews to ensure that these systems do not create an unjustified disparate impact on any protected class of borrowers.

In sum, the CDFI Fund should require certified CDFIs to adhere to the QM product protections to bolster safe and responsible mortgage lending, while permitting the flexible underwriting appropriate for meeting the needs of LMI communities.

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[43] 12 C.F.R. § 1026.43(e)(5).

[44] 78 Fed. Reg. at 35564.

[45] *Id.*

[46] *Id.*

VII. The Fund should impose clear limits on high-cost overdraft programs.

Overdraft fees strip billions of dollars annually from struggling consumers, leaving them less able to save to weather shortfalls, more vulnerable to predatory promises of "short-term" loans, and generally financially worse off.[47] Any CDFI's effort to promote community development is substantially hampered when paired with a high-cost overdraft program.

We appreciate the Fund's recognition of this problem in the proposed application.[48] At the same time, the proposed questions should not be expected to meaningfully address the problem. The application asks whether the CDFI offers at least one account without overdraft fees,[49] but most financial institutions that offer such accounts do so alongside an account that charges typical, abusive overdraft fees. The institution's financial incentives to enroll accountholders in the no-overdraft account are thus significantly compromised. The application also asks whether the CDFI establishes limits on the number and frequency of overdraft fees, but without establishing any benchmark or limit.[50]

We urge the Fund to establish an eligibility requirement that CDFIs charge no more than six overdraft fees in a rolling 12 months, consistent with the FDIC's 2010 guidance addressing overdraft programs.[51] Overdraft fees charged any more frequently are clearly operating not as an occasional courtesy but as a routine, exorbitantly priced credit product that should be operated and regulated as a credit product.

Further, we urge the Fund not to include questions that could be read to discourage depositories from charging a modest monthly fee for checking accounts. Currently, the application suggests that a fee of more than $5 is too much unless it is waivable.[52] But a shift toward modest monthly checking account fees promotes a departure from back-end, unreasonably high overdraft fees that are disproportionately borne by depositories' most vulnerable accountholders.

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[47] *See*, *generally*, Peter Smith et. al, *Overdraft Fees: Banks Must Stop Gouging Consumers During the COVID-19 Crisis*, Center for Responsible Lending (June 2020), https://www.responsiblelending.org/sites/default/files/nodes/files/research-publication/crl-overdraft-covid19-jun2019.pdf.

[48] Proposed Certification Application at 41, 42.

[49] Proposed Certification Application at 41, PM27.

[50] Proposed Certification Application at 42, PM29.

[51] https://www.fdic.gov/news/financial-institution-letters/2010/fil10081.html.

[52] Proposed Certification Application at 41, PM26.

VIII. We support assessing non-depository parents, affiliates, and subsidiaries as a whole.

We strongly support the Fund's proposal to apply the primary mission test as a whole to non-depository parents, affiliates, and subsidiaries engaged in financing. We have been very concerned in recent years about mortgage bankers establishing affiliates that obtain CDFI certification, the merits of which are unclear, and, as a result, receive access to Federal Home Loan Bank advances and the regulatory exemption from Dodd-Frank's ability-to-repay requirements for mortgages. This revised test is essential to helping to keep out lenders that seek CDFI certification without having the purposeful "community development intent" the Fund's proposal emphasizes.[53]

IX. We support the removal of geographic boundaries on most Target Market designations.

Self-Help supports the proposed removal of geographic limits on certified Target Markets. As CDFIs grow, they face the administrative burden of continually requesting Target Market expansions, creating work for both CDFIs and the CDFI Fund staff. This in effect acts as a dis-incentive for CDFIs to lend in new markets and open new branches. Flexibility to lend in broad geographic markets is particularly important for specialized sectors such as food systems, charter schools, and renewable energy, where CDFIs with specific expertise often work to target borrowers on a national scale. Geographic flexibility will also encourage more partnering between CDFIs, particularly where smaller CDFIs need partners to fully finance large high-impact projects.

We emphasize that the eligibility requirements we discuss throughout this comment are critical to ensuring that CDFIs operating on any scale are promoting rather than eroding community development. We further urge the Fund to monitor the extent to which CDFIs with national Target Markets are responsibly reaching borrowers of color; see discussion of Reporting Requirements in the following section. In addition, we urge the Fund to encourage that CDFIs, particularly those serving a national Target Market, prioritize contracting with minority-owned and women-owned suppliers.

X. We urge enhanced reporting of race and ethnicity data with respect to CDFIs and the borrowers and communities they serve, as well as transaction level data for all CDFIs.

We urge the Fund to collect and analyze additional data to aid its ability to assess the extent to which the Fund and CDFIs are serving borrowers and communities of color. These include:

[53] 85 Fed. Reg. 27277.

- whether the CDFI is designated as a minority depository institution (MDI) by the FDIC or NCUA;
- race, ethnicity and gender of a CDFI's leadership;
- race and ethnicity of a CDFI's board of directors;
- race data on borrowers and communities served, even for CDFIs that have not designated a Target Population for their target market; and
- HMDA data for mortgages and, once finalized by the CFPB, reporting on small business lending required under Section 1071 of the Dodd-Frank Act.

It is to be expected that the above metrics for CDFIs serving target markets with fewer residents of color will not reflect the diversity that those serving more diverse target markets will reflect. But collecting and assessing this information is still important, in part to aid the Fund in assessing the extent to which the Fund as a whole is supporting community development for communities of color.

In addition, we support the proposal to require the Certification Transaction Level Report for all CDFIs. Currently, requiring this data only from recent financial assistance (FA) awardees provides the CDFI Fund with an incomplete picture of the CDFI landscape. For Self-Help, the CTLR will not be burdensome even for all of our entities. The fields are relevant fields lenders should be collecting. Requiring only the past 12 months of originations will be effective in limiting reporting burden.

Finally, we note that certain changes to questions on the proposed applications would be needed to reflect the changes to the certification requirements recommended in this comment.

XI. Conclusion

Thank you for considering these comments. We would be happy to discuss them further.

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(see following page for Appendix)

<u>Appendix</u>

Screenshot from Fig Loans website showing CDFI seal beside an example rate of 190% APR