

## **An Overview of Special-Purpose Credit Programs Under the Equal Credit Opportunity Act**

*By Kenneth Benton, Principal Consumer Regulations Specialist, Federal Reserve Bank of Philadelphia<sup>1</sup>*

### **Abstract**

The Equal Credit Opportunity Act (ECOA) and the Fair Housing Act (FHA) generally prohibit creditors from considering certain protected characteristics (such as race, religion, or color) in credit and housing transactions. But the ECOA has an exception for a special purpose credit program (SPCP) that permits creditors to specifically target certain groups of persons and businesses to meet special social needs or to help economically disadvantaged classes of persons. Among other requirements, the creditor must determine the class of persons it is targeting would otherwise be denied credit or receive it on less favorable terms under the creditor's existing credit standards. For example, a creditor might determine that if it used alternative credit data instead of credit scores to qualify Hispanic mortgage applicants in low- to moderate-income (LMI) census tracts, they would likely receive a lower interest rate, so it could create an SPCP targeting these borrowers. After regulators clarified requirements for SPCPs and encouraged lenders to consider them, the number of creditors offering SPCPs has rapidly grown.

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<sup>1</sup> The views expressed here are solely those of the author and do not necessarily reflect the views of the Federal Reserve Bank of Philadelphia or the Federal Reserve System.

## Introduction

To address discrimination in housing and credit transactions, Congress passed the Fair Housing Act (FHA) in 1968 and the Equal Credit Opportunity Act (ECOA) in 1974. These federal fair lending laws prohibit discrimination on the following bases:

Law	Scope	Prohibited bases
ECOA	consumer and commercial credit transactions	<ul style="list-style-type: none"> <li>• race</li> <li>• color</li> <li>• religion</li> <li>• national origin</li> <li>• sex (including gender identity and sexual orientation)</li> <li>• marital status</li> <li>• age</li> <li>• receipt of income from a public assistance program</li> <li>• exercising rights under the Consumer Credit Protection Act</li> </ul>
FHA	residential housing transactions, including mortgage loans	<ul style="list-style-type: none"> <li>• race</li> <li>• color</li> <li>• religion</li> <li>• sex (including gender identity and sexual orientation)</li> <li>• disability</li> <li>• familial status</li> <li>• national origin</li> </ul>

Fair lending violations present significant risks for a bank not only because of the harm to the applicant or borrower but also because of the harm to the bank's reputation and the risk that its regulator will refer the issue to the Department of Justice for further investigation and remediation if it's a pattern or practice.<sup>2</sup> As a result, lenders train their staff to not consider any of the prohibited bases listed in the table in their credit and housing transactions.

Congress created an exception to these requirements in the ECOA 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.<sup>3</sup> Provided all the requirements for an

<sup>2</sup> The ECOA requires regulators to refer a pattern or practice of discouraging or denying credit to the Department of Justice and also permits discretionary referral of a single violation for discriminating in any aspect of a credit transaction on a prohibited basis. 15 U.S.C. § 1691e(G).

<sup>3</sup> See 12 U.S.C. §1691(c); 12 C.F.R. §1002.8(b)(2).

SPCP are satisfied, a creditor may target applicants on a prohibited basis<sup>4</sup> and deny applicants who do not meet the eligibility requirements.<sup>5</sup>

Although SPCPs have been available since 1976, when they were added to the ECOA,<sup>6</sup> they have not been widely implemented. When the Department of Housing and Urban Development (HUD) and other agencies asked lenders about this, lenders said 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.”<sup>7</sup>

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.<sup>8</sup> Following this guidance, several federal agencies issued an interagency statement that encourages lenders to consider SPCPs,<sup>9</sup> and HUD issued guidance to clarify that a compliant SPCP generally does not violate the FHA.<sup>10</sup>

This article (1) discusses the requirements for establishing a compliant SPCP, (2) provides examples of SPCPs that some financial institutions have implemented, (3) reviews the recent plans of government-sponsored enterprises (GSEs) in this space, and (4) provides an update on the Community Reinvestment Act (CRA) and SPCPs in the 2022 CRA rulemaking proposal.

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<sup>4</sup> 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.”

<sup>5</sup> 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] offered by a profit-making organization to meet special social needs...*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.”

<sup>6</sup> See [Equal Credit Opportunity Act Amendments of 1976](#), Pub. L. 94-23, 90 Stat. 251, March 23, 1976.

<sup>7</sup> 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.”

<sup>8</sup> See [86 Federal Register 3762](#), 3763 (January 15, 2021).

<sup>9</sup> See [“Interagency Statement on Special Purpose Credit Programs Under the Equal Credit Opportunity Act and Regulation B.”](#) February 22, 2022.

<sup>10</sup> 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 B](#), December 6, 2021.

## SPCPs Under the ECOA

The ECOA authorizes three different types of 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
- An SPCP offered by a profit-making organization to meet special social needs, according to the standards prescribed in the Bureau's regulations<sup>11</sup>

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."<sup>12</sup>

### Requirements for SPCPs Offered by For-Profit 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.<sup>13</sup>

Here are the details of these requirements:

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<sup>11</sup> 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).

<sup>12</sup> See Senate Report 94-589, 1976 U.S.C.C.A.N. at 409.

<sup>13</sup> See 12 C.F.R. §1002.8(a)(3).

### *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.<sup>14</sup>

### *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.”<sup>15</sup> So, 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 classes of persons an SPCP could target:

- minority residents of LMI 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
- residents living on tribal lands<sup>16</sup>

### *Procedures and Standards*

The SPCP must include the procedures and standards for extending credit and must 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.<sup>17</sup>

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.<sup>18</sup>

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-

<sup>14</sup> See 12 C.F.R. §1002.8(a)(3); 86 *Federal Register* at 3764–65.

<sup>15</sup> See Comment 8(a)-5.

<sup>16</sup> See 86 *Federal Register* at 3765.

<sup>17</sup> See 12 C.F.R. §1002.8(a)(3).

<sup>18</sup> See 87 *Federal Register* at 3765.

year requirement would likely prevent women-owned businesses from qualifying for small business credit.<sup>19</sup>

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.<sup>20</sup> 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, that an SPCP may permissibly request.<sup>21</sup>

#### *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 a 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 first. If the creditor extends the program beyond the plan's date, it must document the extension.

#### *Description of Analysis*

The comments for Regulation B specify that a written plan "must contain information that supports the need for the particular program."<sup>22</sup> To that end, the plan must describe or incorporate the analysis determining the program is needed. A creditor can conduct a broad analysis using internal data, such as its own research, or other 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 create 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 (CA) Letter 19-11 for more information.<sup>23</sup>

#### *Nexus to the Organization's Customary Credit Standards*

A key element of the written plan is establishing that "a class of persons who would otherwise be denied credit or would receive it on less favorable terms" under the

<sup>19</sup> See 87 *Federal Register* at 3765.

<sup>20</sup> See 87 *Federal Register* at 3765.

<sup>21</sup> See Comment 8(c)-1.

<sup>22</sup> See Comment 8(a)-5.

<sup>23</sup> See <https://www.federalreserve.gov/supervisionreg/caletters/caltr1911.htm/>.

creditor's existing credit standards.<sup>24</sup> 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 resulted in a disproportionate number of denials of 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 with insufficient savings to qualify for its mortgage loans (or to qualify, but on less favorable terms, such as a higher interest rate) and will offer them down payment assistance funds under an SPCP. The plan could document that the creditor 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., Hispanic applicants 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 and if the program otherwise satisfies the applicable 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.***<sup>25</sup>

However, if an SPCP has not yet been established, a creditor cannot request demographic information that it is otherwise prohibited from collecting.<sup>26</sup> Instead, the creditor may use statistical methods to estimate demographic characteristics. Similarly, before an SPCP is established, the creditor may not collect demographic information for a preliminary analysis.

Once an 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 LMI

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<sup>24</sup> See Comment 8(a)-5.

<sup>25</sup> See 86 *Federal Register* at 3764.

<sup>26</sup> See 86 *Federal Register* at 3766.

census tract and be Black, Hispanic, or Asian. The creditor could request race or ethnicity information from applicants to confirm eligibility for this program.<sup>27</sup>

### **Discrimination Among Members of the Targeted Class of Persons Is 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.<sup>28</sup>

### **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 an SPCP targets.<sup>29</sup> However, the creditor is still required to provide an adverse action notice to the applicant.<sup>30</sup>

### **SPCP Examples**

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

- eliminating a down payment requirement and closing costs for first-time homebuyers in certain markets with large populations of Black and Hispanic residents;<sup>31</sup>
- allowing low down payments, eliminating the mortgage insurance requirement, and increasing lender-paid assistance programs in majority-Black and majority-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

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<sup>27</sup> See 86 *Federal Register* at 3764.

<sup>28</sup> 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*.

<sup>29</sup> See 12 U.S.C. §1691(c).

<sup>30</sup> 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.”

<sup>31</sup> See [“Bank of America Introduces Community Affordable Loan Solution to Expand Homeownership Opportunities in Black/African American and Hispanic-Latino Communities.”](#) August 30, 2022.



credit scores and other underwriting variables and by relying more heavily on cash flow analysis, an alternative credit data tool;<sup>32</sup>

- identifying existing minority mortgage home borrowers with the bank who would benefit from refinancing their loan at a lower rate;<sup>33</sup> and
- providing a \$5,000 lender credit and more flexible underwriting standards for mortgage loans in the Black and Hispanic communities the bank serves.<sup>34</sup>

## SPCPs and the CRA

The 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 LMI individuals?”<sup>35</sup> A final CRA rule is expected to be issued in 2023.

## SPCPs and GSEs

Freddie Mac and Fannie Mae recently published their plans to develop and implement SPCPs, including purchasing loans from lenders issued under an SPCP. This development enhances the liquidity of SPCP loans.

### *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 underserved minority communities.”<sup>36</sup> This includes:

- purchasing SPCP loans;

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<sup>32</sup> See David Benoit, AnnaMaria Andriotisc, “[Citigroup Joins Industry Effort to Lend to People Without Credit Scores.](#)” *The 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 to the borrower and generally derived from reliable sources, such as bank account records, which may help ensure the data’s accuracy.”

<sup>33</sup> See “[Wells Fargo Expands Efforts to Advance Racial Equity in Homeownership.](#)” April 13, 2022.

<sup>34</sup> See “[TD Bank Introduces New Mortgage Loan Product Designed for Minority Communities.](#)” March 2, 2022.

<sup>35</sup> See [87 Federal Register 33884](#), 33968, June 3, 2022.

<sup>36</sup> See “[Freddie Mac Announces Landmark Equitable Housing Finance Plan.](#)” June 8, 2022.

- offering a FreddieMac SPCP; and
- developing a geotargeted approach to SPCPs, such as targeting majority–minority census tracts.<sup>37</sup>

### *Fannie Mae*

Fannie Mae announced in its Equitable Housing Finance Plan<sup>38</sup> 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”<sup>39</sup>; and
- 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 FHA 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 concerns that: (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 FHA, which prohibits discrimination in housing on a prohibited basis.<sup>40</sup> 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.<sup>41</sup> In support, the opinion noted the rule of construction that similar statutes should be interpreted similarly. Since the ECOA and the FHA both prohibit “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

<sup>37</sup> See [Freddie Mac Equitable Housing Plan](#), p. 17.

<sup>38</sup> See [Fannie Mae Equitable Housing Finance Plan](#), p. 10.

<sup>39</sup> See [Fannie Mae Equitable Housing Finance Plan](#), p. 10.

<sup>40</sup> See [86 Federal Register 3762, 3763](#) (January 15, 2021); “[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, p.2-3.

<sup>41</sup> See [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 B](#), December 6, 2021.

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.<sup>42</sup>

After HUD's general counsel confirmed that the SPCPs do not generally violate the FHA, HUD's Office of Fair Housing and Equal Opportunity (OFHEO) 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.<sup>43</sup>

### **The Interagency Statement of SPCPs**

After the Bureau and HUD issued their SPCP guidance, the federal banking agencies, the 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."<sup>44</sup>

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<sup>42</sup> See [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 B](#), December 6, 2021.

<sup>43</sup> 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, p.3.

<sup>44</sup> 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.

## Conclusion

SPCPs provide a framework for financial institutions to create credit programs to help address special social needs while still 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.