Mr. David Pace

Manager of Regulatory Advocacy,

League of Southeastern Credit Unions

2810 Premiere Parkway, Suite 150

Duluth, GA 30097

Mrs. Sandra L. Thompson

Director,

Federal Housing Finance Agency

Office of the Director

400 7th Street, S.W., 10th floor

Washington, DC 20219

Re: FinTech in Housing Finance

10/16/2022

To Director Thompson:

The League of Southeastern Credit Unions (“LSCU”) representing 310 credit unions with a collective asset size over $176 billion is always looking for items to comment on that might have an impact on our member credit unions. The Federal Housing Finance Agency’s (“FHFA’s”) recent request for information (“RFI”) regarding FinTech and Housing Finance is of interest to us as we hope to see FinTech and traditional finance working together to create a more seamless lending process in all areas, including home lending. FinTech currently resides in a grey area for regulators as their global nature can make it hard to police and regulate them. This lack of regulation can be a hinderance to the interoperability of FinTech with traditional finance, which should be the goal of the government as better compatibility between FinTech and regular financial institutions can improve the security of the wider financial system.

We would define FinTech in the primary and secondary mortgage market as being a company that offers mortgage services that operates wholly online, either through an app or a website. Currently, FinTechs typically operate as a middleman between traditional finance and borrowers. In these cases, the FinTech is providing the service of easier loan paperwork filing than the traditional financial institution might offer. On the other hand, there are FinTechs that do the mortgage lending process from start to finish and could be considered all-in-one apps in this regard. These all-in-one apps are areas where the FHFA could better explore responsible innovation regarding these companies. Traditional financial institutions have faced heavy scrutiny and tight regulations in the realm of mortgage lending, especially since the Great Recession of 2008. These regulations have slowed down innovation in the traditional financial space for home lending, whereas FinTech has faced much lighter regulatory scrutiny and has made leaps and bounds in terms of innovation. This innovation, which is great for consumers, creates a seamless lending process, however, we are concerned about the possible regulatory risk that these loans may pose. We do not wish to see the innovation of the FinTech sector be stifled by over regulation, but we do think that more government oversight may ensure the integrity of the mortgage lending industry. FinTech has been rapidly expanding in the mortgage lending space, but the overwhelming majority of loans are still coming from traditional financial institutions. This is mainly due to the momentum that already exists in the mortgage market and the comfort that consumers feel from getting a mortgage from a bank or credit union that they know as opposed to a brand new app that they find on the app store. If FinTech wishes to continue its rapid expansion, it will need to work with credit unions and banks in order to build up their reputation as trustworthy sources of loans. Laws protecting the privacy of all documents filed with FinTech companies could also encourage wider adoption of the technology. Many people found it repellent several years ago when it was found that major social media companies were selling their data to advertisers and data aggregators. The general public has largely moved beyond these concerns in regard to their personal information, but financial information is a much more sensitive issue. Even if the data is anonymized and aggregated before being sold, we feel that people would be highly opposed to this. Therefore, protections in this area may be necessary to further FinTech adoption.

The primary benefit of FinTech for the housing market is the speed and ease with which it can process applications. According to a study referenced by the IMF, FinTech mortgages are processed faster and often at a lower cost than traditional lenders1. This is important as according to the same IMF paper, FinTech is a key lender for low-income households. This is why we believe greater partnership between FinTech, and traditional finance is important as there are millions of Americans who are considered unbanked in the US2. This resonates with the credit union industry as our motto is “people helping people” and our member credit unions often go to great lengths to serve those who are not served by large financial institutions like big banks. Partnering with FinTechs could help alleviate some of the slower elements in the mortgage application process. On average, the mortgage application process takes about 30 days to complete with it stretching as long as 45 to 60 days if there are issues with the application for credit3. One of the slowest elements of the mortgage lending process is getting an appraisal for the home. This is a federal mandate and cannot be avoided but some FinTech companies have found some interesting work arounds to deal with this process. One of the interesting work arounds we have heard of to speed up the appraisal process is by having someone do a walkthrough of a home that needs to be appraised using a smartphone to record everything and then an AI will generate a 3D floorplan that can be assessed by an appraiser without the appraiser ever needing to visit the home1. With technology like this it can be assumed there are few data based problems that are hindering the adoption of FinTech. Much of the issues lie in outdated regulations that slow down the lending process. Laws like the Home Mortgage Disclosure Act (“HMDA”) and the Truth in Lending Act (“TIL”) do not account for how technology could be used to reshape the lending process and as such slow down new FinTech companies and traditional financial institutions. Reexamining these acts to better align them with the technological reality of the modern world would go a long way toward improving the ability of FinTech to expand in the mortgage market.

1 International Monetary Fund, Ratna Sahay, Ulric Eriksson von Allmen, Amina Lahreche, Purva Khera, Sumiko Ogawa, Majid Bazarbash, and Kimberly Beaton, The Promise of Fintech: Financial Inclusion in the Post COVID-19 Era § (2020). <https://www.imf.org/en/Publications/Departmental-Papers-Policy-Papers/Issues/2020/06/29/The-Promise-of-Fintech-Financial-Inclusion-in-the-Post-COVID-19-Era-48623>.

2 “How America Banks: Household Use of Banking and Financial Services, 2019 FDIC Survey.” FDIC. Federal Deposit Insurance Corporation, December 17, 2021. <https://www.fdic.gov/analysis/household-survey/index.html>.

3 Evans, Julie. “How Long Does It Take to Get a Mortgage?” realtor.com, March 12, 2022. <https://www.realtor.com/advice/finance/how-long-does-it-take-to-get-a-mortgage/>.

FinTech by its very nature is making the lending process more equitable and makes it easier for low-income individuals to get access to credit. Thanks to its everywhere, all the time nature, FinTech is able to reach people who live in banking deserts across the country. According to the Federal Reserve, roughly 3.74 million people live in banking deserts across the country2. These apps go a long ways in improving access to credit for individuals may not be able to get it any other way. There is a potential risk with this, however. Apps can be created quickly and uploaded to the app store with little regard for their legitimacy and then could be used as a tool for fraudsters to steal funds or personal information. Often times these apps can be created to look like the apps of already existent financial institutions or legitimate FinTech companies3. This has proven to be a major problem. Although it has become a more common issue outside of America, there is still the potential of becoming a major issue over here as well. The FHFA or other regulatory entities may need to look at the rules that govern the addition of new apps to app stores and see if there is a way to curtail this fraud. This may require greater oversight of app stores or special rules for financial apps that requires verification that the entity uploading the app is legitimate. These problems are not insurmountable and should be resolved with better cooperation between FinTech, the government, and traditional finance.

As far as the adoption of new technologies for lending goes, there has been a major hurdle put in place around the use of algorithms for making lending decisions, and that hurdle is the Equal Credit Opportunity Act (“ECOA”). We as a trade association are firmly committed to the belief that an individual has the right to access credit without fear of being discriminated against for their, race, creed, gender, sexual orientation, or other protected class. However, we know that several of our credit unions have either moved away from using algorithms or had to do large reworks of algorithms for violations of ECOAs disparate impact clause. Disparate impact is unlike other protections from discrimination as it does not require proof that the institution accused of discrimination is making a conscious effort to discriminate. This disparate impact section can be something as innocuous as requiring a manual review of a credit application if the applicant is under a certain age. This has been used as grounds to write up credit unions during examinations and this could be used against FinTech companies as well. In order for there to be a wider adoption of algorithms for credit making decisions, a rework of disparate impact should be considered as it is presently holding back this innovation that has shown itself capable of speeding up the lending process. Algorithms have a far lower risk of discriminating against a borrower than a human would, and the government should be encouraging their adoption rather than overly scrutinizing them. We understand that protections for protected classes are necessary, but we respectfully request the administration consider how their focus on anti-discriminatory practices may hinder the growth of new technologies.

1 Cantu, Tony. “Fintech Firm Seeks to Modernize Appraisal Process.” Mortgage Professional. Mortgage Professional, March 22, 2022. <https://www.mpamag.com/us/news/general/fintech-firm-seeks-to-modernize-appraisal-process/399527>.

2 Dahl, Drew, and Michelle Franke. “Banking Deserts Become a Concern as Branches Dry Up.” Saint Louis Fed. Federal Reserve Bank of St. Louis, July 25, 2017. <https://www.stlouisfed.org/publications/regional-economist/second-quarter-2017/banking-deserts-become-a-concern-as-branches-dry-up>.

3 Stefanko, Lukas. “Fake Finance Apps on Google Play Target Users From Around the World.” WeLiveSecurity. eset Digital Technology, September 19, 2018. <https://www.welivesecurity.com/2018/09/19/fake-finance-apps-google-play-target-around-world/>.

The risk that FinTechs pose to the housing market and economy overall is fairly minimal at the moment. FinTech is growing rapidly but accounts for a very small percentage of mortgages that are originated in the US. There is a minor risk in that most FinTech companies serve low-income households which means that many of their loans could be considered subprime. So long as these FinTech companies are following the rules set out in the Dodd-Frank Act regarding subprime loans then this should not be a problem for the housing market. So long as there is proper oversight of FinTech in regard to mortgage lending then the threat it could pose to the economy as it grows will be minimal. The financial system is well aware of the risks that failures in the housing market can cause for the wider economy, but we feel that the regulations put in place after the Great Recession are more than enough to ensure that a repeat does not happen again.

We are highly optimistic about the ability of FinTech to reshape the mortgage market and we want to support this effort. Nevertheless, we still have concerns regarding oversight of these companies, and we would support the FHFA in ensuring that there is a healthy regulatory framework for these companies. These companies serve an important role offering financial services to low-income households and as such we support them and wish to work closely with them.

We would like to thank the FHFA for the opportunity to comment on this matter. If you would like to discuss this issue or our comments further, please feel free to reach out to us.

Sincerely,

David Pace

Manager of Regulatory Advocacy