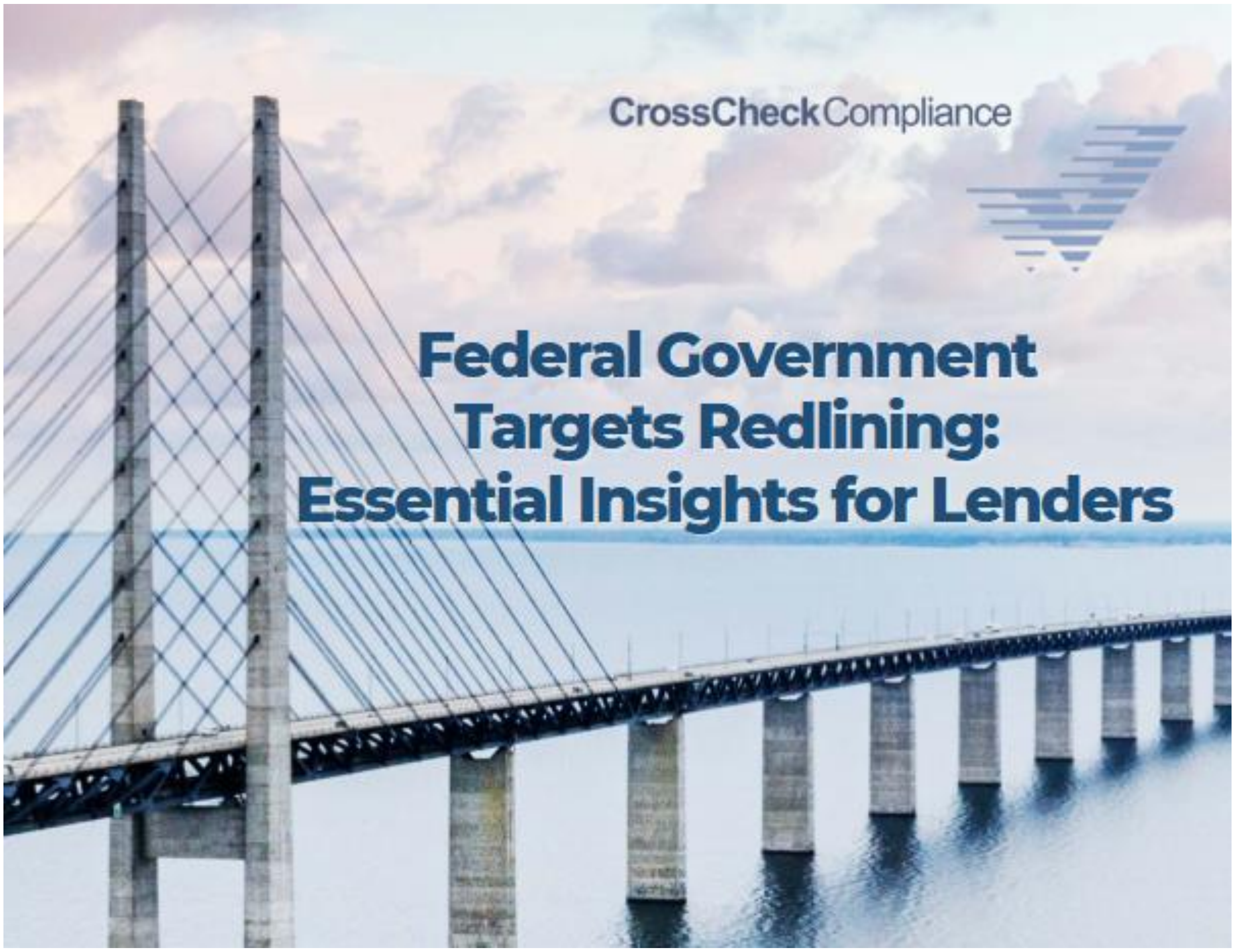
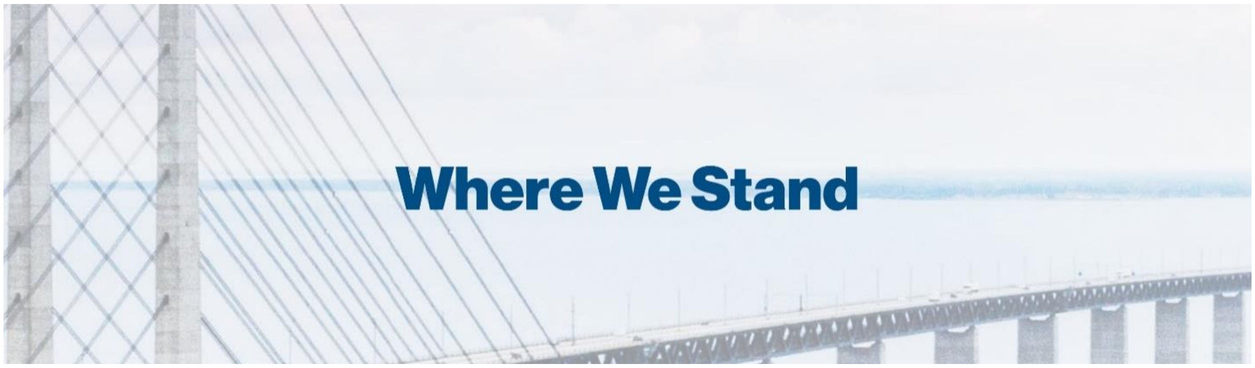


The October 2021 Department of Justice (DOJ) Combatting Redlining Initiative is an aggressive and coordinated effort to eliminate redlining.

Utilizing a whole government approach, the DOJ works with a number of regulators through the financial sector—from the Office of the Comptroller of the Currency to the Consumer Financial Protection Bureau to the National Credit Union Administration, and many other agencies.

Three years later, after the 15th negotiated financial institution settlement, the department certainly seems to have made good on its promise to take “bold” action to crack down on redlining.

The DOJ defines “redlining” as a discriminatory practice where lenders deny or avoid providing mortgages or other credit services to neighborhoods based on the race or national origin of the residents in those neighborhoods.



In October 2024, the DOJ announced two settlements, one with a credit union and one with a mortgage company. That brings the total to 15 institutions that have settled with the DOJ, with over $150 million in penalties assessed so far.

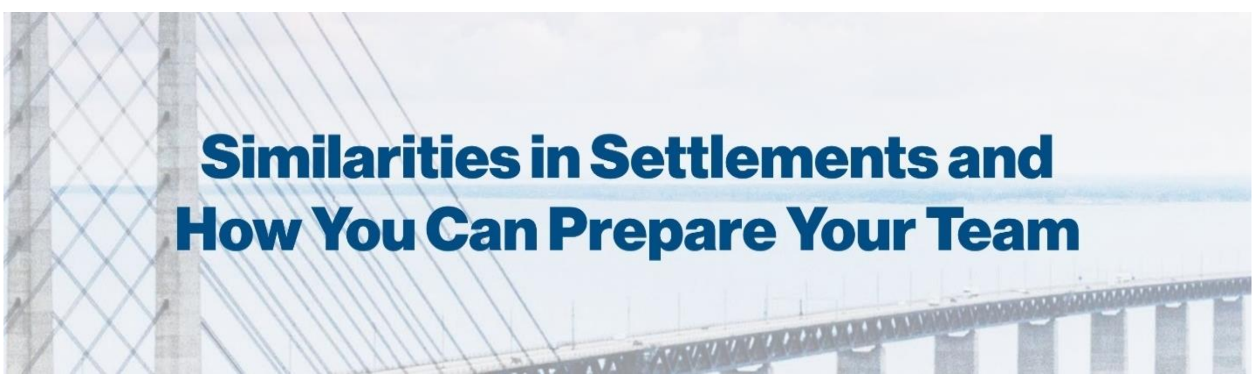
A review of the existing consent orders identifies several trends for companies to consider:

- **Wider range of targets**. Previous efforts have largely focused on depository banks, but the current initiative has expanded that to include non-depository lenders and credit unions.

  In 2023, the CFPB reported that non-depository lenders now account for 63.1% of all mortgage originations, explaining the focus on that sector.

  The recent redlining settlement with a credit union was the first for the DOJ and the DOJ has indicated that there are dozens more investigations pending. More settlements with mortgage companies and credit unions may be forthcoming and should put the industry on notice.

- **Inadequate compliance management systems.** The complaints have cited lenders' deficiencies in preventing discriminatory lending practices due to weak processes and procedures, insufficient monitoring, and limited training.
- **Insufficient engagement with minority communities.** Limited marketing and outreach to majority-minority and low-to-moderate income areas has been highlighted in each case, along with a lack of diverse staffing.



A number of requirements in the settlements thus far are similar, giving an indication of what future settlements could look like. These common obligations include (but are not limited to):

- An injunction against future violations of fair lending laws

- The opening of one or more full-service branches or loan production offices in the affected area
- A community credit needs assessment
- Substantial investments in a residential loan subsidy fund that must be allocated to borrowers in allegedly affected areas for specified purposes
- Donations to community or government organizations that assist with homeownership
- Increased budgets for targeted marketing and outreach in the affected area
- Hiring a director of community lending
- Enhancing fair lending compliance program and risk assessment, including ongoing monitoring.
- Fair lending training.
- Financial education seminars for consumers and loan referral sources in the affected areas.

The DOJ requirements should typically be addressed in your comprehensive fair lending program. Take the following actions to improve your fair lending program:

- **Establish policies, procedures & internal controls.** These elements should be documented and comprehensive. Procedures should be detailed, provide guidance regarding day-to-day activities and limit discretion related to pricing and underwriting.
- **Ensure your training is comprehensive.** Include Fair Housing Act (FHA) and Equal Credit Opportunity Act (ECOA) requirements, among other topics, and tailor your training to all personnel in the lending cycle based on their job responsibilities. Include lenders, processors, administrative staff, board of directors and third-parties (including appraisers, real estate professionals, etc.)
- **Complete a fair lending risk assessment.** Fair lending risk assessment should identify and measure risks throughout the lending life-cycle including product development, marketing, underwriting, pricing, access to credit, etc.
- **Institute continuous monitoring & analysis.** Ongoing monitoring and analysis including levels of assistance, decision and pricing disparities, redlining and steering, etc.
- **Ensure any prior concerns expressed by regulators in examinations are addressed promptly and fully implement any recommendations.** Lenders who disregard regulators' recommendations to identify and address redlining risks are likely to face further scrutiny and increased penalties.
- **Understand the full scope of the communities where the institution lends.** Some lenders could have proactively identified risks by analyzing whether there were nearby communities in majority minority census tracts and/or low-to-moderate income communities adjacent to their lending areas that they could have reasonably served, but

failed to do so. Complete a geographical analysis and mapping of where applications are received and loans originated based on the demographic composition of the area.

- **Engage with community groups with insight about, and experience with, the credit needs of lower-income and minority borrowers.** Community groups play a vital role in linking lenders with potential borrowers, as many of these organizations offer services such as credit counseling programs that create pathways to homeownership. Complete a community credit needs assessment (CCNA) to ensure products and services align with actual needs of the community.
- **Ensure that the institution's compliance management system is accurately measuring redlining risk.** The DOJ often identifies that institutions rely on inadequate metrics, which can create a false sense of security.
- **Maintain governance and oversight.** Board and management should understand risks and ensure the fair lending program is designed and has the necessary resources and funds to mitigate those risks. Management should also oversee the remediation of any prior fair lending compliance issues (monitoring, audit and examination).

Lenders should take adequate measures to protect themselves. A redlining investigation or even complaint could be costly and damaging to your institution's reputation. CrossCheck can assist you with proactively addressing redlining risk. Contact us to learn how we can help.

December 2024