

United States Senate

WASHINGTON, DC 20510

June 10, 2019

The Honorable Jerome H. Powell
Chairman
Board of Governors of the Federal Reserve
System
20th Street and Constitution Avenue NW
Washington, DC 20551

The Honorable Jelena McWilliams
Chairman
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

The Honorable Joseph M. Otting
Comptroller
Office of the Comptroller of the Currency
400 7th Street SW
Washington, DC 20219

The Honorable Kathy Kraninger
Director
Consumer Financial Protection Bureau
1700 G Street NW
Washington, DC 20552

Dear Chairman Powell, Comptroller Otting, Chairman McWilliams, and Director Kraninger:

I write regarding a recently-released analysis which found that the algorithmic models used by financial technology (“FinTech”) companies can result in discriminatory lending outcomes. I am seeking information about the role that your agency can play in ensuring that FinTech platforms serve American borrowers on a nondiscriminatory basis.

Financial institutions have been recently increasing their provision of services through mobile devices or online, with little or no face-to-face interaction with consumers.¹ These financial technology or “FinTech” companies, provide payment services, individual and business loans, financial advice, and more.² FinTech companies often use algorithms to underwrite their loans and help them determine whether a consumer is qualified to receive a mortgage, obtain a credit card, or open a bank account.³ Many of these companies issue loans without any in-person interaction between a lender and a borrower. Traditional lenders are also increasingly using algorithms to supplement or replace their underwriting processes.⁴ While some FinTech products

¹ U.S. Government Accountability Office, “FINANCIAL TECHNOLOGY: Information on Subsectors and Regulatory Oversight,” April 2017, <https://www.gao.gov/assets/690/684187.pdf>.

² U.S. Government Accountability Office, “FINANCIAL TECHNOLOGY: Additional Steps by Regulators Could Better Protect Consumers and Aid Regulatory Oversight,” March 2018, <https://www.gao.gov/assets/700/690803.pdf>.

³ American Banker, “Regulators need to step up their game to stop tech-based discrimination,” Zac Townsend, March 7, 2018, <https://www.americanbanker.com/opinion/regulators-need-to-step-up-their-game-to-stop-tech-based-discrimination>.

⁴ Robert Bartlett, Adair Morse, Richard Stanton, and Nancy Wallace, “Consumer-Lending Discrimination in the Era of FinTech,” October 2018, <https://faculty.haas.berkeley.edu/morse/research/papers/discrim.pdf>.

have the potential to expand access to financial services for underserved populations,⁵ we believe these new business models and products also present new challenges for regulators.

Recent research highlights this tension, demonstrating both the opportunity of algorithmic underwriting's potential to reduce discrimination, while also emphasizing the technologies' current shortcomings. In October 2018, researchers at the University of California, Berkeley released an analysis of millions of mortgages securitized by Fannie Mae and Freddie Mac between 2008 and 2015. This sample included mortgages issues by both traditional and FinTech lenders after both traditional and algorithmic underwriting. Because the credit guarantees by Fannie and Freddie removes all credit risk, researchers were able to isolate prices differentials that were not correlated with risk and may be evidence of either intentional or unintentional discrimination.

Researchers examined whether there were difference between human and algorithmic decision-making in determining whether to issue a loan and at what terms. They expected to find some discrimination in decisions made by humans, but no difference on acceptance rates or terms based on an applicant's race in decisions made by algorithms. They found out that "algorithmic lending," by "increase[ing] competition" in the lending market and making it easier to apply for mortgages, appeared to reduce the likelihood that the loan applications of borrowers of color are rejected—thus reducing discrimination in lenders' "accept/reject" decision-making process.⁶

Other results, however, were less encouraging. Researchers found that "face-to-face and FinTech lenders charge Latinx/African American borrowers 6-9 basis points higher interest rates" than comparable white or Asian-ethnicity borrowers – which is almost identical to the interest rate premium that minority borrowers face with traditional underwriting. In other words, the algorithms used by FinTech lenders are as discriminatory as loan officers. Berkeley researchers estimate that lending discrimination results in Latinx and African American borrowers "pay[ing] \$250-500M per year in extra mortgage interest."⁷

While these results were mixed, this is not an acceptable outcome. There are multiple fair lending laws and regulations in place to address lending discrimination. The Equal Credit Opportunity Act (ECOA) "prohibits discrimination in any aspect of a credit transaction," while the Fair Housing Act (FHA) "prohibits discrimination in all aspects of residential real-estate related transactions," including, but not limited to, mortgages.⁸

⁵ U.S. Government Accountability Office, "FINANCIAL TECHNOLOGY: Information on Subsectors and Regulatory Oversight," April 2017, <https://www.gao.gov/assets/690/684187.pdf>.

⁶ Robert Bartlett, Adair Morse, Richard Stanton, and Nancy Wallace, "Consumer-Lending Discrimination in the Era of FinTech," October 2018, <https://faculty.haas.berkeley.edu/morse/research/papers/discrim.pdf>.

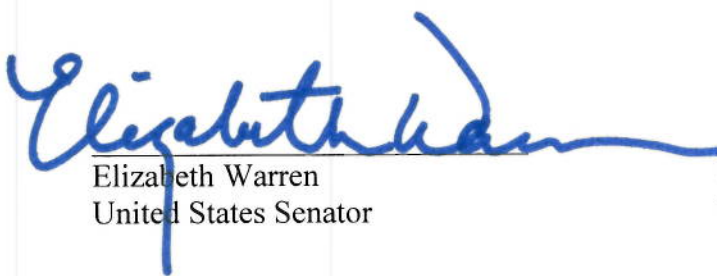
⁷ *Id.*

⁸ Federal Deposit Insurance Corporation, "Consumer Compliance Examination Manual: IV-1.1 Fair Lending Laws and Regulations," September 2015, <https://www.fdic.gov/regulations/compliance/manual/4/iv-1.1.pdf>.

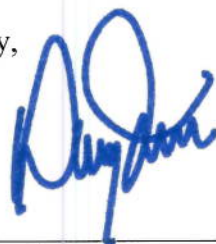
As “consumer loan origination of all types in the United States...become[s] almost exclusively algorithmic,”⁹ the federal government will have to take action to ensure that antidiscrimination laws keep up with innovation. To help me understand the role that [agency name] can play in addressing FinTech discrimination, I ask that you answer the following questions by June 24, 2019.

1. What is your agency doing to identify and combat lending discrimination by lenders who use algorithms for underwriting?
2. What is the responsibility of your agency with regards to overseeing and enforcing fair lending laws? To what extent do these responsibilities extend to the FinTech industry or the use of FinTech algorithms by traditional lenders?
3. Has your agency conducted any analyses of the impact of FinTech companies or use of FinTech algorithms on minority borrowers, including differences in credit availability and pricing? If so, what have these analyses concluded? If not, does your agency plan to conduct these analyses in the future?
4. Has your agency identified any unique challenges to oversight and enforcement of fair lending laws posed by the FinTech industry? If so, how are you addressing these challenges?
5. Has your agency identified increased cases of lending discrimination in financial institutions that participate in the FinTech industry? Are there additional statutory authorities that would help your agency enforce fair lending laws or protect minority borrowers from discrimination in their interactions with the FinTech industry?

Sincerely,



Elizabeth Warren
United States Senator



Doug Jones
United States Senator

⁹ Robert Bartlett, Adair Morse, Richard Stanton, and Nancy Wallace, “Consumer-Lending Discrimination in the Era of FinTech,” October 2018, <https://faculty.haas.berkeley.edu/morse/research/papers/discrim.pdf>.