

**FEDERAL HOUSING FINANCE AGENCY**

**12 CFR Part 1282**

**RIN 2590-AB22**

**Enterprise Duty to Serve Underserved Markets – Colonia Census Tract**

**Amendments**

**AGENCY:** Federal Housing Finance Agency.

**ACTION:** Final rule.

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**SUMMARY:** The Federal Housing Finance Agency (FHFA) is adopting as final, without change, a proposed rule that amends its Enterprise Duty to Serve Underserved Markets regulation to add a definition of “colonia census tract,” to serve as a census tract-based proxy for a “colonia.” The final rule also amends the definition of “high-needs rural region” in the regulation by substituting “colonia census tract” for “colonia.” In addition, the final rule revises the definition of “rural area” in the regulation to include all colonia census tracts regardless of their location. These changes will make certain activities by the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) (collectively, the Enterprises) in all colonia census tracts eligible for Duty to Serve credit. The intent of the changes is to facilitate the Enterprises’ ability to operationalize their Duty to Serve activities in colonia census tracts and thereby help increase liquidity in these underserved communities.

**DATES:** The final rule is effective July 1, 2023.

**FOR FURTHER INFORMATION CONTACT:** Ted Wartell, Associate Director, Office of Housing and Community Investment, 202-649-3157, [ted.wartell@fhfa.gov](mailto:ted.wartell@fhfa.gov); Marcea Barringer, Supervisory Policy Analyst, Office of Housing and Community Investment, 202-649-3275, [marcea.barringer@fhfa.gov](mailto:marcea.barringer@fhfa.gov); or Dinah Knight, Assistant General Counsel, Office of General Counsel, (202) 748-7801, [dinah.knight@fhfa.gov](mailto:dinah.knight@fhfa.gov), Federal Housing Finance Agency, 400 Seventh Street, SW, Washington, DC 20219. These are not toll-free numbers. For TTY/TRS users with hearing and speech disabilities, dial 711 and ask to be connected to any of the contact numbers above.

**SUPPLEMENTARY INFORMATION:**

**I. Statutory and Regulatory Background**

The Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (Safety and Soundness Act) provides generally that the Enterprises “have an affirmative obligation to facilitate the financing of affordable housing for low- and moderate-income families.”<sup>1</sup> Section 1129 of the Housing and Economic Recovery Act of 2008 (HERA) amended section 1335 of the Safety and Soundness Act to establish a duty for the Enterprises to serve three specified underserved markets in order to increase the liquidity of mortgage investments and improve the distribution of investment capital available for mortgage financing for certain categories of borrowers in those markets.<sup>2</sup> Specifically, the Enterprises are required to provide leadership in developing loan products and flexible underwriting guidelines to facilitate a secondary market for mortgages on housing for very low-, low-, and moderate-income families for the manufactured housing,

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<sup>1</sup> See 12 U.S.C. 4501(7).

<sup>2</sup> See 12 U.S.C. 4565.

affordable housing preservation, and rural housing markets.<sup>3</sup> In addition, section 1335(d)(1) of the Safety and Soundness Act requires FHFA to establish, by regulation, a method for evaluating and rating the Enterprises' compliance with the Duty to Serve underserved markets.<sup>4</sup>

FHFA's current Duty to Serve regulation implements these statutory requirements.<sup>5</sup> Specifically, the regulation requires each Enterprise to adopt a three-year Underserved Markets Plan (Plan) containing the specific objectives and activities the Enterprise will undertake during that time period in each of the three underserved markets.<sup>6</sup> The regulation sets forth specific "Regulatory Activities" under each of the three underserved markets that are eligible for Duty to Serve credit and that an Enterprise may choose to include in its Plan. One such Regulatory Activity in the rural housing market is Enterprise activity in "high-needs rural regions," which are defined to include colonias.<sup>7</sup> The regulation defines a "colonia" as an identifiable community that meets the definition of a colonia under a federal, State, tribal, or local program.<sup>8</sup> The regulation defines a "rural area" as (i) a census tract outside of a metropolitan statistical area (MSA) as designated by the Office of Management and Budget (OMB); or (ii) a census tract in an MSA but outside of the MSA's Urbanized Areas as designated by the U.S. Department of Agriculture's (USDA) Rural-Urban Commuting Area (RUCA) Code #1 and outside of tracts with a housing density of more than 64 housing units per square mile

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<sup>3</sup> See 12 U.S.C. 4565(a). The terms "very low-income," "low-income," and "moderate-income" are defined in 12 U.S.C. 4502.

<sup>4</sup> See 12 U.S.C. 4565(d)(1).

<sup>5</sup> 12 CFR part 1282, subpart C.

<sup>6</sup> 12 CFR 1282.32.

<sup>7</sup> 12 CFR 1282.1, 1282.35(c)(1).

<sup>8</sup> 12 CFR 1282.1.

in USDA's RUCA Code #2.<sup>9</sup>

## **II. Implementation Challenges**

FHFA has identified two main challenges that have hindered the Enterprises' Duty to Serve activities in colonias. The first challenge is an operational one that has prevented the Enterprises from easily identifying and verifying Duty to Serve-eligible loan purchases and outreach activities in colonias. The identification of a colonia under the existing Duty to Service regulation's definition relies on the identification of the community as a colonia using federal, State, tribal, or local definitions. These definitions are based on varied criteria and boundaries. Some rely on descriptive terms that may be meaningful only at the local level, such as neighborhood names, and are generally not tied to any standard geographic identifiers used by lenders such as census tracts. There is no specific, uniform definition of "colonia" that can be easily operationalized and included in a public database that the Enterprises and lenders can check to determine if a particular loan is located in an eligible colonia. As a result, the Enterprises and lenders must engage in a time-consuming and labor-intensive process that is susceptible to error to determine whether a particular loan falls within the specified boundary of a colonia that meets the definition.

In light of these challenges, Fannie Mae engaged a nonprofit organization with research capacities, the Housing Assistance Council (HAC), to conduct research and analysis in an effort to develop a nationwide, usable and programmatic methodology that would enable accurate targeting and tracking of loans in these communities. As part of this research, HAC mapped federal, State, tribal, and local definitions of colonia to census

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<sup>9</sup> 12 CFR 1282.1.

tracts.

The second challenge is related to the ability of the Duty to Serve program to effectively target eligible households in colonias due to the under-inclusion of colonias in the Duty to Serve regulation's existing "rural area" definition. Under the Duty to Serve regulation, an Enterprise is eligible to receive Duty to Serve credit for activities supporting colonias if the activities (*e.g.*, loan purchases) are located in a "colonia," as defined in the regulation, and the colonia is located in a "rural area," as defined in the regulation. FHFA has learned that its definition of "rural area" has unintentionally excluded a large share of colonias from eligibility for Duty to Serve credit.

To address these challenges, FHFA published a Notice of Proposed Rulemaking (NPRM or proposed rule) in the *Federal Register* on October 5, 2022, that proposed to amend the Duty to Serve regulation to: (1) add a definition of "colonia census tract," meaning a colonia located in a census tract, to serve as a census tract-based proxy for a "colonia"; (2) amend the definition of "high-needs rural region" by substituting "colonia census tract" for "colonia"; and (3) revise the definition of "rural area" to include all colonia census tracts regardless of their location within or outside an MSA. FHFA also specifically requested comments in the proposed rule preamble on the following three questions about the identification and verification of Duty to Serve-eligible activities in colonias:

- *Question 1 -- What are the advantages and disadvantages, if any, to using colonia census tracts instead of colonias, for purposes of identifying and verifying Duty to Serve-eligible activities?*
- *Question 2 -- Are there other ways to identify the geographic areas in which the Enterprises should receive Duty to Serve credit for eligible activities addressing*

*colonias? If so, describe the alternative approach(es) and any advantages and disadvantages over the proposed census tract-based methodology.*

- *Question 3 -- What are the advantages and disadvantages, if any, to revising the Duty to Serve “rural area” definition to incorporate all census tracts that contain a colonia regardless of their location?*

The public comment period on the proposed rule ended on December 5, 2022.<sup>10</sup>

### **III. Public Comments Received on the Proposed Rule**

FHFA received 10 comments in response to the proposed rule. Comments were submitted by Fannie Mae, Freddie Mac, four nonprofit organizations, two policy advocacy organizations, and two individuals. FHFA has reviewed and considered all of the comments. The comments received and FHFA’s responses are summarized by topic in the sections below.

#### *A. Definition added for use of colonia census tracts*

A majority of the commenters supported the proposal to add a definition of “colonia census tract” to mean a census tract containing a colonia, which will serve as a proxy for the colonia. Both Enterprises, the four nonprofit organizations, and the two policy advocacy organizations stated that the proposal would improve and enhance the ability of the Enterprises to meet the credit needs of these high-poverty areas. Several of the commenters stated that the current regulation’s definition of “colonia” does not fully reflect or encompass the evolving geographies and characteristics of colonias.

Commenters stated that the proposed use of “colonia census tracts” as a proxy for colonias would result in a clear, functional, usable, and flexible methodology for

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<sup>10</sup> 87 FR 60331 (Oct. 5, 2022).

identifying and verifying Duty to Serve-eligibility criteria, which would enhance stakeholder certainty with respect to targeting loan purchases and outreach to colonia census tracts.

Commenters stated that the proposed amendments would structurally incentivize the Enterprises to do more for hundreds of communities along the United States-Mexico border and greater southwest, and thereby help to increase liquidity in these underserved communities. Many of the commenters also suggested that the proposed use of colonia census tracts could “create a beneficial ripple effect” if replicated by other federal agencies that have colonia-focused programs. For example, three of the nonprofit organizations projected that widespread implementation of the proposal “would result in the real possibility of economically integrating colonia communities to their surrounding economies, supercharging efforts to address decades of disparities.” One of the policy advocacy organizations also predicted that adoption of the proposal by other federal agencies “could further comprehensive community development efforts to the benefit of all in those communities.”

In response to FHFA’s Question 1 about the advantages and disadvantages of using colonia census tracts instead of colonias for purposes of identifying and verifying Duty to Serve-eligible activities, three nonprofits and the two policy advocacy organizations highlighted the advantages of, as well as their own experiences with, using colonia census tracts. The three nonprofit organizations stressed that the main advantage in using colonia census tracts is that it achieves stability in the methodology while maintaining flexibility to adapt to evolving geographies. Some commenters also stated that federal efforts to define colonias geographically have historically failed due to the

evolving nature and characteristics of colonias, especially since the passage of the North American Free Trade Agreement (NAFTA) in 1994. The commenters noted that shifting geographic footprints, a lack of understanding as to what constitutes a colonia, and deference to contradictory parameters at the state level have all contributed to the failures to define colonias. As a result, the commenters stated that the Enterprises have lacked clear guidance on what counts as Duty to Serve-eligible activities in colonias, rendering any potential efforts to hone best practices in serving these unique communities unworkable. These commenters also emphasized the ease of obtaining, as well as the accuracy of using, colonia census tracts as opposed to the existing Duty to Serve definition of colonia. The commenters also provided examples of how they have successfully used colonia census tracts to target and direct resources to colonias, even when those colonias are surrounded by mixed-income non-colonia communities.

In response to FHFA's Question 2 on whether there are other ways to identify the geographic areas in which the Enterprises should receive Duty to Serve credit for eligible activities addressing colonias, one policy advocacy organization, HAC, noted that it had conducted extensive research and analysis in an effort to develop a nation-wide, usable and programmatic methodology that would enable accurate targeting and tracking of loans in colonias. The commenter stated that it found that other approaches have serious disadvantages when compared to the use of a census tract-based methodology. As a result, the commenter stated that its research, which it described as carefully considered, rigorous, and thoroughly reviewed by experts, concluded that the use of a census tract-based methodology would best enable mortgage lenders and other financial service providers to target and serve colonia communities more efficiently and effectively.

An individual commenter stated that while the proposed amendments would require that the Enterprises serve colonia census tracts, they would not hold the Enterprises accountable for serving colonias themselves, which the commenter further stated could undermine FHFA's rationale for proposing the amendments. Another individual commenter stated that the matters covered by the proposed rule reside with the Department of Housing and Urban Development, not FHFA and the Enterprises, and that the goal for FHFA should be conserving and preserving to put the Enterprises on stronger footing, not mandating more risk or serving the interests of specific administrations or FHFA Directors.

FHFA has considered the comments received on the use of colonia census tracts and continues to be persuaded that adding a definition of "colonia census tract" to serve as a census tract-based proxy for a "colonia" will enhance the ability of the Enterprises to meet the credit needs of these high-poverty areas. A census tract-based approach will also align FHFA's treatment of colonias under the Duty to Serve regulation with other census tract-based standards for Enterprise reporting to FHFA. For example, FHFA collects data at the census tract level to assess compliance with other Duty to Serve requirements and the Enterprise Housing Goals. Specifically, census tracts serve as the basis for identifying other geographically based underserved areas, including low-income areas and area median income to determine affordability and compliance with Duty to Serve and Enterprise Housing Goals objectives.

Regarding the commenter's concern about holding the Enterprises accountable for serving colonias themselves, FHFA will encourage the Enterprises to work with local entities that specifically serve colonias to increase access to credit in these areas.

Regarding the comment on FHFA’s and the Enterprises’ role in this area, FHFA clearly identified and described in the NPRM its statutory authority for regulating the Enterprises’ Duty to Serve responsibilities and activities. These Duty to Serve responsibilities of each Enterprise include developing and executing a Plan describing the specific activities and objectives it will undertake to fulfill its Duty to Serve in each underserved market over a three-year period. In addition, FHFA issues Evaluation Guidance that describes procedures for preparing the Plans and the standards FHFA has established for evaluating and rating Enterprise compliance with the Plans, as well as the impact on each of the underserved markets.<sup>11</sup> Together, these measures establish and communicate a framework and expectations for holding the Enterprises accountable for fulfilling their Duty to Serve responsibilities. FHFA will monitor and evaluate the impact of implementation of this final rule on Enterprise activities in colonia census tracts, and may modify its Evaluation Guidance to address any Enterprise underperformance in this underserved market.

*B. Revising the definitions of “high-needs rural region” and “rural area” to include all colonia census tracts*

A majority of the commenters also supported the proposal to revise the Duty to Serve regulation’s definition of “high-needs rural region” to include colonia census tracts, and to revise the Duty to Serve regulation’s definition of “rural area” to include all colonia census tracts, regardless of their location within or outside an MSA, due to the inherently rural nature and characteristics of all colonia census tracts. In response to

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<sup>11</sup> The current Duty to Serve Evaluation Guidance is *available at*: [https://www.fhfa.gov/PolicyProgramsResearch/Programs/Documents/Evaluation-Guidance\\_2022-5.pdf](https://www.fhfa.gov/PolicyProgramsResearch/Programs/Documents/Evaluation-Guidance_2022-5.pdf).

FHFA's Question 3 about any advantages and disadvantages associated with revising the Duty to Serve "rural area" definition to incorporate all census tracts that contain a colonia regardless of their location, the nonprofit organizations and the policy advocacy organizations pointed out that a colonia's proximity to an MSA does not guarantee that it has access to public utilities and transportation infrastructure. The commenters stated that colonias embody a rural existence because they are often cut off from municipal services and denied integration into the surrounding economy as local governments have chosen not to incorporate them. For these reasons, the commenters described the proposal to include all colonia census tracts, regardless of their location, in the definition of "rural area" as a "commonsense measure" capable of further incentivizing the Enterprises to meet their Duty to Serve obligations. The commenters also highlighted as another benefit associated with revising the "rural area" definition that it would streamline the process of identifying Duty to Serve-eligible loans.

An individual commenter, while acknowledging that colonias are vastly underserved regions with similar characteristics to rural areas regardless of their location, stated that treating all colonia census tracts as rural, regardless of whether they are located within or outside an MSA, would differ from the regulation's use of an MSA-based standard for the other high-needs rural regions, which could lead to confusion and difficulty in implementing the proposed amendments.

A policy advocacy organization recommended that the regulation provide greater, or weighted, Duty to Serve credit for Enterprise activities in colonia census tracts located in rural areas as the latter term is defined in the current regulation, on the basis that the needs in such rural colonia census tracts are even greater than those in urban colonia

census tracts. As an alternative, the commenter suggested that FHFA base the weighting differential on poverty rates rather than location, with greater Duty to Serve credit given to Enterprise activities in the highest poverty tracts.

After considering the comments, FHFA remains persuaded that the proposed amendments to revise the definitions of “high-needs rural region” and “rural area” to include all colonia census tracts, regardless of their location, is appropriate. While FHFA appreciates the recommendation that greater weight be given to Enterprise activities in colonia census tracts located in rural areas as currently defined in the regulation, the final rule does not adopt this suggestion. The NPRM described a number of challenges the Enterprises have encountered over the years in targeting colonias, including operational challenges that have prevented them from easily identifying and verifying Duty to Serve-eligible loan purchases and outreach activities in colonias. Another challenge the Enterprises have faced is their inability to effectively target eligible households in colonias due to the under-inclusion of colonias in the current Duty to Serve regulation’s “rural area” definition. Placing greater weight on Enterprise activities in certain colonia census tracts would introduce a layer of complexity that may detract from the stated objective of the proposed amendments—to facilitate the Enterprises’ ability to operationalize their Duty to Serve activities and thereby help increase liquidity in these underserved communities.

Regarding the comment about the proposal not relying on an MSA-based standard for colonia census tracts as is used for the other high-needs rural regions, FHFA notes that the rationale for departing from this standard was addressed in the NPRM. The NPRM stated that an analysis of 2020 census data found that only 260 of the 577 census

tracts that contain colonias meet the current Duty to Serve “rural area” definition.<sup>12</sup> The remaining 317 colonia census tracts, which are located within an MSA, do not qualify for Duty to Serve credit under the current “rural area” definition.<sup>13</sup> The NPRM also noted that all colonia census tracts have high poverty rates and low housing density, which contribute to limited access to credit for the households in those communities.<sup>14</sup> Based on this analysis, FHFA determined that Enterprise activities in all colonia census tracts—regardless of whether they are located within or outside an MSA—should qualify for Duty to Serve credit. As a result, FHFA is confident that implementation of the amendments will reduce the challenges and difficulties the Enterprises have encountered implementing the current definitions.

Therefore, FHFA believes that it is appropriate to amend the definitions of “high-needs rural region” and “rural area” in § 1282.1(b) to include all colonia census tracts regardless of their location. Accordingly, the final rule amends the definition of “high-needs rural region” by substituting “colonia census tract” for “colonia,” and revises the second component of the “rural area” definition (par. (ii)) to include colonia census tracts that would not otherwise satisfy the “rural area” definition.

### *C. Updating colonia census tract data*

The NPRM discusses how FHFA currently publishes and regularly updates on its website a Rural Areas Data file that specifies the census tracts in the other high-needs rural regions where Enterprise activities are eligible for Duty to Serve credit.<sup>15</sup> FHFA stated in the NPRM that it has not been able to include colonia census tracts in the Rural

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<sup>12</sup> See 87 FR 60335.

<sup>13</sup> *Id.*

<sup>14</sup> See 87 FR 60336.

<sup>15</sup> See 87 FR 60335.

Areas Data file due to the absence of a comprehensive list of census tracts containing colonias. The Rural Areas Data file will be expanded to include colonia census tracts now that the federal, State, tribal, and local definitions of colonia have been mapped to census tracts. The availability of this information in the Rural Areas Data file will make it easier for the Enterprises and lenders to target outreach and loan purchases in these locations, and to assess the impact of efforts to improve housing conditions in these areas.

In the NPRM, FHFA stated that it would periodically update the colonia census tracts included in FHFA's Rural Areas Data file, for use by the Enterprises and other interested parties.<sup>16</sup> A nonprofit organization and a policy advocacy organization supported FHFA's intent to periodically update the colonia census tracts included in the file. The commenters appeared to interpret the word "periodically" to mean once every 10 years, when census tract boundaries are updated in the decennial Census and stated that that cadence may not be sufficient. The commenters noted that more frequent updates by FHFA may be necessary as federal, State, tribal, or local governments may update their definitions of "colonias" more frequently than every 10 years. Both commenters recommended that FHFA provide updates if a significant development or change occurs during the 10-year period after census tract boundaries are updated, such as if new data is developed by a public entity, a major study is issued, or a new investment initiative is introduced.

FHFA agrees that more frequent updates to the colonia census tracts included in the Rural Areas Data file may be necessary during the 10-year period after census tract boundaries are updated. The NPRM described FHFA's plan to periodically update the

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<sup>16</sup> See 87 FR 60337.

colonia census tracts in the file, by which FHFA meant on an “as needed” basis.<sup>17</sup> FHFA also agrees with the types of events the commenters identified as reasons for periodically updating the colonia census tracts in the file. FHFA plans to monitor for significant developments or changes that would necessitate the need to update the colonia census tract data and will include such updates in the file.

*D. Effective date of the final rule*

Both Enterprises provided recommendations on when the final rule should take effect. Fannie Mae expressed concern that if the final rule were to become effective some time after January 1, 2023, the Enterprises would have administrative challenges with applying two different definitions of “high-needs rural region” and “rural area” in 2023, as the current regulation’s definitions would continue to apply until the final rule’s new definitions became effective. Accordingly, Fannie Mae recommended that the final rule be effective on January 1, 2023. Although Freddie Mac did not recommend a specific effective date for the final rule, it requested a three-month implementation period to update its reporting platform.

FHFA has decided to make the final rule’s effective date July 1, 2023, the beginning of the third calendar quarter of 2023. FHFA acknowledges that the Enterprises may encounter administrative challenges associated with applying two different definitions of “high-needs rural region” and “rural area” in 2023. However, as Freddie Mac commented, FHFA recognizes that the Enterprises will need time to prepare for their implementation of the final rule. An effective date of July 1, 2023 will give the Enterprises time after publication of the final rule to notify lenders and other stakeholders

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<sup>17</sup> *Id.*

of the rule's amendments, adjust their marketing strategies and other outreach activities as necessary, and update their reporting platforms to be able to accurately report on loan purchases and other activities in colonia census tracts. In addition, because the Enterprises report to FHFA on their Duty to Serve performance on a quarterly basis, establishing the effective date as the beginning of the third calendar quarter will avoid their having to report based on two different definitions within the same calendar quarter.

#### **IV. Regulatory Flexibility Act**

The Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) requires that a regulation that has a significant economic impact on a substantial number of small entities, small businesses, or small organizations must include an initial regulatory flexibility analysis describing the regulation's impact on small entities. FHFA need not undertake such an analysis if FHFA has certified that the regulation will not have a significant economic impact on a substantial number of small entities (5 U.S.C 605(b)). FHFA has considered the impact of the final rule under the Regulatory Flexibility Act and FHFA certifies that the regulation will not have a significant economic impact on a substantial number of small entities because the regulation only applies to Fannie Mae and Freddie Mac, which are not small entities for purposes of the Regulatory Flexibility Act.

#### **V. Paperwork Reduction Act**

The Paperwork Reduction Act (PRA) (44 U.S.C. 3501 *et seq.*) requires that regulations involving the collection of information receive clearance from the Office of Management and Budget (OMB). The final rule contains no such collection of information requiring OMB approval under the PRA. Therefore, FHFA has not submitted the final rule to OMB for review under the PRA.

## VI. Congressional Review Act

In accordance with the Congressional Review Act (5 U.S.C. 801 *et seq.*), FHFA has determined that this final rule is a major rule and has verified this determination with the Office of Information and Regulatory Affairs of OMB.

### List of Subjects in 12 CFR Part 1282

Mortgages; Reporting and recordkeeping requirements.

For the reasons stated in the preamble, under the authority of 12 U.S.C. 4501, 4502, 4511, 4513, 4526, and 4561-4566, FHFA amends part 1282 of subchapter E of 12 CFR chapter XII, as follows:

#### **PART 1282—ENTERPRISE HOUSING GOALS AND MISSION**

1. The authority citation for part 1282 continues to read as follows:

**Authority:** 12 U.S.C. 4501, 4502, 4511, 4513, 4526, 4561-4566.

2. Amend § 1282.1(b) by:

a. Adding in alphabetical order the definition of “Colonia census tract”;

b. In paragraph (iii) of the definition “High-needs rural region” removing the term “colonia” and adding the term “colonia census tract” in its place; and

c. Revising the definition of “Rural area”.

The additions and revisions read as follows:

#### **§ 1282.1 Definitions.**

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*Colonia census tract*, for purposes of subpart C of this part, means a census tract that contains a colonia.

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