



January 15, 2025

# Regulatory Sandboxes at the Consumer Financial Protection Bureau

Policymakers in recent years have considered implementing regulatory sandboxes in financial services. Regulatory sandboxes are frameworks set up by regulators where firms are exempt from legal risk of certain regulations. Firms that violate the terms of the sandbox are open to potential regulator recourse. Sandboxes typically occur under close regulatory supervision and generally to test a novel product in the marketplace. Regulatory sandboxes in financial services exist at the state level in at least 10 states, internationally in countries such as the United Kingdom, and at the federal level at the Consumer Financial Protection Bureau (CFPB), the topic of this InFocus.

Legislation was introduced in the 118<sup>th</sup> Congress to expand federal regulators' sandbox policies in financial services (e.g., H.R. 9309/S. 4951, H.R. 6584, H.R. 7440, and S. 4919).

## Overview of Sandboxes

Sandboxes are used commonly in a number of industries but prominently in financial services. Regulatory sandboxes can potentially encourage financial firms to test new technologies or lending methods without legal risk. This is because particularly consumer-facing financial firms often worry about regulatory burden and uncertainty associated with novel lending activities. This might be especially beneficial for start-ups, firms making changes to existing products, or firms less familiar with financial regulation. According to the World Bank in 2020, worldwide there were 73 financial technology (“fintech”) sandboxes in 57 different countries.

Generally, sandboxes have an application and approval process, with timelines for firms to receive safe harbor from regulations. Sandboxes are offered for set periods of time to bring products into legal compliance or alleviate regulatory risk as a temporary solution to regulatory uncertainty.

## Regulatory Considerations

Sandboxes are often implemented through “No-Action Letters” (NALs), through which regulators promise not to take legal action against applicants for engaging in activities specified in the NAL. These agreements can be terminated if a firm oversteps the bounds of the NAL. Sandboxes are often accompanied by provisions for baseline consumer protections and sometimes require firms to outline steps to compensate harmed consumers.

Sandboxes are generally offered through the agencies with primary enforcement authority over the laws from which financial institutions are being provided safe harbor. Because firms often have multiple regulators in the United States, sandboxes often contend with multiple regulators.

## Regulatory Sandboxes at the CFPB

While other federal financial regulators, such as the Office of the Comptroller of the Currency and Financial Crimes Enforcement Network, and numerous states have implemented sandboxes, the CFPB has been particularly active in this space in recent years

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank, P.L. 111-203) states that one of the CFPB's statutory objectives is to ensure that “markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation.” Some CFPB directors have exercised this authority to implement regulatory sandbox programs.

While Dodd-Frank expressly requires the CFPB to issue a number of rulemakings, it does not mandate a sandbox regime. Instead, the act gives the CFPB director fairly broad authority to set the CFPB's priorities (12 U.S.C. §5492). This broad discretion, coupled with changes in CFPB leadership, has led to divergent sandbox policies over time.

The CFPB finalized its initial NAL policy in 2016 under the name **Project Catalyst**. Overall, this policy enabled the CFPB to offer NALs to firms with “substantial consumer benefit” where there is “substantial uncertainty” surrounding the application of statutes to that policy. Under this program, in 2017 the CFPB issued a NAL to a nonbank lender called Upstart to utilize alternative data, including education and work history, to underwrite consumer loans.

Following a leadership change at the bureau, the CFPB made additional modifications to the sandbox in 2018 and 2019 and created the **Office of Innovation**. The policy motivation behind this shift was to provide additional regulatory certainty to entities under the sandbox. These changes centered around a more streamlined review process, two new policies, an expansion of NAL coverage, and a partnership with state attorneys general. This office offered programs including a disclosure sandbox, a compliance assistance sandbox, and a revised NAL program. In total, the CFPB granted 10 NALs or other similar orders at the Office of Innovation. These included:

- A new NAL issued to Upstart in November 2020.
- NALs issued to the Bank Policy Institute and Bank of America to experiment with using cash flow in underwriting small dollar loans.
- A Compliance Assistance Statement of Terms (CAST) issued to PayActiv, an Earned Wage Access (EWA)

provider in which the CFPB stated that, because PayActiv's product did not entail a credit risk assessment or mandate fees, it was not "credit," and, therefore, PayActiv would, in offering of the product, have a safe harbor from liability under the Truth in Lending Act.

Following another leadership change, in May 2022 the CFPB opened a new office called the **Office of Competition and Innovation**. Recent CFPB rulemakings and speeches by CFPB leadership have expressed reservations for certain fintech companies and some recent market developments. The CFPB's recent sandbox policy reflected this skepticism. Recent actions under the Biden Administration included the following:

- In June 2022, the CFPB rescinded Upstart's NAL, because the firm wanted to add a "significant" number of new variables to its underwriting and pricing models beyond what was approved in the NAL.
- In June 2022, the CFPB also rescinded PayActiv's CAST, in part as a response to CFPB concerns that the company has suggested that the CFPB endorsed its product. More recently, the CFPB has proposed an interpretative rule on EWA products that arguably contradicts aspects of the PayActiv CAST order.
- In September 2022, the CFPB entirely rescinded its previous policies for its NAL and CAST policies because it now determined that these policies did not facilitate "consumer-beneficial" or "market-wide" innovation. The CFPB kept the Disclosure Sandbox in effect.
- In January 2025, the CFPB issued policy statements with new NAL and CAST policies. These frameworks may be issued only for a "new financial product or service" rather than "minor adjustments" to existing products or services. Additionally, rather than issuing an order to one firm, the CFPB will reach out to the applicant's competitors and grant similar approvals to those firms as well. All applications would be public. The CFPB will not consider applications from former CFPB attorneys or financial firms with federal consumer finance violations in the past five years.

This sandbox policy may also be modified by new leadership at the CFPB.

## Impact on Consumers

Supporters of sandboxes argue that they can benefit consumers, while detractors are concerned with their potential risks to consumers.

Consumer advocates and certain attorneys general have also criticized some of the CFPB's sandbox policies, specifically their duration, the consumer protections offered under an NAL, and the breadth of the legal safe harbors provided. A letter to the Trump-era CFPB by some state attorneys general argued that the CFPB's sandbox policies undermined state action and represented "ill-considered changes."

Advocates, including some state attorneys general, argue that the policies facilitate innovation that will ultimately benefit consumers while maintaining certain consumer protections. Advocates say regulatory sandboxes might aid innovation by providing new products that offer benefits, including decreased prices. Many sandbox applications require firms to describe their explicit consumer protections. Certain state attorneys general have argued that sandboxes provide regulatory certainty for "consumer-benefiting innovation" with consumer safeguards.

## Other Considerations

Because regulatory sandboxes are implemented with one firm at a time, regulators may weigh efficiency and equity concerns in the broader market. Financial firms within sandboxes might benefit from the additional flexibility associated with sandboxes and regulatory certainty. This could lead to novel product development by financial firms. Firms within regulatory sandboxes could engage in regulatory capture, enabling them to reshape broader regulation in their favor at the expense of competitors.

Alternatives to sandboxes may be desirable to achieve similar goals of promoting new product development. For example, some have proposed a "beach" for broader deregulation that does not advantage selected firms, such as widespread safe harbors for particular products. Others have called for decreasing barriers to entry into consumer financial markets and providing informal regulatory guidance to reduce regulatory uncertainty without providing regulatory immunity.

## Selected Legislation

As demonstrated by the CFPB, sandboxes that are implemented by federal financial regulators can often result in fluctuations with changing Administrations and agency leadership. If Congress wants to encourage sandbox development in financial services, engraining such programs in legislation can potentially ensure that sandboxes are more stable with consistent guidelines. Congress could also do nothing and leave sandbox policy development to the discretion of federal financial regulators or mandate certain sandbox protections such as disclosures.

In the 118<sup>th</sup> Congress, H.R. 9309/S. 4951 would have created sandboxes at financial regulatory agencies to execute artificial intelligence projects. H.R. 6584 would have restored the CFPB's sandbox and NAL policies to their 2019 form, including imposing the protections from CFPB legal action. H.R. 7440 would have established Financial Services Innovation Offices to implement sandbox policies at each federal financial regulator. S. 4919 would have created a new office in the Office of Management and Budget that would create a universal sandbox that would potentially exempt firms from agency guidance and rules from across the executive branch.

---

**Karl E. Schneider**, Analyst in Financial Economics

**IF12875**

## Disclaimer

This document was prepared by the Congressional Research Service (CRS). CRS serves as nonpartisan shared staff to congressional committees and Members of Congress. It operates solely at the behest of and under the direction of Congress. Information in a CRS Report should not be relied upon for purposes other than public understanding of information that has been provided by CRS to Members of Congress in connection with CRS's institutional role. CRS Reports, as a work of the United States Government, are not subject to copyright protection in the United States. Any CRS Report may be reproduced and distributed in its entirety without permission from CRS. However, as a CRS Report may include copyrighted images or material from a third party, you may need to obtain the permission of the copyright holder if you wish to copy or otherwise use copyrighted material.