Testimony for the CRA Public Hearings
on assessing bank performance under the Community Reinvestment Act (CRA)

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As a member of the National Community Reinvestment Coalition, and director of Home Repair Resource Center, Cleveland Heights, OH, I thank you for convening these hearings and urge you to embark on a regulatory rulemaking to strengthen the Community Reinvestment Act (CRA). As a HUD counseling agency, we have experienced firsthand the devastation of our neighborhoods caused by predatory lending from unregulated mortgage brokers. Every day we work with clients who are faced with the prospect of losing their homes because they received a mortgage loan that was fashioned by greedy lenders who had not thought or care about the future ability of the homeowner to continue to pay or the impact on the community they live in when they couldn't pay. It is a tragedy and a crime that our whole region is left in the wake of this devastation.

The CRA law requires safe and sound lending, and would have been a preventative cure to the foreclosure crisis had it covered a broader range of institutions. Research conducted by Federal Reserve economists documents that home loans made by banks in their CRA assessment areas are about half as likely to end up in foreclosure as loans issued by independent mortgage companies.[1] In addition, CRA small business and community development lending exceeded $1 trillion for America's neighborhoods from 1996 through 2008.[2]

Meaningful reforms to CRA will ensure economic recovery that promotes sustainable lending to small businesses for job creation and responsible home lending. While we applaud your intentions to improve CRA, regulatory action alone is not sufficient. Congress needs to apply CRA broadly throughout the financial industry in order to maximize safe and sound lending and investment in communities.

Although CRA has been instrumental in boosting lending and investing, the neglect of certain parts of the regulation has meant that CRA has not realized its full potential. If CRA had been updated, the level of CRA-lending and investing would have been substantially higher. In particular, we believe that a regulatory rulemaking should address the following areas:

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[1] Elizabeth Laderman and Carolina Reid, Federal Reserve Bank of San Francisco, "CRA Lending during the Subprime Meltdown in Revisiting the CRA: Perspectives on the Future of the Community Reinvestment Act," a Joint Publication of the Federal Reserve Banks of Boston and San Francisco, February 2009, http://www.frbsf.org/publications/community/cra/cra_lending_during_subprime_meltdown.pdf

[2] Figures calculated by NCRC from data available on http://www.ffiec.gov.

Assessment Areas

As currently defined by the CRA regulation, assessment areas, the geographical locations covered by CRA exams, generally consist of metropolitan areas or counties that contain bank branches. However, while some banks still issue loans predominantly through branches, others make the majority of their loans through brokers and other non-branch means.

As a result of the current definition of assessment areas, the share of all home purchase loans made by banks operating in their CRA assessment areas has dropped to about 25 percent.[3] Narrow assessment areas facilitate problematic lending practices that are not scrutinized on CRA exams. Research demonstrates that lending by institutions not covered by CRA or by banks outside of their assessment areas are more likely to be high-cost.[4]

The Office of Thrift Supervision (OTS) is the one agency that went beyond official assessment areas on CRA exams for non-traditional thrifts, but these exams still examined only a minority of the thrifts' loans. We ask the agencies to significantly improve upon the OTS' precedent and meaningfully include the great majority of bank and thrift loans on CRA exams.

Mandatory Inclusion of Mortgage Company Affiliates on CRA Exams

Under CRA, banks have the option of including their non-depository affiliates, such as mortgage companies, on CRA exams. Banks are tempted to include affiliates on CRA exams if the affiliates perform admirably, but will opt against inclusion if the affiliates are engaged in risky lending or discriminatory policies. We believe the agencies have the authority to include all non-depository affiliate lending on CRA exams to ensure that the lending affirmatively responds to credit needs in a safe and sound manner.

Include Bank Lending and Service to Minorities on CRA Exams

Given the evidence of lending disparities by race, we believe that CRA exams must explicitly examine lending and services to minority borrowers and communities. A large body of research shows that minorities received larger percentages of subprime loans than whites, even after controlling for borrower creditworthiness and other characteristics.[5] Overall, it is probable that considering lending and

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[3] Ren Essene of the Federal Reserve Bank of Boston and William C. Apgar of the Joint Center for Housing Studies, Harvard University, *The 30th Anniversary of the CRA: Restructuring the CRA to Address the Mortgage Finance Revolution*, in Revisiting the CRA: Perspectives on the Future of the CRA, eds. Prabal Chakrabarti et al., A Joint Publication of the Federal Reserve Banks of Boston and San Francisco, 2009.

[4] Robert B. Avery, Kenneth P. Brevoort, and Glenn B. Canner, Higher-Priced Home Lending and the 2005 HMDA Data, Federal Reserve Bulletin, Fall 2006, see page A154.

[5] NCRC, *Foreclosure in the Nation's Capital: How Unfair and Reckless Lending Undermines Homeownership* . Paul S. Calem, Kevin Gillen, and Susan Wachter, *The Neighborhood Distribution of Subprime Mortgage Lending*, October 30, 2002. Available via pcalem@frb.gov. also Paul S. Calem, Jonathan E. Hershaff, and Susan M. Wachter, *Neighborhood Patterns of Subprime Lending: Evidence from Disparate Cities*, in Fannie Mae Foundation's Housing Policy Debate, Volume 15, Issue 3, 2004 pp. 603-622

branching by race of borrower and neighborhood on CRA exams would lessen the racial disparities by encouraging banks to increase their lending and services in communities of color. Before the 1995 changes to the CRA regulation, CRA exams considered lending to minorities as an assessment factor, suggesting the agencies thought they had the authority to consider lending to minorities on CRA exams.

CRA Exam Ratings and Weights

The scale of four possible ratings does not provide meaningful distinctions in performance and has resulted in a 98 to 99 percent pass rate over the last several years. The agencies should introduce Low and High Satisfactory as possible ratings in addition to the four existing ratings. In addition, the agencies should develop better weighting systems so that routine investments like purchasing loans on the secondary market do not receive as much weight as more difficult investments such as equity investments in small businesses.

We do not believe that major changes in CRA examinations are desirable. Some will argue that more banks should be eligible for streamlined exams; we believe that the recent changes went too far in making exams too easy for mid-size banks. Rigorous exams require more safe and sound lending from institutions.

CRA Enforcement Mechanisms

Mergers have traditionally been a major means of CRA enforcement but the frequency of mergers are likely to continue decline over the next several years. Consequently, additional enforcement mechanisms are needed. For instance, banks could be required to submit CRA improvement plans, subject to public comment, when they receive either a low rating overall or in any assessment area. CRA exams and merger approval orders could include an "expectations section" that either mandates or recommends (depending on the extent of the deficiency) improvements to specific aspects of CRA performance such as a particular type of lending or investment.

The agencies must also boost the rigor of the fair lending reviews that probe for evidence of illegal and discriminatory lending. Fair lending reports on CRA exams must be detailed explanations of the fair lending tests used instead of the one or two sentences currently on most CRA exams. In addition, the concept of illegal and discriminatory lending must be expanded to include unsafe and unsound lending. Banks have failed CRA exams because they made or financed unsafe loans; the fair lending review must routinely indicate whether the review found evidence of unsafe and unsound loans.[6]

Some commentators will favor "incentives" to coax institutions into improved CRA performance. We would be supportive of exploring programmatic methods to increase tax credits under the Low Income Housing Tax Credits or New Markets Tax Credit for institutions receiving Outstanding ratings. But we

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[6] See FDIC CRA exam of CIT Bank of May 2008. The bank failed because it purchased high levels of problematic subprime and non-traditional loans. http://www2.fdic.gov/crapes/2008/35575_080512.PDF

are opposed to exemptions from CRA review on merger applications or decreasing the frequency of CRA exams for institutions with Outstanding ratings. CRA performance is likely to decline when institutions receive less frequent exams and public scrutiny.

Data Enhancements

By holding lenders accountable, publicly available data, particularly the Home Mortgage Disclosure Act, has been vital for increasing responsible lending to traditionally underserved borrowers. Applying a similar rationale, the limited CRA small business data must be enhanced to include the race and gender of the small business borrower. In addition, the agencies must require census tract level disclosure of community development loans and investments. In order to promote access to basic banking services, the agencies must require disclosure of enhanced data that shows types of deposit account (such as basic lifeline) by census tract location of the residence of bank customers. Likewise, data on the type consumer lending by borrower demographics and census tracts can promote access to affordable consumer loans and alternatives to abusive payday loans. Improvements in data disclosure will enhance the ability CRA exams to assess if banks are responsive to the full range of credit needs of communities.

Community Development

Some have suggested that banks receive favorable CRA consideration for investing in multi-regional funds for Low Income Housing Tax Credits and other purposes. In the interest of serving diverse geographical areas including rural areas, we are supportive of these suggestions as long as banks have adequately responded to the needs in their assessment areas. A bank could be required to have a rating of Outstanding on the investment test in most assessment areas, for example, before being allowed to invest outside of their assessment areas in multi-regional funds.

Conclusion

The severity of the foreclosure crisis would have been substantially lessened if the entire financial industry had an obligation to serve all communities consistent with safety and soundness. We believe that the regulatory agencies can contribute significantly to ensuring sustainable economic recovery by updating the CRA regulation. In addition, we believe that Congress must do its part and apply CRA to non-bank institutions including mainstream credit unions, independent mortgage companies, insurance firms, and investment banks.

Sincerely,

cc. The National Community Reinvestment Coalition