S. HRG. 102–904

CURRENT STATUS OF THE COMMUNITY REINVESTMENT ACT

HEARING

BEFORE THE

SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

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TUESDAY, SEPTEMBER 15, 1992

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS,
Washington, DC.

The subcommittee met at 10:27 a.m., in room SD–538 of the Dirksen Senate Office Building, Senator Alan Cranston (chairman of the subcommittee) presiding.

OPENING STATEMENT OF SENATOR ALAN CRANSTON

Senator CRANSTON. The hearing will please come to order. I apologize for the delay in convening but we had to have a vote at exactly our convening time on the Senate floor.

This morning the Housing Subcommittee is holding an oversight hearing on the Community Reinvestment Act. CRA was enacted 15 years ago to stop the pervasive and insidious form of discrimination known as redlining, the practice whereby financial institutions literally draw red lines around sections of cities where they refuse to lend.

Discrimination hurts us all. It tears at the fabric of our society. It destroys people, it destroys neighborhoods, and ultimately it can destroy societies.

Eradicating discrimination is a difficult task. Enacting laws is not enough. They must be enforced. We certainly learned that in this particular instance.

As important, attitudes must change. Government cannot legislate these changes in attitudes, but it can and must provide the legal context so that they can occur.

In today's hearing we'll consider what progress we have made in the last decade and a half in eliminating the persistent discrimination that still exists in lending.

The underlying question for this hearing is what is the current status of CRA? Do the deficiencies in the banking system that motivated Congress to pass the law still exist? Do all segments of communities in both rural and urban areas have access to capital?

We do not debate these questions in the abstract, and I think that the answers are unfortunately clear. We saw clearly in Los Angeles 6 months ago what can happen when a community that has been systematically disinvested erupts in rage and frustration. While Los Angeles must be the most prominent example we have, similar problems exist in virtually every major metropolitan area in the country.

We have the honor of having State Senator Joe Neal, of Nevada, here to discuss the problems in Las Vegas.

The Congress and the administration are considering the merits of enterprise zones. This proposal must be discussed in the larger context of sound urban policy. The enterprize zone approach, with its emphasis on tax relief, will only go a small part of the way in meeting the desperate needs of our cities. Access to capital for home ownership, small business, and economic development is even more critical if distressed urban neighborhoods are to be revitalized.

CRA has been inforce for 15 years. Presumably more than enough time to work out any procedural or process problems. Regrettably, that does not appear to have been the case. It seems that we are still struggling with the basics of implementing this law properly.

The agencies charged with enforcing CRA tell us things are fine. They say things are great. Eighty-nine percent of all banks that were evaluated in the last 2 years received a rating of satisfactory or better. In a farewell address to the banking industry, former FDIC chairman William Seidman—whose responsibility it was to enforce CRA—stated that laws requiring banks to invest in local communities were "no longer required or affordable."

The glowing assessment provided by the regulators conflicts with reports this subcommittee has received from community groups and local governments about the banks' performances. They conflict with the numerous studies of different metropolitan areas, including one by the Federal Reserve, which revealed that minorities with comparable incomes are at least twice as likely to be rejected for loan applications as whites.

The regulators' assessment certainly is not supported by recent events in Los Angeles and other cities like Las Vegas.

Finally, these assessments conflict with the data we have heard about the crisis that we faced in affordable housing in Los Angeles.

Where is the disconnect? It appears to be enforcement. The key to the CRA process is the evaluations performed by the regulatory agencies. If the evaluation process is performed well, the CRA system will work.

Because these reports are so critical, I have had my staff review almost 300 of them. The survey suggests deeply disturbing patterns. The first is that, after all of this time, the reports are still woefully inadequate. The quality of the reports ranges from excellent to worthless among the agencies and even within various regions of the same agencies.

This inconsistent performance is totally unacceptable. I can find no reasonable excuse for the agency's failure to meet their obligations to enforce the law properly.

Even more disturbing is the apparent failure of certain agencies to fulfill the requirements of the law when clear patterns of discrimination have been discovered.

I am submitting for the record three instances in which FDIC examiners found clear indications of possible violations of the Equal Credit Opportunity Act and the Federal Fair Housing Act.

In response to inquiries from me, the FDIC stated that although the practices of the banks were questionable, because the banks had agreed to cease these activities, the FDIC determined that no further action was required.

This decision appears to be a direct contradiction with the Federal Deposit Insurance Corporation Improvement Act that requires the regulatory agencies to report to the Department of Justice any time that they have reason to believe that there is a pattern or practice of discrimination. The tendency of agencies to act as protectors of the banks rather than as regulators profoundly distorts this process.

CRA is arguably the most important Federal tool for increasing private lending in the inner cities and in impoverished rural areas. Yet we see a well orchestrated campaign under way within the banking industry to eviscerate CRA. There are a number of legislative proposals pending before Congress, the most recent from President Bush, whose intent is to neutralize the CRA.

I believe this campaign is misguided and serves the banking community and all communities very poorly. CRA is good business. We have witnesses here today who will describe thriving markets in low- and moderate-income areas. In the highly competitive banking field, it seems imprudent for banks to overlook these opportunities. It is good business for a bank to know how many loans it originated and where they were located. It is good business to know whether marketing efforts are working.

Most important, giving all segments of society the economic opportunity to improve their lives is not only good business, it is the right thing to do.

I look forward to hearing from witnesses as to how we can do better business with and through CRA.

And I would now like to turn to Senator Bryan from Nevada for any opening comments he would like to make.

OPENING REMARKS OF SENATOR RICHARD H. BRYAN

Senator BRYAN. Mr. Chairman, let me preface my comment this morning by expressing my appreciation to you for your leadership on this issue and for convening this important hearing this morning. I have a statement which I would like to ask with unanimous consent be made a part of the record.

I thank the Chair.

But I would like to say, on a personal note, that Senator Joe Neal who joins us this morning and who you have been kind enough to acknowledge, is a person with whom I had the privilege 20 years ago of being elected to serve in the State senate. He has been an active community leader. He has spent a considerable amount of time studying this issue as well as others that affect low-income neighborhoods in our own community.

And I must say, on a personal note, that I am delighted that he is here this morning and look forward to his testimony and his wisdom and enlightenment as I did some 20 years ago when we sat side by side in the Nevada Legislature, and I thank you, Mr. Chairman. I, too, look forward to hearing the rest of the witnesses as well.

PREPARED STATEMENT OF SENATOR RICHARD H. BRYAN

I want to commend you, Mr. Chairman, for holding this hearing on the Community Reinvestment Act—15 years later. The CRA has been an important tool for low- and moderate-income neighborhoods to access private capital for community development.

I am pleased to introduce Nevada State Senator Joseph Neal. A State Senator for 20 years, he has been a leader in Nevada advocating for the needs of the West Las Vegas citizenry. He has spent much time studying the Community Reinvestment Act and how it can benefit residents of low-income neighborhoods.

I am also pleased to see representatives of the banking industry here today. I believe it is important for us to hear how they are meeting the credit needs of their communities and how the Act is working after FIRREA modifications.

The effectiveness of the Community Reinvestment Act is especially important as we grapple with ways to stimulate our economy. Access to capital is the only means individuals and businesses have for economic growth, opportunity, and jobs. People who are invested in their neighborhoods take pride in ownership and prosperity. The availability of financial resources assist communities in eradicating poverty and hopelessness. This is true in the inner-cities as well as in small rural areas.

I look forward to the testimony from our witnesses today. Private investment in our troubled communities is an admirable goal and we are eager to hear the record of 15 years of CRA.

Senator CRANSTON. I would like now to ask the first panel of witnesses to come forward and take their places at the witness table.

I want to thank each of you for coming from so far, from Los Angeles and Nevada, to participate in today's hearing.

I ask that each of you begin with your opening statement. Please keep it as brief as you can so that we can hear from all of our witnesses and have some time for questions and give and take.

Whoever of you would like to lead off, please do so.

Ms. Butler, since you're in the middle, why don't you go first.

Ms. BUTLER. I'll be happy to, Senator.

STATEMENT OF SHARON BUTLER, VICE PRESIDENT, COMMUNITY DEVELOPMENT, GREAT WESTERN BANK, LOS ANGELES, CA

Ms. BUTLER. Mr. Chairman, members of the subcommittee, I thank you very much for the opportunity to testify today on the Community Reinvestment Act.

Mr. Chairman, you are aware that Great Western Bank is located in Los Angeles, CA, and so we are most pleased to be here.

On behalf of the Great Western Bank, I commend you, Mr. Chairman, as well as others of the subcommittee for your willingness to have hearings on this subject.

I am Sharon Butler, vice president of Community Development for Great Western Bank, a Federal savings bank, the principal subsidiary of Great Western Financial Corporation, with $38.6 billion in assets.

Great Western is one of the Nation's leading residential real estate lenders, with 190 home loan offices in 21 States. In California, our home State, Great Western ranks first in mortgage market share for purchase loans zero to $1 million. In our home town of Los Angeles, we are also number one.

Mr. Chairman, at the end of last year, Great Western had nearly one third of its home mortgage portfolio, some $12 billion, in low- or moderate-income or minority neighborhoods. In South Los Angeles where we have long been the leading home mortgage lender, Great Western wrote more than $260 million worth of home loans over the past 2 years. That made home ownership possible for more than 2,200 African-American and Latino families.

We are very proud of this record. We know that many believe lenders will not or cannot operate in the inner cities of America. Great Western's message today is that lenders can and will invest in all communities.

We also know that many believe that investment will be made only as a result of the requirements of the Community Reinvestment Act. Great Western's message today is that our lending record is the result of fundamental business strategies, strategies that were in place before the Community Reinvestment Act came into existence and strategies that we would pursue if there were no CRA.

These strategies are built around several simple elements. First, we believe smaller balance loans made to people where they live are less risky than the more speculative loans at the upper end of the scale. So we have consciously targeted our efforts at the affordable end of the housing market.

Second, once you have made that assumption, it is only logical to open or maintain lending offices in those bread-and-butter communities. We have nine offices in our South-Central Los Angeles region serving all communities, including South-Central. These are not savings branches. They are freestanding lending offices.

Third, those offices are staffed by commission loan personnel. These mortgage loan consultants have every incentive to scour the territory where they work each day for credit worthy loans. If they do not, they do not make a living.

Fourth, it is not our loan consultants alone who work out of these offices. They are part of an on-site team that handles appraisals, underwriting, processing, and all the elements of a loan decision from start to finish on a decentralized basis.

We call these full funding offices, but perhaps we should call them equal opportunity offices because by their very nature, they help eliminate the stereotypes that discourage lending in such communities.

The loan consultant has an incentive not to discriminate his or her pocketbook. The office manager has an incentive to hire agents who can effectively produce credit worthy loan volume in their local community. So for example if the market gradually becomes Spanish speaking, it will almost inevitably follow that our managers will look to hire bilingual loan personnel. Half of our top 10 loan personnel are bilingual nowadays.

Finally, the back office team that underwrites and processes the loan is not sitting 50 miles away in a centralized decisionmaking center with no feel for the nuances of a neighborhood or an individual property. They work and often live in the very community where we are lending.

Self interest is a powerful motivator, Mr. Chairman. Our loan system illustrates how effectively it can work.

We believe there are three other important factors in our success. First, we are a portfolio lender. We sell many of the loans we originate in the secondary market. We have an appetite for loans we will hold in our own portfolio. Over the years, that has given us added flexibility in understanding the circumstances of the individual borrower.

Second, we are primarily an adjustable rate mortgage lender. For the better part of the last decade, the ARM has allowed us to offer better opportunities for affordable home ownership with payment protection to borrowers in every community we serve.

Finally, we are a color blind lender. In 1968, Great Western developed an explicit written policy against denying loans based on geographical considerations, a decade before the Community Reinvestment Act outlawed such practices.

We are proud of our insistence that our people make their lending decisions based on the value of the property and the borrower's ability and willingness to repay.

Mr. Chairman, there are many other elements of Great Western's performance under the Community Reinvestment Act that are important. We know we cannot meet all the needs of our communities through our lending activity and therefore we have been a pioneer supporter of a wide range of low-income and affordable housing programs through our community development activities.

We would be happy to provide you with any additional information on these efforts as well as the full extent of our success in lending in low- and moderate-income and minority communities if you would wish.

The heart of our success is our lending program. And the secret to that record is not special programs; it is not looking at certain neighborhoods as though they need special treatment by lenders. In fact, the deterrence to move active investment in all neighborhoods will not be overcome until they are seen as Great Western sees them: Neighborhoods in which we can make good money by doing what for us is business as usual.

We have built this record because we felt it would be prudent and profitable and, therefore, in the interest of our shareholders to do business this way. Perhaps this is testimony to the kinds of incentive that would be most powerful and most effective in improving the Community Reinvestment Act.

The carrot of profitmaking or profit enhancement incentives should be a far more powerful inducement for lenders to do the right thing than realms of paperwork or the threat of punitive action.

Finally, in closing, Mr. Chairman, I want to make an admission on behalf of the people who run our lending group. We feel as though we are playing with a double-edged sword today. The more our competitors adopt the Great Western formula the more competition we will face. You can't entirely blame us for wanting to have the field to ourselves.

But, in the long run, if our message is heard by you, it is heard by the regulatory community and by other lenders, the results can only be good for communities like South-Central Los Angeles. That is why we are here today.

I would also like to introduce my colleague, Ian Campbell, who is the senior vice president for Corporate Communications. Mr. Campbell will assist me in any questions that you might have that are beyond my direct involvement.

Thank you.

Senator CRANSTON. Thank you.

I want to compliment you and through you the Great Western Bank for an outstanding record. You have been conscientious and ethical and have shown that that can be profitable and I wish that there were more banks that have a similar record.

Thank you a great, great deal for what you represent here today.

Senator Neal.

STATEMENT OF JOSEPH NEAL, JR., NEVADA STATE SENATOR

Senator NEAL. Thank you, Mr. Chairman and Senator Bryan.

I am Joe Neal, State Senator from Nevada, representing today the Las Vegas Alliance For Fair Banking.

In the course of last year, Las Vegas has become a scene of ferment around banking issues. Two community based coalitions have been formed, the Alliance, which I represent, and the Southern Nevada Affordable Housing Committee.

For the first time, our financial institutions are encountering organized, consistent, and well founded challenges to business as usual. As they are also finding new partners for commitment to affordable housing, fair lending, low checking accounts, and other programs that make credit and banking services available to all members of our community.

The Community Reinvestment Act has played a pivotal role in this ongoing transformation of the Las Vegas banking arena. And we are strongly opposed to any measures that would weaken the act or limit its scope.

Let me give you an example of what CRA means to us.

You will find these in greater detail in the Alliance's report, entitled "Cashing Out," which I have submitted for the record.

When the Alliance examined the 1990 home mortgage data for Las Vegas, we found patterns that have now become familiar in one city after another throughout the Nation.

Virtually no home loans to African-American neighborhoods of West Las Vegas.

Very few home loans to largely black and Hispanic neighborhoods of the central city.

Thousands of loans to upper-income neighborhoods and hundreds to low- and moderate-income neighborhoods.

Denial rates for upper-income African-Americans and Hispanic applicants that matched the denial rates for low- and moderate-income white applicants.

In short, we found that banks in Las Vegas had cordoned off our minority and working class communities and imposed a financial curfew on them. What we saw the sheriff and police doing in the streets of our city last April and May, in the aftermath of the Rodney King verdict, the bankers have been doing for years behind closed doors.

We decided to approach local financial institutions with our comments on their community reinvestment records at the earliest possible time, rather than wait to protest an application. We were guided in this decision by the 1989 Joint Statement of the Federal Financial Supervisory Agencies regarding the CRA, which encourages community organizations to follow this procedure.

We contacted First Interstate Bank of Nevada which was not involved in a merger or other application process——

Senator CRANSTON. Excuse me. May I interrupt for one moment? Unfortunately, there is another roll call.

Dick, if it's OK with you, I'll run over and get back as fast as possible. You keep going as long as you can. If you have to leave at some point during, I'll start again when I come back.

Senator BRYAN. I appreciate the confidence you have invested in me.

Senator CRANSTON. You and the Senator from Nevada are fully in charge now.

Senator BRYAN. Please, Joe.

Senator NEAL. First Interstate has played a key role in financing the gaming industry in Las Vegas and is one of the largest retail banks in Nevada. It also has lots of room to improve its community reinvestment record.

We presented our concerns to First Interstate, and our proposals for addressing them. After three inconclusive meetings, the bank is stonewalling us.

In such circumstances, community organizations are right to conclude that, despite the good intentions of the 1989 Joint Statement, nothing seems to concentrate the minds of bankers on their community responsibilities as effectively as a CRA protest.

Which brings us to a notion of safe harbor, that is, exempting banks from CRA challenges if they have received a high rating. From our experience, it wouldn't take long for banks to turn a safe harbor into a smuggler's cove.

New banks are coming into our community. Last year, Bank of America acquired Valley Bank. This year, U.S. Bancorp is acquiring former Bank of America and Security Pacific branches. Both these acquisitions were protested on CRA grounds by the Southern Nevada Affordable Housing Committee.

The community wanted CRA-related commitments as a condition of these big players coming in. And we got commitments. With safe harbor provisions, B of A and U.S. Bancorp might well have been immune to the protests that leveraged the commitments, because in their home States they have "outstanding" CRA ratings.

Or take First Interstate Bancorp. Back in 1987, when FIB wanted to buy Allied Bancshares of Texas, the Federal Reserve approved. Community groups protested, but the Fed responded that FIB's subsidiaries all had "satisfactory" CRA ratings.

Nevertheless, something must have concerned the Fed because FIB was required, as a condition of approval, to make semiannual reports on its CRA progress. What happened? Within 3 years, four of FIB's subsidiaries had dropped from "satisfactory" to "needs to improve" ratings.

If banks can shortchange their CRA responsibilities while under constant Federal Reserve scrutiny, as this case seems to demonstrate, what reason is there to think that giving banks a safe harbor will benefit our communities?

In fact, we would like to see more disclosure, and more objective ways of evaluating it. In Las Vegas, we are working with our county commissioners and city council members to develop a program to take the community reinvestment record of banks into account when deciding where our public funds are deposited.

We are following the lead of cities like Boston, Pittsburgh, and Los Angeles in asking banks to provide information on small business lending, student loans, support for affordable housing, low-cost banking services, and other criteria.

These voluntary, local programs have demonstrated that effective mechanisms can be established for collecting and evaluating a broader range of data than is currently available for CRA purposes. And we would support the inclusion of similar, broader disclosure requirements in the CRA process.

Mr. Chairman, I thank you for the opportunity of allowing us to present this statement.

Senator BRYAN. We thank you very much for your testimony.

And next, in the absence of our Chairman, may we hear from Ms. White.

STATEMENT OF MICHELLE WHITE, EXECUTIVE DIRECTOR, FAIR HOUSING CONGRESS, SOUTHERN CALIFORNIA, LOS ANGELES, CA

Ms. WHITE I am former special assistant for civil rights for the Office of the Comptroller of the Currency, so I come to you with both regulatory and enforcement experience.

As the executive director of the Fair Housing Congress, we have engaged in enforcement activities related to banks and also did a study for the city of Los Angeles whereby we studied the practices of lending institutions within the city.

I just want to give you a short, brief background of Los Angeles's interlocking between race and income. There is an absolute interlocking there. And when you start talking about community reinvestment issues as if they are economic issues only, you miss a great deal of the point, because they are also issues that relate to race and also are very much tied into national origin. Both of these are covered, of course, by the statutory provisions of the Equal Credit Opportunity Act as well as the Fair Housing Act and as well as the constitutional provisions of the U.S. Constitution.

Therefore, we would very much argue that you cannot disassociate economics from race within Los Angeles and many of the large urban communities. This is what has been occurring within the regulatory agencies, however, by taking a look at things as if they are merely economic issues and not racial and national origin issues. They can write off practices as if they have less importance.

We strongly disagree with this approach and believe that another needs to be undertaken and very quickly.

We do not believe that there has been over the last 15 years a very serious effort on the part of the bank regulatory and the thrift regulatory agencies to deal with the issue of community reinvestment or fair housing or fair lending. That is because if you take a look at the financial regulatory agencies you will see they have allowed things such as minimum loan amounts of $250,000 and $350,000 within Los Angeles. This means that areas such as a large part of South-Central, and other areas of color do not qualify for those loans off the bat.

In addition, you will find that these same financial institutions do not locate branches within certain areas of the city. Part of the study was devoted to looking at exactly where branches are located.

What we found was, if you looked at the branching, you found that for every 10,000 persons in high income and Anglo areas, you had 2.9 branches per 10,000 persons. If you made the same comparisons in low-income and minority areas, you only found 1.3 comparable branches.

The effect is obvious. You bank where you live, you bank where you do your work. And the problem is that, of course, those persons who do not have access to adequate transportation and do not have branching in their area will not bank with traditional institutions.

As a result, what we have found is we have a large evidence of lending scams that are prevalent in low-income and minority areas. We also have hard money lenders that are very prevalent in these areas. And that is because the banks do not stand up and take their position in the areas and lend in those areas in the same degree that they will lend in high-income and Anglo areas.

We also found that if we compared the ratings that we did on banking institutions with those that were then available through the lending—the bank regulatory agencies, that we differed quite substantially with the ratings that were received. More often than not, our ratings based on the amount of lending that was going on in specific areas and also other public information which was made available to us, our ratings were much lower than those that were received by the regulatory agencies.

We also found that 7 percent of the lending institutions didn't even make assessments of what their credit needs were within the city of Los Angeles, which was their service area. This is a very basic requirement under CRA and something for which they were not held accountable by bank regulatory agencies.

The cities of San Diego and Oakland have found it necessary to go out and conduct their own assessment of credit needs because they found that those being conducted by the banks were inadequate.

We also found that inadequate information was being collected on business loans and it was impossible based upon the information that was being collected to determine whether there was any disparity based on race or other illegal bases. So therefore if that information is not being collected, there is no way for the bank regulatory agencies to truly assess whether discrimination is occurring.

Finally, the bank regulatory agencies and financial regulatory agencies—I don't want to leave out the thrifts—have found virtually no discrimination on the basis of applicant pools or redlining in the last 15 to 20 years. We believe this is incredible because we know of 20 cases that throughout the United States that have gone to trial or been settled where a finding has been made.

I would like to enter into the hearing testimony a documentary transcript of a recent work that was done by the Center for Investigative Reporting and aired on Frontline, and it is entitled "Your Loan is Denied." It depicts exactly what has occurred over the last 15 years with the financial regulatory agencies.

Senator BRYAN. Ms. White, that will be made part of the record. And we thank you for your testimony.

We are going to have to take a recess for at least 5 minutes because the roll call is running down and Senator Cranston will rejoin us in a moment.

[Recess.]

Senator CRANSTON. The hearing will please come back to order. I understand we made some progress during my absence. I am sorry I didn't hear all of your testimony, Senator Neal, and yours, Ms. White, but I will be aware of the record that you have made. Mr. Bodaken, would you now proceed?

STATEMENT OF MICHAEL BODAKEN, COMMUNITY REINVESTMENT COORDINATOR, OFFICE OF MAYOR TOM BRADLEY, LOS ANGELES, CA

Mr. BODAKEN. Good morning, Mr. Chairman. Thank you for the opportunity to address you this morning.

I am Michael Bodaken, Community Reinvestment Coordinator for Mayor Tom Bradley in Los Angeles. And today I take the key for my remarks from your own remarks that the CRA should be remeasured, that evaluations should take into account actual performance in the field as well as process inside the bank.

In fact, we are guided, Senator, by the actual language of the act which explicitly provides that an institution's record of meeting the credit needs of the entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of such institutions is the criteria by which they are supposed to be evaluated.

Nevertheless, regulators do not presently require that banks with inadequate lending performances actually receive a less than satisfactory rating. We know from our work that there are 12 factors that bank regulators and lending regulators use to evaluate banks. And a bank can receive a satisfactory ranking by simply determining that it is satisfactory on the 12 factors taken as a whole. Only three of those factors relate to actual lending performance.

Evaluation results that were conducted by your staff and by myself as well confirm this very dismal record.

In preparation for this testimony, I reviewed 2 years of statistics of the Federal Deposit Insurance Corporation and found, as did your staff for a much longer period, that 91 percent of the institutions surveyed had both outstanding or satisfactory responses. And, again, as you noted, this is in direct conflict with many of the stories that we've received about bank regulations, about banks not meeting the credit needs of the entire community.

It is therefore my urgent request that the committee and Congress consider reevaluating those evaluation criteria to not only include the marketing of credit but actually take into account the performance and show that banks are providing significant loans to low- and moderate-income communities, and that no bank receive a satisfactory record until it can demonstrate that such loans are in fact taking place.

My concern about the actual provision of credit to communities is, of course, highlighted by the recent Los Angeles Times articles that have focused on the lack of home mortgage loans in South Los Angeles by major banking institutions in Los Angeles. Those articles, as you know, pointed out that major banking institutions in Los Angeles are not making home mortgage loans. We know this to be a fact, over the past 2 years.

I won't go into the details, but suffice it to say that something is wrong. In response banks often tell us that banks not only make home mortgage loans but that they make small business loans, they make consumer loans, they have low-cost checking accounts, they have a whole portfolio of lending activities. And we agree.

It is precisely that which leads me to my second point. What evaluators need to do is start looking at an entire banking portfolio, not focusing only on home mortgage loans. Let's get the entire picture out on the table. Let's take a look at the small business loans, the consumer loans, the low-cost checking accounts, and really see and make that public. So that the banks can really be evaluated fairly.

So if they are making small business loans in South-Central Los Angeles they will get credit for it. If they are making consumer loans in South-Central Los Angeles, they will get credit for it. And if not, then they won't.

Right now, we have half a picture. And we think the whole picture should be told, should be given to us.

Precisely at this time in our Nation's history, when we are in the grips of a dismal recession, it would seem most appropriate for small business lending activity to be revealed. The need for this data is buttressed by a couple of examples I brought with me today, provided to me by the Community Development Department of the city of Los Angeles.

An owner of three community markets in Los Angeles needed to provide extra space for his customers and so he sought reconstruction financing for all three markets. Two were in middle-income areas and one was in a low-income area. All three financials were almost identical. In fact, the profit margin in the lower-income area was actually a little bit better than in the middle-income areas. Not surprisingly, the construction financing in the low-income area was much more difficult to obtain than in the middle-income areas. Similarly, a major manufacturer of shopping carts and shelving for supermarkets located in Watts, had been in business for 40 years in Watts. They had an excellent credit reputation. And two of their competitors had gone out of business. So they decided to expand.

They went to a major bank, the name of which I won't disclose. But it was a major bank, a major California institution, and asked for a loan to expand their facilities.

A mid-level bank executive came out to that particular location in Watts, took a look around, and denied it on the basis of some kind of nebulous risk.

These are loans that are never disclosed to the public. The only reason we know about these is because these people eventually came to the city of Los Angeles and disclosed their problems.

What the CRA needs to do is focus on that kind of activity as well as home loans, so we can get a broader picture of what's really happening.

I know there are some who would argue against the modifications that I am urging today. In fact, we understand from your staff that a safe harbor provision has been proposed by the administration and some in Congress. Indeed, some believe that that should give them a safe harbor provision, at a time of merger, of acquisition, or at a time of a branch closing.

I am particularly concerned about this viewpoint. Apart from the theoretical problem that over 90 percent of the banks would have such safe harbor provisions based on the statistics that have been gathered by your staff, there are practical concerns as well. Because it is precisely at the time of merger or acquisition that we get into the point of what reinvestment gains can really be made.

The most recent example is, of course, the Bank of America, Security Pacific merger in California and all over the Nation. In that particular example, Bank of America had an outstanding community reinvestment record when it started the process. And Security Pacific had a satisfactory rating.

Community groups, such as those you heard testify today, and State Senators such as Senator Neal, myself and others, said it was important that their reinvestment goals be enhanced. And as a result of our concerns that we laid out on the table during that 6-month process, the community reinvestment goal for Bank of America was increased from 33 percent from some $9 billion to some $12 billion. There is no way that would have happened without the Community Reinvestment Act. That would not have taken place.

Similarly, in the city of Los Angeles, we formed a community reinvestment committee, with community groups, with the banks, and with city officials. And we have been able to make some small milestones. We have been able to establish a community financial resource center, which is discussed in Councilman Thomas's testimony which I am also submitting for the record today. And a bank community development corporation.

The first, the resource center, is a one-stop shopping center for economic development and home loan counseling, staffed by banks in a city building. A bank community development corporation is another milestone. It provides gap financing for small businesses from $25,000 to $250,000. But it would not have occurred without the Community Reinvestment Act.

So today I come before you asking you to not only maintain the CRA but to enhance it, especially in these difficult times.

Thank you.

Senator CRANSTON. Thank you very much for your very constructive testimony.

Ms. Haas.

STATEMENT OF GILDA HAAS, COMMUNITY ORGANIZER, COMMUNITIES FOR ACCOUNTABLE REINVESTMENT, LOS ANGELES, CA

Ms. HAAS. Good morning. Thank you for allowing me the opportunity to present the views of Communities for Accountable Reinvestment. We call ourselves CAR.

We are a coalition of grassroots community organizations. Our representation is ethnically diverse. We represent African-American, Asian-American, Latino, and white constituencies across Los Angeles and Riverside County and San Bernadino County.

They are also diverse in the terms of the kind of work they do. Some are nonprofit housing developers, some represent tenant unions. Others work in the fair housing arena. Some of our organizations are based in churches and others in labor organizations.

And as a coalition, we come together at the intersection of civil rights and economic development. And in spite of our diversity we share one common agenda. We do not believe that we will have achieved our goal unless it is achieved for all of our communities.

CAR is opposed to weakening CRA in any form and we strongly believe that the law should in fact be strengthened and the purpose of my remarks today is to convince you of our position.

One proposal that has repeatedly surfaced to weaken CRA has been to exempt banks with satisfactory ratings from scrutiny of the law. We have already talked about that.

Our experience shows that even banks with outstanding CRA ratings have huge racial and class disparities in lending. Let's take Bank of America, for example. We have a lot of experience with Bank of America.

Our organization filed a challenge against the Bank of America Security Pacific merger based on what we felt was a need to improve community reinvestment experience. Today Bank of America, after the merger, is the second largest bank in the country. In 1990, Bank of America had a 6.6 percent share of the overall Los Angeles county home mortgage market. In communities in Los Angeles County that are overwhelmingly white, the market share jumps up to 11 percent. In minority communities, the market share drops to 2.7 percent. This is in a county where the population is 60 percent people of color.

This to us is not responsive banking. It certainly isn't outstanding. It is not outstanding performance, and it certainly is not one that should be exempt from accountability to the Community Reinvestment Act.

Now such unresponsiveness by banks to the needs which in Los Angeles is the greater community, has created a two-tier financial system in Los Angeles, one that is separated by race and class. For example, in South-Central Los Angeles, the majority of home loans are neither made by banks, that make about 3 percent of the loans, or thrifts, which make about 35 percent of the loans. Most of them are made by mortgage and finance companies that charge more, where people pay more for mortgages and loans, like they do for lots of other things.

There are about 18 bank branches in South-Central serving a 60-square-mile area where about 600,000 people live who more frequently use the more conveniently located 133 check cashing facilities in the community.

The real problem with CRA from our view has been its lack of effective and more importantly relevant enforcement. I have already mentioned the problem of grade inflation with respect to Community Reinvestment Act ratings. Another problem tends to be for banks and their regulators to marginalize community needs to the central purpose of their business objectives, relegating them to a side issue akin to corporate philanthropy.

But what could be more central to banking than community needs? Our experience shows that this strategy leads to marginal performance in low-income and minority communities. We did the same kind of research on several banks including Great Western, whose representative is sitting near me, and compared them to Bank of America. Now both these banks have outstanding CRA ratings.

In high-income communities in Los Angeles County, both of these banks hold an equal 9 percent share of the market. But in stark contrast to Bank of America, Great Western's market share increases to 24 percent in low- and moderate-income census tracks, while Bank of America's drops to 3.5 percent. And unlike Bank of America, Great Western's home loan market share is almost five times as large as its market share in white communities. In contrast, Bank of America has more than four times the share in white communities as those where people of color live.

What seems to be the main difference between the two banks is the level at which the needs of working class and minority communities are integrated into the strategic business objectives of the bank. Unlike Bank of America, Great Western sees our community as the large profitable markets that they are, that market products in our communities and sell them. And it shows in performance.

I think our regulators need to take a page from Great Western's book.

There's no comparison between that bank and the others. CRA has not been able to prove itself in objective performance measures, and that's why study after study shows that redlining is still persistent and pernicious. It is time to more seriously link the laws implementation to performance in terms of loan production and distribution and appropriate underwriting criteria, in the wake of Los Angeles' civil unrest today.

In Los Angeles today, more and more people understand the relationship between historic disinvestment by banks, and the under development of our inner-city communities

More people recognize the relationship between disinvestment by banks and the accelerated commiseration of people who live in those communities.

They can now see the relationship between the destabilizing forces of redlining and conditions of economic disenfranchisement which, in part, underlie civil unrest in the first place.

Our organization certainly sees these relationships, and we've been moved to escalate our scrutiny of banks in our communities.

To this end, we've developed a CRA performance examination. I've enclosed it with my written remarks. It looks like this. And actually it's very similar to what Mr. Bodaken was talking about, but we've developed a vehicle for doing it.

We have been issuing, to the 25 largest banks in Los Angeles, a simple form for them to fill out which identifies their performance in a range of categories that are important to us and our communities.

It's really important to our diverse constituencies that objective criteria are used to measure performance, and that performance is looked at, rather than plans, in order to fulfill the promise of eliminating redlining once and for all.

Thank you very much.

Senator CRANSTON. Thank you very much.

I appreciate the testimony of all of you.

Senator D'Amato of New York is still with us, the ranking Republican member of the Housing Subcommittee.

Al, do you have any opening remarks?

OPENING REMARKS OF SENATOR ALFONSE M. D'AMATO

Senator D'AMATO. Mr. Chairman, so that we can get to the panel, I'm going to simply ask that my statement be included in the record as read in its entirety.

Senator CRANSTON. It will, of course, appear in the record.

I also have statements from Senators Riegle, Sanford, and Sasser that shall be inserted in the record.

PREPARED STATEMENT OF SENATOR ALFONSE M. D'AMATO

Senator D'AMATO. Thank you, Mr. Chairman. At today's hearing, the subcommittee will be reviewing the status of the Community Reinvestment Act (CRA). The CRA was created in 1977 to discourage redlining and to emphasize the importance of increasing lending in certain low-income and minority neighborhoods that received less attention under normal banking practices. Under the CRA, banks must identify their market areas and describe how they are meeting the lending needs of those areas.

Since the CRA was established, banks, regulators, the Congress, and community groups have all become much more aware of the need for the CRA and the problems with implementing and enforcing the CRA. Furthermore, there has been a great deal of discussion regarding why capital does not flow as freely into certain areas as it does into others and what impact the CRA has had in increasing lending to underserved areas.

As CRA enforcement has evolved, both financial institutions and community groups have raised questions regarding how to make enforcement more effective. While most parties agree on the goal of increasing safe investment in low-income and minority areas, financial institutions want to reduce regulatory burden, and community groups want regulatory examinations to more accurately reflect banks' practices and encourage more "community reinvestment."

I look forward to discussing these issues during today's hearing so we can develop a better understanding of the CRA and lending practices. Maybe then we can determine how to increase the availability of capital to areas and individuals that need it and want it.

Thank you, Mr. Chairman.

PREPARED STATEMENT OF SENATOR DONALD W. RIEGLE, JR.

Senator RIEGLE. I am very pleased that you have called this hearing on the Community Reinvestment Act (CRA). CRA is a critical piece of legislation for maintaining and restoring the health of our cities. Only since CRA was enacted in 1977 and Congress declared that financial institutions have an affirmative and continuing obligation to meet the credit needs of the communities in which they are chartered, have banks more actively sought to extend credit to low-income, elderly and minority borrowers. Prior to CRA, these community needs went largely unmet. Although originally intended as an anti-redlining tool—CRA has also proven to be an effective mechanism in promoting investment in low-income housing, community revitalization, and small business development.

Unfortunately, a significant body of evidence suggests that CRA has not been properly enforced. Last year, the Federal Reserve released a study based on data from the Home Mortgage Disclosure Act. The findings of the report were alarming—blacks with comparable incomes were twice as likely as whites to be rejected for home mortgage loans. Yet, despite this fact, over 87 percent of all financial institutions received ratings of satisfactory or better. This indicates that the bank regulatory agencies are not properly enforcing CRA.

Another disturbing trend that has emerged is that many banks may be siphoning deposits from minority neighborhoods—leaving residents of these neighborhoods unable to access credit from the very institutions where they place their savings. A recent study of banks in 14 cities found that for every dollar on deposit in predominantly minority neighborhoods, about 4 cents was loaned for mortgages in those same neighborhoods. Yet, for every dollar on deposit in predominantly white neighborhoods, nearly 8 cents are reinvested in those same neighborhoods. I look forward to hearing the testimony of our witnesses on these trends and how the Federal Government can—through regulation and legislation—address these problems which threaten to accelerate the decay of our cities.

I would also like to recognize the work of the Shorebank Corporation which is represented by James Fletcher on our second panel. The Shorebank Corporation has been an innovator in developing new approaches to bringing credit to capital starved communities. Shorebank has also been instrumental in assisting the committee in putting together the Community Investment Corporation Demonstration program that I included in the housing reauthorization bill. This demonstration program is designed to plant the seeds of a national network of community development banks based on the South Shore Bank model. The program would provide grants and technical assistance to start or expand these innovative organizations.

Although the Shorebank Corporation lends and invests in neighborhoods that most banks shy away from, its lenders do not lose money and even make money. Community Development Banks are prudently managed as indicated by its returns on earnings or assets; their loan losses are low and consistently outperform those of other financial institutions; and delinquency rates at these banks are within—or better than—industry norms. It is this success story that the Community Investment Corporation Demonstration is designed to replicate and form the basis of a new urban strategy for reinvestment in our neighborhoods and communities.

PREPARED STATEMENT OF SENATOR TERRY SANFORD

Senator SANFORD. Thank you, Mr. Chairman.

I would like to commend you for holding this important hearing this morning. Issues surrounding the Community Reinvestment Act (CRA) are critical to the economic well-being of all segments of a community. It is important that we constructively use this forum to discuss the original intent of CRA, the results, or lack thereof, this law has produced, and finally, we must work toward designing a feasible implementation of this law.

CRA was designed in 1977 to combat redlining practices by the banks and ensure adequate access to capital for all segments of a community. Geographical discrimination in lending practices inevitably have an adverse affect on low-income communities. The tragic riots America witnessed in Los Angeles last spring provide a case study to help us to better understand the extent of the dangerous deterioration occurring in our inner-cities. The events in Los Angeles serve as a wakeup call illustrating the need for immediate and serious revitalization of our urban areas. This call cannot afford to go unanswered.

There is evidence that indicates that CRA has not been working as originally intended. The release of the Home Mortgage Disclosure Act data last fall showed that blacks with comparable incomes were twice as likely as whites to be rejected for home mortgage loans. Furthermore, that study points out that in 1990, the denial rate for conventional home purchase loans was approximately 14% for white applicants, while the denial rates for black and Hispanic applicants were 34% and 21% respectively. I believe that there is a linkage between home ownership and strong communities. It is imperative that we do all that we can to eliminate all forms of discrimination no matter how subtle or unintended, in an effort to make the entire home buying, home financing process fairer, less intimidating, and accessible to all creditworthy Americans.

In addition, I have great concerns about the actual implementation of this law, and its long-term effect on our financial system. Originally, CRA was designed to ensure that financial institutions ascertained the credit needs of the entire community and provided appropriate banking products to the various population segments. Somewhere along the line, the enforcement of this law has been flawed, and I fear that the objective has been lost. The regulators seem to stress process over substance which results in excessive documentation. Small banks are unable to shoulder this kind of paperwork burden. I think it is important that we recognize the diversity of our banks and promote consistency and flexibility when implementing this law. This also calls into question the competitiveness factor in the banking industry. I have advocated for sometime the importance of reforming our financial system to create a level playing field. CRA is a good example of the many inconsistencies that exist in the present system. Other financial intermediaries who offer bank-like products are not held to the same standard of community responsibility as are banks. If we wish to increase the flow of capital and mortgage credit into low-and moderate-income communities, we must make sure that all the players are using the same rules.

Disinvestment in a community causes a spiraling deterioration. It is vital that financial institutions take the lead in helping to rebuild our decaying communities. Banks cannot restore our communities alone, but they can go a long way toward facilitating increased mortgage credit availability and small business capital. CRA helps to bring the interested parties to the table, but we must work on this law to see that it is implemented in such a way that it provides incentives to offer adequate financial services to low- and moderate-income neighborhoods, and does not hinder the safety and soundness of our financial institutions.

Again, I thank the Chairman for calling this important hearing and I look forward to hearing from our witnesses.

PREPARED STATEMENT OF SENATOR JIM SASSER

Senator SASSER. Mr. Chairman, I would like to thank you for organizing this valuable review of the Community Reinvestment Act.

The review is justified not only by the events in Los Angeles this past summer, but also by an increasing volume of complaints about the workings of the act.

Mr. Chairman, I have supported CRA throughout my career in the Senate. We cannot tolerate redlining. The banking system enjoys the financial backing from the Government; the public expects that in return for its guarantee of stability that a public purpose be served. Evidence abounds that despite CRA's passage, lending patterns still reflect discrimination against certain communities and certain ethnic groups.

CRA has an ancillary benefit of serving as an excellent tool for community based nonprofits. CRA affords nonprofits an entree to their local lenders. I think we have seen many new and creative partnerships arise around the country as a result.

Having said this, Mr. Chairman, I believe that the banks' complaints about excessive paperwork and uneven application of the law are not without merit. I sense, however, that the blame for these complaints lies not in the CRA statute, but in the application of the law by the regulators.

The regulators seem more interested in the process of CRA enforcement than in the outcomes that the law strives to promote. The complaints that I heard about the act do not necessarily argue for "safe harbors" or "small bank exemptions," but meaningful regulatory relief that substitutes a renewed commitment to the intent of the act in exchange for reducing its bureaucratic burdens. Mr. Chairman, I believe that the regulators should undertake a systematic review of their practices with this trade-off in mind.

So, in closing, Mr. Chairman, thank you again for calling these hearings today. I look forward to hearing the testimony of the witnesses.

Senator CRANSTON. You've raised a number of important points this morning and I thank each of you for your excellent testimony.

There are several issues I'd like to go into in a bit more depth.

We hear repeatedly, and much of your testimony this morning confirms, that the inner cities are starved for capital and certain segments of the city have been abandoned by the regulated financial institutions.

Los Angeles and Las Vegas are prime examples of cities with disinvested communities.

So, first, what is your assessment of the credit needs of Los Angeles beyond South-Central? Are there other areas that have also been disinvested?

Ms. WHITE. Yes. Virtually every area that's low-income. We have enterprise zones in Los Angeles. Those have been disinvested. Minority areas.

The study that I referred to, "Taking It To The Bank," pretty much outlines that the number of loans, the amount of dollars going into minority and low-income areas is dramatically less than Anglo and high-income areas.

Senator CRANSTON. Senator Neal, is the west side of Las Vegas the only problem area, or are there others in Las Vegas?

Senator NEAL. No, Senators, it's not the only problem area but it's endemic of the problem that we have in our community.

To give you an example, we have one major bank there, the FIB, that has two branches on the east and west side of a predominantly black community, and we were able to review the assets or get a picture of the assets of that financial institution for 1990, and it had $94 million.

And we were able to estimate that about $64 million of those dollars came from the black community, itself, but during that same year, they only loaned $59,000 back into the community.

Also, we found that as the black population and the Hispanic population move into other areas where that population began to increase, we see a decrease in the lending of those institutions to that particular group.

So the money seems to follow a racial pattern within our community.

Senator CRANSTON. Thank you very much.

Beyond what you've already said in your testimony, do you have anything add about what should be the role of CRA in helping to alleviate the problem? And what more can banks do and should they do beyond what the Western Bank is doing? Do you have any comments on that?

Senator NEAL. Yes, I can start off, Senator Cranston, by answering the question.

One of the things that we can do, we can add to the CRA disclosure the number of applicants that actually file for loans. One of the things that we found, in dealing with the banks in our area, that once we confront them with the information, the data that we collected under the 1990 CRA disclosure, they came back to us and said, this does not reflect the number of applicants.

So we need to have them give us that type of information. And I think that the communities can use that.

The other thing that we are attempting to do in our community, through local government, is to ask for further disclosure in the area of consumer loans, other than affordable housing loans, and look at all other credit products that those banks delivered to other communities, and make sure that those same products are available to low and moderate and minority communities.

Senator CRANSTON. Are there other responses to that question? Ms. Haas?

Ms. HAAS. First of all, there's three basic things that communities need before you can even talk about community reinvestment.

They need to have physical access to banks. If there's no banks in your community—because I work with a community that doesn't have any banks for a 3 mile radius. We're starting a community development credit union —the question is moot. People aren't going to go to a bank that is miles and miles away.

The second thing is that we need to have underwriting criteria that realistically assess what does it mean to be credit worthy in a low-income community. And that means that if you have incentives for your home mortgage, people selling your home mortgages to make bigger loans, then that's going to knock a whole lot of working class people out of the box right there. The same thing goes for business loans.

The other thing is that we found during the Security Pacific and Bank of America merger, we looked at their record in branch closures and where the branches were closed. And we found that 71 percent of Security Pacific's branch closures and 67 percent of Bank of America's closures over a 10-year period, prior to the application, were in low- and moderate-income communities.

These are things that regulators should look at. We need to have a commercial disclosure law, so we can have information on these loans.

Everybody in South-Central Los Angeles knows, for example, that some of our major commercial lenders do not make any loans in that community.

People in Pico Union, people in East Los Angeles, they know that those banks don't make loans in our communities. And we can't prove it. We've done surveys, we've interviewed businesses, et cetera, but we need to be able to hold commercial lenders up to the same standards that we do for mortgages.

And finally, as long as people have allowed there to be a two-tiered financial system in our cities, where white middle class people use banks, and low-income and working class people and minority people use check cashing facilities, we need to regulate those too.

There was just an example last year in Los Angeles where two money order companies, two very large money order companies went bankrupt. So we have a situation where people who have $100,000 certificates of deposits are ensured, and people who bought money orders from those companies who are paying their rent and paying their bills, their money orders bounced, and there was no protection for those people. And they need the protection the most.

Thank you.

Ms. WHITE. With respect to underwriting criteria, most of the underwriting criterion is set in such a way that it's designed to respond to the credit needs of middle income persons.

Most of the people that we deal with spend 50 to 70 percent routinely of their income on housing costs. And to then limit the housing amount that they can spend to 28 or 32 percent of their income is not reflective of the credit needs of low-income persons.

Underwriters must be much more flexible with respect to who they're dealing with and what kind of credit history they have, and if they have in fact paid their bills and they are spending more than 28 percent of their income on housing, then that needs to be taken into account.

The branch closures that Gilda Haas was talking about are very critical in all of this. And branch closures are done on the basis of notice to regulators. There was a time when they had to get approval and it was subject to CRA protests. That's no longer the case.

Those need to be taken into account because not only are there economic impacts with regard to this, there are racial and national origin ramifications because of the placement or the displacement of those branch locations.

One of the other things that we found, which is very alarming, is that at least one of the very large scam artists who was recently subject to litigation, was financed by one of our very large banks.

There has to be more taken into account and more disclosure, as well as more investigation made with respect to who banks are lending to.

Also, we are finding, especially in light of the uprising, that there's a great deal of need for cashing of Government checks that is not always the case. It was clearly not the case prior to April and May.

Some of the banks are now doing it, but we clearly need to have banks allow Government checks to be cashed on a routine basis. This should be something that's done all the time.

We also find a great deal of difficulty with the photo ID's, and the fact that banks are requiring that persons have credit cards and driver's license before they can cash checks.

We are dealing with low- and moderate-income individuals who routinely use public transportation. They don't have driver's license and some do not have credit cards. And to require this as a requirement to open an account is clearly a disincentive.

Finally, with respect to multifamily lending, this is an area—Los Angeles is largely an area of renters, and we need access to multifamily home loans. We are finding difficulty with respect to lenders who will extend permanent mortgage loans, and not just construction loans, on multifamily loans. This is especially true in low- and moderate-income areas.

And we are also finding that with respect to those loans that are going to service those pre-paid expiring subsidies for HUD financed properties, we're having difficulty getting those financed because many financial institutions do not want to accept the 5-year section 8 project based securities as security for those loans.

I'm just giving you a list of various things that we think are necessary in order to meet the credit needs of Los Angeles.

Senator CRANSTON. Thank you.

Al, do you have any questions?

Senator D'AMATO. Yes, Mr. Chairman.

Just to Sharon Butler. You stated that Great Western's success was the result of fundamental business strategies that were in place before the CRA came into existence.

Could you share with us, what strategies in particular you believe could help make a difference?

Ms. BUTLER. Senator, further in the testimony, we talk about what we feel makes a good loan. We talk about the fact that we think a smaller balance loan made to a person who's going to live on the property is a safe and sound loan to make.

We find large numbers of those loans in low-, moderate-income, and minority communities.

So pursuing that business strategy gives us significant market share where those factors are present.

Senator D'AMATO. Why is it that Great Western has undertaken this, and that others in the financial community have not?

Ms. BUTLER. I couldn't answer with any degree of certainty why they have not. It's really a part of our history.

Our founders, many many many years ago, were interested in making loans to people who were getting their first home, smaller balance loans. That in fact has gone on under different leadership throughout the company, and it's been very successful for us.

Senator D'AMATO. Regardless of the community that the person may be living in or whether the applicant is a minority applicant, this has been a standard that you're saying Great Western has followed?

Ms. BUTLER. That's correct.

Senator D'AMATO. And it has really put on what we call the blinders as it relates to any factors other than the soundness of the loan.

Ms. BUTLER. That's correct.

Senator D'AMATO. OK. This is tough. Can the same thing be done by others? And are they shirking their responsibility, those in the financial community?

Ms. BUTLER. We have some evidence. I read a recent story in the Los Angeles Times that others are beginning to take notice of that, and are in fact beginning to have some market share in areas in South-Central Los Angeles. So it would suggest that others, using their own strategies could also make a difference as well.

Senator D'AMATO. So you're saying others could make a difference and that——

Ms. BUTLER. And some are.

Senator D'AMATO. Do you believe that there's substantial room for improvement in this area?

Ms. BUTLER. Well, Senator, I, I——

Senator D'AMATO. I know it's tough to ask you, but, you know, that's why we're holding this hearing.

Ms. BUTLER. It is a tough point here. We'd like to have all the loans that we can get in all of the communities that we're involved. We think we see different lenders who are making some pretty decent strides in trying to gain some market share, and that is being done.

Some are creeping up slowly. Some are moving a little bit more quickly. So I think it's fair to say that, yes, things are happening and more things can happen.

Senator D'AMATO. So you would view it as progress being made even by those financial institutions that have not met the same kind of standards that you have met?

Ms. BUTLER. I think they're going to think it's progress too, very soon.

Senator D'AMATO. Mr. Bodaken, in your statement, you said that after the Home Mortgage Disclosure Act made findings that place the Bank of America in a rather unfavorable light, that you saw a change in their perspective, and that they changed their practices as related to lending practices to both the minority community and to the various low-income areas. Is that correct?

Mr. BODAKEN. Not precisely, but it's generally correct.

Senator D'AMATO. Well, then you tell me.

Mr. BODAKEN. Basically, I was taking that from a Los Angeles Times article of September 8, I believe, which I attached to my testimony, which indicated that in South Los Angeles, Bank of America had begun to make more loans, more home mortgage loans in South Los Angeles this year, as a result of disturbing data concerning their HMDA disclosure.

So generally I agree with what Ms. Butler just mentioned regarding Bank of America's performance. Is still probably too early to tell whether other banks are following that lead.

Another major financial institution, for example, has only made five loans in South-Central Los Angeles, although they've received an outstanding rating on community reinvestment.

And so I think it's a mixed bag out there. It's too early to tell, in my mind, whether other financial institutions are going to perform as has Great Western in this area.

And I think that further points out the need to look at all of the banks' lending activity, including their small business and consumer loans, so maybe they're doing well in other areas. We just don't know.

Senator D'AMATO. Some have said that the CRA enforcement could be improved by using a more objective measure of the CRA performance.

What would you suggest in relationship to that?

Mr. BODAKEN. In particular, I think we really need to look at the loans that are being made on the street.

You go back down and you say—you basically look like, as you do with home mortgage loans, you take a look at all the lending activity, and you look at performance. You look at it just the way any other business looks at its own activity. What kind of performance have we been making in these areas, what market share do we have in these particular areas, what kinds of loans are we getting back.

I think that what you'll find is that certain strategies are both not only common but also profitable, and that banks will profit in good community reinvestment as a main line activity, when it's not pushed off to the side and not marginalized, can actually help both banks and communities.

Senator D'AMATO. It would seem to me that public information, in other words, the reports that are made available, are beneficial and certainly are a kind of bully pulpit that can be used to encourage major financial institutions to reexamine their lack of participation in these areas. Would you agree with that?

Mr. BODAKEN. Absolutely. That's the reason disclosure's so critical.

Senator D'AMATO. Ms. Butler?

Ms. BUTLER. I would agree with that, as well.

The data that allowed people to look at our loans has been available for some time through the Home Mortgage Disclosure Act. And it's with increased interest from the press that the general community gets this kind of visibility.

Probably one of the single most factors that has made a difference in this whole area has been the Atlanta Journal's article, I believe it was 1989. So between the involvement of the current information that we have, as well as the visibility that it gets from the media, I think the community, as a whole, gets more involved.

Senator D'AMATO. Thank you.

Thank you, Mr. Chairman.

Senator CRANSTON. Thank you very much.

Dick?

Senator BRYAN. Thank you very much, Mr. Chairman.

Ms. Butler, you made a comment in your testimony with respect to the number of loans that you originate and retain in your portfolio, as opposed to selling in the secondary market.

I want to make sure that I understood the thrust of what you were saying.

Are you suggesting that there is a pattern that those institutions which retain a larger percentage of their loans, as opposed to selling them in the secondary market, tend to have better records with respect to making loans in the minority community?

Ms. BUTLER. I haven't had the ability to examine the records of other portfolio lenders. Great Western, as a portfolio lender, does have greater flexibility, because it does have the ability to hold some loans. And primarily, we are originating loans for our portfolio.

However, just to go further with this, we do originate loans that we sell on the secondary market, and we haven't detected any reluctance on the secondary market to purchase those loans.

Senator BRYAN. Perhaps others might comment.

Is there a correlation between those institutions which retain a larger portion of their loans originated in a minority or economically disadvantaged community, versus those that market more aggressively into the secondary market? Is there any trend line at all there that's significant?

Ms. WHITE. I don't know whether I can comment on that question, per se, but recent HMDA statistics reveal that with respect to those secondary lenders that buy up, say, 80 percent of the mortgage loans—it's either 80 or 90 percent of the mortgage loans—only 3 percent purchase from minority—only 3 percent of their portfolios are from minority areas, and about 9 percent are from low-income areas.

So I would say that even though, say, Fannie Mae's guidelines look like they are responsive to the needs of low- and moderate-income areas, the practices are such that in fact they do not purchase from those areas.

Senator BRYAN. Another point that Ms. Butler made—and Mr. Bodaken, I didn't mean to interrupt you if you wanted to make a comment. Another observation Ms. Butler made with respect to Great Western is the decentralized lending authority.

And I thought you made a pretty compelling argument in terms of your own policy to have the people that are making those decisions not only located in the branches, but living in the community itself, so that they had more than just a business interest, that they had a personal commitment in the community, itself.

Another question addressed to you, generally, in terms of the broad picture here. Is there a correlation in your judgment? Those of you who have maybe just a little broader view than perhaps those of us on the committee who know of a particular situation, which I want to inquire from Senator Joe Neal about in a minute, is this helpful in terms of increasing lending in the community?

Ms. HAAS. Communities for Accountable Reinvestment has had discussions with banks about this. The tendency is just the opposite.

As banks are consolidating and merging, they're centralizing to cut costs, and the banking profession has changed in that way.

So, for example, a whole lot of what bankers used to pride themselves on was their ability to read people, to make, I think they call it character judgments, that does not happen on boiler plate applications that all get sent to a location. And when your branch manager, who has known you for 20 years, has no influence in the making of the loans.

We've been lobbying extensively for even banks that refuse to experiment with decentralizing their loan making and having more local people making the loans, to at least do trainings, community based trainings for their loan officers and for their managers. It makes an enormous difference.

And I know, personally, from my own home loan, that it made an enormous difference to be talking to the person that was going to be—it happened to be from a black owned bank—to be talking to the person who was going to loan to me.

Senator BRYAN. And that is a comment that I think we hear not only from the minority community, but——

Ms. HAAS. Everybody.

Senator BRYAN.—the business community generally, and particularly with these consolidations that are occurring. In a small State, such as my own, where in effect the decision making authority may now not only be out of the community, out of the city, it may very well be out of the State. So there's considerable alarm that——

Ms. HAAS. Yes. It has a huge impact on small business lending, a huge impact on it.

Ms. WHITE. And as more banks and other financial institutions go to credit scoring systems for mortgage loans, as well as their credit cards, this becomes even more alarming, because as long as it's statistically reliable, no matter what the racial impact might be or the low-income impact might be, this is a scoring system that will routinely be approved by the regulators. It's very frightening.

Senator BRYAN. Senator Neal, I know that there has been some progress that you and other local community leaders have made possible with respect to increased access in banking in terms of a branch location in the low-income community.

Could you give us an update on that, and tell us how those negotiations went in dealing with the banking industry in our own State.

Senator NEAL. Yes, Senator. There are a couple of national banks who wish to locate branches within the predominantly west side community, which is predominantly black. And we're in the process of negotiating that particular move right now.

What we do not want is a branch that comes in and just sit down on the bucket, you know, and take it home at the end of the day, you know, and not give anything back to the community.

So we want to make sure that we have certain restraints governing the placement of those branches within the community, so we have sought the participation of the county and local government in identifying the services that these banks can offer to the community, based upon the fact that if they turn out to demonstrate a good record in their service to low-income community, that will become an incentive for placement of public monies within those particular institutions.

And so we are looking at it from that particular standpoint as a leverage in trying to get them to service the needs of all the community.

We are not asking these financial institutions to come into our community and just give out loans without restraints or anything like that. The only thing that we've asked them to do is to be as fair to the black community and the Hispanic communities as they have been to, say, the upper-income white communities.

Senator BRYAN. Senator, in your testimony, you mentioned the consolidation of banking in our State, and you made the comment that as a result of the Community Reinvestment Act, that you were able to secure, in your words, some additional commitments from these institutions.

Are you at liberty to share with us what those are and how you think that they might be helpful?

Senator NEAL. Well, the commitments that we had reference to was commitments in terms of affordable housing. And this was based on the fact that we had some institutions that wanted to merge with other banks in our particular State. And so we required them to give to us, in writing, commitments that what they could do in terms of service to the community in terms of affordable housing, and other type of products that they would be bringing to the community, to make sure that those products are made available to the minority community.

And such as lending, putting of the branches within the area, and also having checking, low-interest loans, to develop, and there was a whole list—I can't site them all—but there was a whole list of things that we considered.

And of course, I might add that we were dealing with an institution that came from the West Coast that already had a substantial record of doing good things in the financial world, and that was the U.S. Bank Corps that came out of Oregon. And they wished to merge with a couple of branches, branch banks within our State.

They came in and met with the minority community, the business community and asked essentially what they could do in terms of being able to be a good corporate citizen coming to our community. We just merely suggested things that they could do.

Senator BRYAN. With the Chair's indulgence, if I might, Mr. Chairman, just one or two quick questions.

I was particularly struck by Ms. White's example that what may, on the face, appear to be a reasonable underwriting criteria, namely, the amount of income that's spent for housing, may, in practical application in the minority community, render it virtually impossible to make loans following those underwriting guidelines.

Were any of your discussions with the banks that you've dealt with—and I'm aware that you're dealing with two different groups—did you get into the underwriting criteria and asking them to re-examine, not in terms of the quality of loan, but, I mean, in terms of the criteria which may, with a low-income family, indicate that they will pay a disproportionate amount of their income for housing, as opposed to those whose income levels are much higher and the percentages are within the underwriting criteria that she alluded to, the 28 to 32 percent, or whatever it happens to be.

Senator NEAL. We did, Senator. And one particular branch of the bank in our State called us in to discuss this very thing. And that they decided that they would go ahead and reevaluate, you know, their lending practices in this particular area.

But on the other hand, when we dealt with what we call the giant of our area, the FIB, which is in our State, which is that national institution, we were not able to get anything from them in this regard. They just merely said that, you know, just warded us off. Even though we had three meetings with them, it was just like we did not attend, you know. They would never acknowledge anything that we suggested to them, and didn't even acknowledge our presence, even in meeting with them.

Senator BRYAN. And the last question, Senator, and I appreciate the Chair allowing me to go over my time a bit, we've heard a blizzard of statistics and data that document the case.

Tell us, you've represented that community for 20 years, what does that mean in human terms? I mean, try to translate all this, if you can, in terms of how it affects people, and particularly people in the community that you've represented.

Senator NEAL. Well, if you do not have a financial institution to turn money back or loan money back into the community, it virtually kills a community. Because you cannot develop business, you cannot improve homes.

As in one particular case I made reference to, the West Side community, that is an older community. The houses there are about 40 years old and in need of finance for rebuilding and remodeling and things like that. So when you cannot get money to do that, then you have virtually a rundown community.

So in human terms, it becomes very effective in destroying a community when a financial institution does not make loans to the community for improvements.

As you might have heard, I mentioned about the two branch banks that were situated on the east and the west side of our community which had the total of $94 million in assets in 1990, and they only loaned $59,000 to a predominantly black community.

That just tells you what they have really done to that community. And you have blacks actually putting money into those particular branches, and did not get anything back in terms of loans to improve, to do business, to have other things that were necessary to keep a community viable. So, as a result, the community becomes run down, and then we pay the cost in terms of getting Federal loans to try to go into redevelopment and other things in trying to correct that. And when the corporate happens to be the financial institution in this regard.

Senator BRYAN. Mr. Chairman, I thank you very much for your indulgence.

And I obviously thank my friend and the other members of the panel for their testimony.

Senator CRANSTON. Thank you, Dick.

I just have one last question, and I'd appreciate very brief responses, so we can get to the next panel.

An essential part of any community's credit needs is affordable housing finance. Multifamily housing, particularly in Los Angeles, where housing is so very costly, is a key element of the strategy. Many of the banks which received outstanding ratings, however, have little or no multifamily housing or investment presently. What's the reason for this, and how can we remedy the situation?

Ms. WHITE. To the extent that we found banks that are willing to do multifamily housing lending, they are willing to do construction lending but not permanent financing.

They cite the regulators as the reason for not wanting to get into permanent financing. The reasoning that they've set forth is that they will become criticized by the regulators for making such long-term investments.

I don't know, there does not seem to be any kind of rational basis for failing to engage in multifamily lending of the type that we have in mind, because more often than not, the type of lending that banks become involved in is the stop gap financing. Typically, it's much less than 80 percent of the loan to value ratio. It's more around 40 or 50 percent, so they're certainly covered.

And before them on the loans are usually governmental agencies, so that the likelihood of a loan of this type going into foreclosure is almost nil.

I don't know the reason.

Senator CRANSTON. Do you have anything to add?

Ms. BUTLER. Just a little, Senator Cranston.

Great Western, as you know, is principally a single family lender, but we have long understood the need for multifamily lending, particularly for housing that was in the low- and very low-income areas.

To that end, Great Western, in 1977, was one of the founders for the Savings Association Mortgage Company. Savings Association Mortgage Company does provide financing for multifamily housing.

And in connection with other lenders, there is construction financing and multifamily financing to keep that pipeline moving.

Local governments use that quite regularly.

Mr. BODAKEN. Just very briefly, Senator, I want to point out that I agree totally with what Ms. White said.

And for the record, would point out that of 184 publicly financed bond projects in Los Angeles have ever been in default where banks have participated.

So I agree wholeheartedly that it is a very rational thing for banks to be involved in at this point in time.

Ms. BUTLER. Senator Cranston, before we end the panel, I'd like to make just one final remark.

On behalf of Great Western Bank, I want to State that we're very pleased with our opportunity to talk about our record but more importantly we're very pleased to do this on your subcommittee. Throughout your career, you've been a tireless and effective advocate of housing and have represented California exceedingly well in this area. And we just wanted to take the opportunity to say, thank you, before this panel closed.

Senator CRANSTON. Thank you very much. That's very nice of you.

Mr. BODAKEN. Thank you, Senator. I join in those remarks.

Senator CRANSTON. Thank you. You've all been exceedingly helpful witnesses, and I thank you each very much.

And I'd like the second panel members to come forward.

Senator CRANSTON. I thank you for your patience through a long morning.

We will begin, as with the previous panel, with opening statements. Please be sure to keep within the 5-minute limit which you will see by the lights. We have to adjourn at about 12:50 p.m. and I do want an opportunity to ask a few questions. Perhaps other Senators will also.

Mr. Fletcher, would you like to lead off?

STATEMENT OF JAMES FLETCHER, PRESIDENT, SOUTH SHORE BANK, CHICAGO, IL

Mr. FLETCHER. Thank you.

Mr. Chairman, members of the subcommittee, I am Jim Fletcher, president and CEO of South Shore Bank of Chicago, IL. It is my belief that South Shore Bank was the only bank in the country to testify in favor of the Community Reinvestment Act prior to its enactment in 1977. So it is, therefore, a great pleasure that I return today to reiterate our bank support for CRA as well as to provide an overview of the impact that CRA has had on neighborhoods such as the one in which we work.

On the other side of that issue, it is a little painful to think that 15 years later we are still engaged in discussing what banks ought to be doing in their service areas when, in fact, a charter issued either by the State or by the Federal Government is to serve the community, and we are still trying to get banks to read their charter to serve their community.

I will argue not only should Congress continue to support vigorously the 1977 Community Reinvestment Act, but should also consider the public policy benefits of enhancing the capacities of community development banks in our country.

South Shore Bank is a community development bank located on the south side of Chicago. With almost 225 million in assets, the bank targets 5 minority communities in Chicago's south and west sides for its development lending efforts.

Since the current ownership and management bought the bank 19 years ago in August of 1973, we have made over $220 million in loans in these targeted communities. Through our subsidiary and affiliate companies, we have leveraged an additional $100 million in economic development finance.

South Shore Bank is the architect and perhaps best known practitioner of community development banking. Its Shore Bank parent holding company is in the business of rebuilding underinvested communities. That is, neighborhood development is our corporate mission.

To achieve the central purpose, we own and insure depository institutions and several proactive community development subsidiaries and affiliates. The Shore Bank organizational chart is attached to my written testimony.

South Shore Bank initiated its reinvestment lending prior to the passage of CRA. The Shore Bank blueprint dates to 1972 when the holding company was incorporated. It continues to expand its community reinvestment activities not out of pressure to comply with CRA but because community reinvestment is our business.

As I review the history of CRA I am struck by how much discussion and effort has gone into the processing of defining compliance, monitoring the effectiveness of the regulators in enforcing the law and documenting individual lender efforts. I am also struck by how many banks and savings and loan associations continue to view CRA and community reinvestment as a burden rather than an opportunity.

Development loans in South Shore Bank are market rate, unsubsidized credits made within the bank's target areas. The purpose is to accrue to the long-term economic development of those areas and their residents. As such, development lending falls into the categories of commercial, community organization, multifamily, home improvement, and education loans. Loans made by South Shore Bank to residents and local entrepreneurs to rehabilitate housing, finance businesses, buy or repair homes, and support nonprofits meets the credit needs of low- and moderate-income people.

Further, South Shore Bank's designed lending areas are neighborhoods that other lenders have considered and many continue to consider too risky to lend into. While our borrowers may appear to be unsophisticated, they have proven to be extraordinarily creditworthy. Our success in demonstrating how underinvested communities can, over time, become prudent lending areas and profitable markets has attracted other lenders to some of our target areas.

Let me illustrate our reinvestment efforts on one product, single family home mortgages. When current management bought the bank in 1973, single family homes in South Shore had been declining in value for a prior decade and precipitously since the mid-1960's. The area had been redlined by banks and savings and loans due to the rapid racial change that had occurred from 1965 to 1972 when, in fact, the neighborhood went from predominantly white to 95 percent African-American.

New bank management recognized the value of solid, gracious homes in the area and established single family home mortgages as one of its lending priorities and opening strategy.

Between 1974 and 1980, the bank made approximately $32.7 million in home mortgages in South Shore. As a result, home values increased faster in South Shore during this decade than any other community in the city of Chicago, and other lenders began to lend in South Shore.

By 1980, South Shore Bank had significantly reduced its single family mortgage lending in South Shore because the private market for credit was once again functioning. This decision has proved correct. According to the HMDA data, other banks and thrifts and mortgage companies made 232 home mortgages totaling $13.9 million in South Shore in 1990.

Despite the perception by many bankers that reinvestment lending is too risky and unprofitable, the experience of the South Shore Bank demonstrates that these perceptions are inaccurate. With the exception of 1 year over the last 10 years, the bank has consistently achieved a return on assets in excess of .80 percent as well as double digit return on equity. The bank's 1991 net loan losses were less than ¾ of 1 percent.

That was on $147 million outstanding loan portfolio, and continued the record of a 10-year outstanding trend.

Unfortunately, making loans in underinvested communities is not a priority for most banks. The Community Reinvestment Act and effective enforcement of the law is one of the most critical resources available to low- and moderate-income people in the communities. In Chicago alone, this law has produced CRA loan commitments totaling over $300 million.

Through discussions with nonprofit organizations, Chicago banks realized the need for first mortgages for larger multifamily buildings in city neighborhoods. And there is now an active lending market for acquisition and rehab of these buildings.

A similar process led to the creation of loans for mixed use buildings that have both residential and commercial use. It is hard for me to believe that without CRA enforcement that these loans would be available.

It is important that CRA continue to offer low- and moderate-income minority communities protection and not be dismissed by the banks in their rush to pursue bigger profits and faster profits. As we have seen to our peril often, these profits are short lived and in many cases extraordinarily costly.

Finally, I want to reemphasize that I believe it is not difficult to seek and find creditworthy borrowers in low- and moderate-income neighborhoods, and even less difficult to find less creditworthy borrowers in every level.

However, it is difficult to achieve long-term community development in underinvested communities by merely this act alone.

At the same time, we need specialized financial intermediaries, such as community development banks that are uniquely qualified to serve as models for broad scale and long-term development that can make the difference. Congress should, therefore, do two things:

Continue to support and strengthen CRA action and, two, examine ways to provide and strengthen and create the sustained and specialized financial institutions. This could include encouraging banks to invest capital in community development banks as one of the ways to make CRA responsible, and I will stop there, Senator.

Senator CRANSTON. Thank you.

I want to note that your prepared statements will appear in full in the record as if read and will be, of course, considered by the committee.

Ms. Johnson.

STATEMENT OF JULIA JOHNSON, VICE PRESIDENT FOR COMMUNITY REINVESTMENT, BANC ONE CORPORATION, COLUMBUS, OH

Ms. JOHNSON. Thank you, Mr. Chairman.

Thank you for inviting me here today to speak on the important matter of CRA.

I have prepared written testimony and would request that it be entered into the record so that I could just give you a brief summary of my remarks.

I am Julie Johnson. I am vice president of Banc One Corporation. We are a multibank holding company operating banking facilities in Indiana, Illinois, Michigan, Kentucky, Ohio, Texas, and Wisconsin. We have 57 different banks.

We have small banks in rural areas, we have large banks in metropolitan areas. Some are regulated by the Federal Reserve, some by the FDIC, some by the OCC. It's kind of a management challenge, but it gives us a breadth of experience that I think is helpful in the debate here before us.

Given that background, the first thing that I would like to say is that I do not see how we can discuss granting exemptions or safe harbor to anyone if CRA is considered in the context of our business. At Banc One we regard CRA, just as Great Western articulated earlier, as business as usual. If it is business as usual, it has got to be profitable.

We do not ask our shareholders to grant us safe harbor if we have had good earnings in one quarter. It makes as little sense to grant safe harbor to small banks or banks that have outstanding ratings.

I think that what we can do is make compliance more germane to the business that we do. To the extent that it is not relevant to our business, it can be considered a burden. I think that banks that require their board members to go out and do ascertainment in the community or make their CEO's spend the weekends painting houses might feel burdened.

Our senior management has to hold our lenders accountable for making loans. That's what they're there for. Our regulators need to look at our performance in the context of the business that we're in. Not all banks are all things to all people. Some banks are retail banks, some are mortgage lenders, some focus on commercial real estate.

I think that it is unreasonable and to some extent burdensome to ask a bank whose principle line of business is retail consumer lending to make unusual or unreasonable efforts in the areas of small business, just as it doesn't make sense to make a small business lender accountable for how many credit card loans they made someplace.

The whole thing needs another look in terms of the business, the strategic plans of our banks. If we look at that, we are going to be looking at a long term issue and not a short-term issue.

We are going to be looking at how we can develop markets; what kind of flexibility and creativity we need; what kind of support we need from local government and the Federal Government to facilitate the extension of credit profitably. It would cause us to review our underwriting criteria. Right now there is not an incentive to do that, at least there is not a perceived incentive to do that.

I think that to the extent that the banking industry looks at this problem as an immediate and short-term issue, many of them delegate their lending responsibilities to consortia in their community and so they figure if they've got it out of the bank and gave the job to somebody else, then there is no further requirement of them.

In addition to that, we have a number of financial institutions who are panicked and they attempt to buy market share by offering their products at a below market rate. I don't think you can sustain a program like that and I think that we need, over the long term, programs that are profitable and that will be sustained for that reason.

I think banks which set aside a limit for how much they are going to lend in a particular area are a reflection of an attitude that it's not profitable and so they need to limit the extent to which they are not going to have earnings in a particular area. So we need to take a look at that.

We need to focus on consumer lending in one way, small business lending in another, and the larger commercial real estate lending in yet another. I don't think you can lump them all together.

The last thing I would like to say quickly is the HMDA data is going to be coming out this year soon, maybe this week, maybe some of it is already out.

I don't think a lot of it is going to look much better than it looked last year, and I think a part of that is because the data came out in October of last year. I don't know any financial institution that had a poor record last year that in the two remaining months of 1991 could make a difference in their record.

In the debate that ensues in the coming days, we need to keep that in mind. And I think we need to be looking at what the 1992 data is going to look like.

With that, thank you very much.

Senator CRANSTON. Thank you very much.

Mr. Bradford.

STATEMENT OF CALVIN BRADFORD, PRESIDENT, COMMUNITY REINVESTMENT ASSOCIATES, DES PLAINES, IL

Mr. BRADFORD. Thank you, Mr. Chairman.

Access to capital and credit is the engine that drives all developing economies. But today as Congress reviews bill after bill to strip the Community Reinvestment Act of its powers, we have to ask ourselves if we care more about the economies of Poland, the former Soviet Republics, our North and South American neighbors, or almost any developing economy in the world than we do about our own inner-city communities in America.

Economists at the Fed have lauded the diversion of funds from the savings of individuals in lower income and declining income areas to areas of high growth and speculation as the efficient operation of a natural market channeling money to areas of highest demand. But when these false markets collapsed of their own weight, the taxpayers, whose Government guaranteed the flow of funds to the banking industry by insuring its deposits, were left to bear the costs of bailing out the fools and felons who ran these institutions into the ground under the watchless eyes of the Federal agencies charged with protecting the public interests.

Under the smoke screen of the alleged regulatory burden, the banking industry and the present administration are trying to gut the CRA and excuse our banking industry from the only obligation it has to serve the people in America.

The banks and thrifts claim a paperwork burden from an act that has no reporting requirements and requires only the production of a Community Reinvestment Act statement that we find is typically less than 4 pages long.

While the regulatory agencies claim that only performance counts, the CRA guide for the American Bankers Association states, "documentation is everything" and regulators in spite of their official policies seek out piles of papers and plans as a substitute for compliance.

The FFIEC contracted with a private compliance consulting firm to train its regulators and develop its compliance examination program. That firm subsequently sold its services to the American Bankers Association to develop their compliance manual.

It is a dereliction of duty for the regulatory agencies to farm out their compliance program development to private firms whose income clearly depends on the increase in paperwork burden. Even with public ratings, over 90 percent of all lenders get passing grades. It is no wonder the lenders want to use these to create safe harbor exemptions.

But in my work, I see lenders systematically cited for violations of HMDA, fair housing, and Equal Credit Opportunity Act violations and then given outstanding ratings.

For example, in New York, which has more multifamily housing than any other city in the Nation, both Manufacturers Hanover Trust and Chemical Bank, two of the largest lenders in the Nation, are given outstanding ratings even though between them they only made one multifamily loan, one multifamily loan in all of 1990.

Disclosure has been at the heart of reinvestment, but the Fed has consistently obstructed efforts to reproduce the data.

The regulators, however much they have denied the need for commercial loan disclosure, recognize its value so much that they tried to coerce lenders into producing it for them internally, but not for the public, in their policy statement last winter. Chicago has had commercial loan disclosure for institutions that want city deposit of funds for over 19 years. It works. It has provided a resource for identifying commercial credit needs in some of the most successful reinvestment programs in the Nation.

What remains a mystery is how newspapers, fair housing groups, community groups, and legislators have been able to find discrimination in the lending markets while the regulators have not. One case in the many I have given in my written statement serves to illustrate.

Peter and Delores Green sought a loan on the west side of Chicago, an African-American couple seeking to buy a home in an African-American community. They were turned down by Avenue Bank of Oak Park. The Greens easily qualified for a loan from another lender, but the Greens filed a complaint that was sent to the FDIC.

The FDIC never contacted the Greens to explore their complaint. The FDIC simply asked the bank for a reason for the denial and the bank responded that the loan was denied because of a low appraisal, a reason that was accepted by the FDIC even though, it turns out, the bank never did an appraisal.

The FDIC has 15 pages of guidelines for investigating complaints, the first of which says, contact the complainant. The guidelines were simply ignored.

When I asked an FDIC examiner how she knows if the bank is telling the truth when it explains why a loan is denied, she said, with confidence, "we trust our banks."

This sums up the attitude of the regulators. They see the lenders as "their banks" and are simply not interested in attending to the rights of minorities. Certainly we must have reached the low point of fair housing enforcement when the Greens now have to seek, in addition to suing the bank, legal support to sue the FDIC.

Finally, lenders often say it is not necessary for them to serve minority communities because these communities are served by FHA and VA loans made through mortgage banking companies who are fast becoming the largest lenders in the country. This, to me, is like the old lunch counter argument segregationists used to use in the South. It was OK as long as blacks had lunch counters of their own; it didn't make any difference; they didn't need to be able to eat at white lunch counters.

But FHA loans are, by design, high risk products. These high risk loans produce high losses when they are concentrated in single neighborhoods where there is no conventional lending.

As an added form of abuse, HUD requires properties to be conveyed to HUD vacant, resulting in foreclosures becoming abandoned properties.

A recent study by the National Training and Information Center of FHA foreclosure data reveals that in many minority neighborhoods delinquency rates run as high as 29 percent on FHA loans and foreclosures as high as 21 percent, resulting in abandonments. Just 2 weeks ago, Chicago was shocked when a 6-year-old African-American child named Lindsay Murdock was found beaten, raped, and stabbed to death in the garage of an FHA abandoned home just two blocks from where he lived, a home the community had been unable to get HUD to demolish.

The time has come to strengthen the CRA. Treat our inner-city neighborhoods and communities at least as well as we are now treating the former Soviet Union. Thank you.

Senator CRANSTON. Thank you very much.

Ms. Goldberg.

STATEMENT OF DEBORAH GOLDBERG, REINVESTMENT SPECIALIST, CENTER FOR COMMUNITY CHANGE, WASHINGTON, DC

Ms. GOLDBERG. Good morning, Mr. Chairman. I guess now it is good afternoon.

My name is Debby Goldberg and I am acting director of the Neighborhood Revitalization Project of the Center for Community Change.

I want to thank you for the opportunity to testify here this morning and even more I want to thank you for holding this oversight hearing.

It has been my observation over the years that the amount of energy devoted by the regulatory agencies to CRA enforcement is directly related to the amount of oversight conducted by Congress.

As you have heard from members of the previous panel, vigorous enforcement of this law is more important than ever for members of poor communities in Los Angeles and across the country. I hope that one of the results of today's hearing will be to add some stiffness to the spines of those in the banking regulatory agencies.

I have submitted written comments for the record and I want to just spend my time today on a few points. First of these is, how well those agencies are doing in enforcing CRA.

Three years ago, Congress made some very significant changes in the law. The hope was that by opening up the CRA process through requiring the regulators to make CRA ratings public along with evaluation reports, that CRA enforcement would become tougher.

Those changes have now been in effect for 2 years and it is a good time to look at how well they've been working.

On the surface, the numbers would appear to indicate that things are improving. The agencies are spending more time on CRA exams and the ratings distribution has shifted somewhat.

Four years ago, 99 percent of institutions examined received satisfactory or better CRA ratings. Now that number is 89 percent. However, I think the numbers hide the real story, which is first of all that the agencies are still not tough enough when they evaluate banks.

Second, the agencies don't use the full range of enforcement powers that they have to enforce CRA compliance.

Third, the evaluation reports that they issue are not nearly as useful as they could be.

Fourth, lenders performance in rural areas does not receive the same kind of scrutiny as that in urban areas.

And, fifth, far too much weight is given to CRA ratings in the application process.

I don't have time to talk about all these points, but I would like to focus for a moment on CRA enforcement in rural areas. Of particular concern to me is the weight given to a bank's performance in rural areas when its lending territory also incorporates urban communities. Take for example the Bank of America, which other people have mentioned here this morning, which had an outstanding CRA rating.

This is one of the largest banks in the country. It has 850 branches. It claims the entire State of California as its community for CRA purposes. The State of California, as you know far better than I, includes both some of the biggest cities in the country and vast rural areas as well.

If you read B of A's evaluation report which is about 11 pages long, you will find exactly two references to its performance in rural areas. I will quote them in their entirety.

First, we're told that "the bank extends a sufficient volume of agricultural loans, including credit to small farms," although we're never told how many loans that actually is.

Second, we're told that, the bank's participation in governmental insured, guaranteed, or subsidized programs includes, "the Farmers Home Administration." Again, we're given no indication of how many Farmers Home loans were made by B of A.

I should note that this lack of detail is common in evaluations of banks of all sizes, both urban and rural. And it illustrates just one of the many problems with the way evaluations are written.

But from B of A's evaluation and others that I've read, it appears to me that as long as a bank can show that it is doing something in urban communities, it can virtually ignore the rural parts of its territory with total impunity. This must change. If it doesn't, then I fear for the future of rural America.

And what about small banks in rural areas? These institutions are lobbying heavily for exemption from CRA. They argue that they couldn't exist if they didn't serve their communities and that CRA constitutes an unnecessary regulatory burden. I call this the "I am, therefore I comply," theory of CRA.

And I would like to look at each of these assertions in turn.

First, there is no evidence that small banks actually make significant volumes of loans. According to research by the staff of the House Banking Committee, the average ratio of domestic loans to total assets of banks over $10 billion is 63 percent. For banks under $100 million in assets, that average is only 55 percent, a substantially lower figure.

Other research has turned up individual small banks with much lower loan-to-asset ratios. Whatever these banks may be doing with the money they take in from their communities, they aren't lending much of it back out.

Further, if small banks had exemplary CRA records, one would expect to see them getting a disproportionally high percentage of the good CRA ratings that are given out. In fact, the opposite is true. Banks with assets under $100 million represent 74 percent of all banks examined for CRA compliance to date. Yet they received only 55 percent of the outstanding ratings.

What about the question of regulatory burden? Banks think that they have to spend a lot of time manufacturing meaningless paper to show their examiners. Then they are not paying attention to what the agencies say, because the agencies have been very clear that the documentation they expect is only what a bank needs in the normal course of its business.

I would like to refer to the manual that Cal described earlier published by the ABA. Because I think this may be part of the source of the problem. That CRA compliance manual suggests that banks ought to be maintaining 15 separate CRA documentation files with various subfiles, and they provide more than 80 pages of forms for banks to use to fill up all those file folders.

It doesn't surprise me that bankers claim that CRA is a headache.

I would like to close by saying that while many banks are focusing on how to produce more paper, community groups are focusing on how to get more loans in their neighborhoods. Unfortunately they still aren't getting much help in this effort from the banking regulators.

I hope that this subcommittee and all of Congress will continue to turn up the heat on agencies until they learn how to do the job properly and until all the banks in the country come to learn the lesson illustrated so well by South Shore and a handful of others, namely that CRA can be good business as well as being good for the community.

Thank you, Mr. Chairman. That concludes my testimony.

Senator CRANSTON. Thank you very, very much.

I have just a few questions and I ask you to be as brief as you can in responding so we can finish our work on schedule. Your testimony has been very helpful.

CRA has become the focus of a great deal of controversy in the last couple of years. There are a number of legislative proposals that seek to limit the law. There are a variety of proposals that exempt banks of certain asset size and provide a safe harbor for other banks.

President Bush has sent us a proposal that would allow banks under $100 million to self-certify compliance and that would provide safe harbor to other banks. The President's bill would also eliminate language that Congress included in FDIC/CRA that mandates that the evaluation include supporting data for the evaluation.

How important is this law to the efforts you have described this morning and what would be the impact if banks were exempted from regular CRA examinations as is proposed in the Bush bill and other legislative initiatives? How do you view the safe harbor initiatives? And, finally, why is CRA, a law that has been in effect for 15 years, only become controversial now? If you can answer that broad question briefly, I would appreciate it.

Ms. Johnson.

Ms. JOHNSON. I will give it a quick shot.

I believe that the history of banking and the extent to which the industry has been heavily regulated has been an impediment to the creative thinking of many bankers. And I think that that is what CRA requires, that we think, that we be creative, we reflect, and that's kind of the beauty of it. We're not told what to do; we're told to think and act strategically.

I think that without CRA, that most bankers would probably go back to not really thinking about it.

Senator CRANSTON. Any other comments?

Ms. GOLDBERG. It was a multipart question, so it is hard to answer them all.

I would agree with what Julia has just said. I think the reaction that we get from the community groups that we work with around the country is that whatever advances we've made in getting access to credit from banks have been the direct result of CRA.

But if CRA were taken away, they feel that they would go back to square one in terms of their ability to get access to credit for their communities.

And I think all of the provisions that you've described in the Bush bill would have a devastating impact in addition to sending really the wrong message to the industry and sending the message that it doesn't really matter and you don't have to worry about it.

I want to make one particular point about the safe harbor provision, because I think that is a particularly bad public policy idea. I think it has been extremely important in the way that we administer regulations and laws in this country that the agencies involved are required to develop as complete a record on a particular issue, in this case an application, as possible. And the agencies all admit that the examination process that they undertake for CRA compliance is far less than complete and far less than perfect.

So that the reflection of the record of a bank's performance that they get through the evaluation reports is incomplete and imperfect and not in and of itself a valid basis for making a decision on an application to the exclusion of all other evidence. And what a safe harbor would do would be to prevent people who have relevant and important comments to make and information to provide about a bank's record from providing that, to be part of the agency's consideration in the process. And it simply doesn't make sense to do that.

Senator CRANSTON. Thank you very much.

Do you have a comment?

Mr. BRADFORD. I would just comment that I think the response of the administration to essentially try and gut the CRA is so incredibly ironic. Over the last 20 years you have really had a revolution at the community level of people changing from organizing to get access to Government funds to people organizing to get the private economy to work in their neighborhoods. And the main resource they've used has been the CRA. Which means essentially that community organizers who are often thought of as radical have adopted a sort of Reagan-Bush economic approach to saving their neighborhoods and now the administration wants to turn around and take away the resource they have used to make that happen and that saves the Federal Government billions of dollars in public money by using private money for this development.

Senator CRANSTON. Several of you on both panels noted serious deficiencies in the enforcement of CRA. This is a question we have been struggling with for some time. The requirements are really quite minimal compared to other consumer laws and the safety and soundness requirements.

Why do you think that the regulatory agencies have had so much difficulty or failed as they have in enforcing the law? Is it a lack of capability, a lack of commitment, or both?

If you could—and let me then add if you could choose two ways in which you could improve enforcement of CRA, what would those two ways be?

Who would like to respond? Yes.

Ms. JOHNSON. I would like to respond. I said before in my testimony that CRA is oftentimes not tied into the business plan of a bank. To the extent that it bears no relevance to the business plan, regulators come in and are asked to evaluate something that doesn't make any sense.

I think it is only natural that they have a difficult time trying to enforce the statute. They are not doing it in an environment that makes a lot of sense.

So if I had two wishes, it would be that the regulators require that the CRA programs make sense in terms of the business plan and not require that everybody be everything to everyone.

The other thing is I think we ought to start including some of the other lenders. We are not the only lenders out there. We could spread CRA to other lenders.

Thank you.

Mr. FLETCHER. I think one of the problems with the unevenness with regulators is that the waters have gotten muddied with all of the documentation that was spoken earlier, that if the regulators were asked to come in and look at production, how many loans did you put out and where did you put them out and document that and evaluate that process, and not how many pieces of paper one had in one's file, that you would see the regulators—I think they would be much happier with that kind of thing.

And certainly, I think that the banks that are doing the job are getting credit out in lower- and moderate-income neighborhoods, would feel far more effective by what they're being judged by.

Mr. BRADFORD. I would just say that I think that as far as enforcement is concerned that the regulators again do need to look at performance. And if you find a lender that is performing, that is providing banking services and making loans that are consistent with its reasonable business plan, you should go home, give them the rating and go home. Do not harass these people. And that seems to be, I think, one of the major problems.

But I think the agencies are incapable, because they have a lack of commitment to use both questions, and as I have submitted in my written statement, there are just numerous examples of the incompetency of the way the process works.

I was asked to testify in a fair housing case in Toledo against Home Savings of America, which has a home base in California. It is the largest depository lender in the country in home lending. The branch manager there had lost two-thirds of all of the fair housing records that were required to be kept by the regulators and was unfamiliar in the deposition she gave with how to interpret some of this information.

It is amazing that the OTS that supposedly regulates this institution would allow that to happen when their regulations say they're supposed to check the data's accuracy.

What was more amazing was a week after this branch was closed, this branch manager went to work for a consulting firm that later was hired by the OTS to train them in fair housing enforcement.

I think they are incompetent because they don't care. They have never hired fair housing people who have any background in litigation or enforcement of fair housing. They have hired people who used to work for banks or used to work for the regulatory agencies.

So if they were really serious about enforcement, they would hire people who know both to deliver their programs.

I keep a library of CRA agreements. Unfortunately the regulators do not. It seems to me if they were interested in reinvestment, they would want to know what those programs look like so they would know what success would look like.

Ms. GOLDBERG. I guess I would add to the list why the agencies haven't done a better job. I think for many years CRA enforcement was an extremely low priority within the agencies and that, even though that has changed somewhat, they are still plagued by the attitude that safety and soundness is what they are really about and that this is less important stuff.

And in addition, there is a tendency among the agencies to kind of view the industry as their clients. And as long as you view the industry as your client, you are not going to be very tough in enforcing the law.

And I think in addition to the suggestions that the other panelists have made about ways to improve CRA enforcement, two that I would add would be for the agencies to use the full range of compliance tools that they have, not just to wait until a bank files an application and then think about whether or not to deny that application or impose conditions, things that don't happen very often.

But they have a whole range of tools that they use in their enforcement of a lot of other laws and regulations that they don't tend to haul out in the CRA context.

And the other suggestion would be to spend a lot more time outside the bank, not just listening to the bank's side of the story about its performance but to listen to what people in the community have to say. To not just trust but also verify what the bank claims to be doing. And that incorporating outside comments ought to be part of their application approval process as well.

Senator CRANSTON. One final thing I would like to get into. It appears that one of the principal problems is CRA enforcement. There is an overemphasis on process and underemphasis on performance. Banks that receive outstanding ratings may be outstanding only in the amount of documentation that they produce.

Of the 12 assessment factors of the CRA evaluations, only three—only three—directly pertain to actual lending efforts.

How do we focus the evaluations on performance? Does the rating system need to be revised and do the number of assessment factors need to be reduced? Do you have any comments on that?

Ms. JOHNSON. I think that the process is good the way it is, I think it can work. We need to have a framework within which to operate our CRA programs. And if we have a process such as the one that we have, we can measure our results within that context. If we don't have the results then we know where to go to start tinkering with the process, whether it is in our marketing or in our underwriting.

So I think that it is important that we retain that, that we use it all. But I do think that we have to do a much better job of measuring and evaluating that process in terms of the results.

Senator CRANSTON. Finally, I was interested to note in Ms. Goldberg's testimony that the American Bankers Association puts out a 475 page guideline book on how to implement CRA, 84 pages alone is devoted to setting up CRA files.

Is that what causes in good part the paper burden? And what about the role of consultants? Are they making the process more convoluted than direct? Final comments on this point?

Ms. GOLDBERG. That was my testimony; I guess I may as well take a crack at it.

I think that the real problem is the way that the agencies have been enforcing the law in that the consulting industry that has grown up has taken advantage of the weaknesses in the agency's own enforcement process. And it really goes back to the earlier question that you just asked about the overemphasis on process and the underemphasis on performance.

In my view, Congress has made tremendous efforts to get the agencies, at least in their evaluations, to shift that emphasis.

I mean, first you asked them to put in facts about banks' performance and then when they didn't do that, you asked them to put in data to support their facts. I don't know how many more synonyms there are out there to get the message across that you want them to focus on whether a bank is actually making loans and not on whether it is just producing paper.

I think part of the answer is going to be continued oversight, and I am not sure what the rest of the solution is on this point.

Senator CRANSTON. Any other comments?

Ms. JOHNSON. Just one more point. If we look at this in terms of business again, our CFO doesn't hire a consultant to come in and explain our earnings. So if we don't understand our own numbers, then God help us all.

[Laughter.]

Senator CRANSTON. You've been—do you have a comment?

Mr. FLETCHER. I just want to add one little thing. Not on this so much, but that is to say that I think part of the problem is the fundamentals. That what we have got here is a negative response.

If a bank doesn't want to do anything, it doesn't care about its CRA rating. If it wants to merge or go someplace, then it cares. I think we've got to find a way to put some carrots in this piece of legislation and not just have it be all sticks, or we will continue down this road.

Senator CRANSTON. You have all been very helpful. I thank you very much.

We may have some further questions submitted for written responses for members of both this and the first panel.

I thank all of you for your cooperation, for your attendance, for your interest.

We stand adjourned.

Thank you very much.

[Whereupon, at 12:45 p.m., the hearing was adjourned.]

[Witnesses prepared statements and additional material supplied for the record follow:]

TESTIMONY OF SHARON BUTLER
GREAT WESTERN BANK

Mr. Chairman, members of the subcommittee, thank you very much for the opportunity to testify today on the Community Reinvestment Act. On behalf of Great Western Bank, I commend you, Mr. Chairman, as well as other members of the subcommittee for your willingness to have hearings on this subject.

I am Sharon Butler, Vice President of Community Development for Great Western Bank, a Federal Savings Bank, the principal subsidiary of Great Western Financial Corporation with $38.6 billion in assets. Great Western is one of the Nation's leading residential real estate lenders with 190 home loan offices in 21 States. In California, our home State, Great Western ranks first in mortgage market share for purchase loans, zero to one million dollars; in our hometown, Los Angeles, we're also number one.

Mr. Chairman, at the end of last year, Great Western had nearly one-third of its home mortgage portfolio—some $12 billion—in low- and moderate-income or minority neighborhoods. In South Los Angeles, where we have long been the leading home mortgage lender, Great Western wrote more than $260 million worth of home loans over the past 2 years. That made home ownership possible for more than 2,200 African-American and Latino families.

We are proud of this record. We know that many believe lenders will not . . . or cannot . . . operate in the inner cities of America. Great Western's message today is that lenders can and will invest in all communities.

We also know that many believe this investment will be made only as a result of the requirements of the Community Reinvestment Act. Great Western's message today is that our lending record is the result of fundamental business strategies—strategies that were in place before the CRA came into existence and strategies that we would pursue if there were no CRA.

These strategies are built around several simple elements. First: We believe smaller balance loans, made to people where they live, are less risky than the more speculative loans at the upper end of the scale. So we have consciously targeted our efforts at the affordable end of the housing market.

Second: Once you make that assumption, it is only logical to open or maintain lending offices in those bread and butter communities. We have nine offices in our South Los Angeles Region, serving all communities including South-Central. These are not savings branches. They are free standing lending offices.

Third: Those offices are staffed by commissioned loan personnel. These mortgage loan consultants have every incentive to scour the territory where they work each day for creditworthy loans. If they do not, they don't make a living.

Fourth: It is not our loan consultants alone who work out of these offices. They are part of an on-site team that handles appraisals, underwriting, processing and all the elements of a loan decision from start to finish, on a decentralized basis.

We call these full-funding offices. Perhaps we should call them equal-opportunity offices. Because by their very nature, they help eliminate the stereotypes that discourage lending in such communities.

The loan consultant has an incentive not to discriminate—his or her pocketbook. The office manager has an incentive to hire agents who can effectively produce creditworthy loan volume in their local community. So, for example, if a market gradually becomes Spanish speaking, it will almost inevitably follow that our managers will look to hire bilingual loan personnel. (Half of our top ten loan personnel are bilingual nowadays.) Finally, the back office team that underwrites and processes the loan is not sitting fifty miles away in a centralized decision-making center with no feel for the nuances of a neighborhood or an individual property. They work, and often live, in the very community where we are lending.

Self interest is a powerful motivator, Mr. Chairman. Our loan system illustrates how effectively it can work. We believe there are three other important factors in our success.

First, we are a portfolio lender. While we sell many of the loans we originate in the secondary market, we have an appetite for loans that we will hold in our *own* portfolio. Over the years, that has given us added flexibility in understanding the circumstances of the individual borrower.

Second, we are primarily an adjustable rate mortgage lender. For the better part of the last decade, the ARM has allowed us to offer better opportunities for affordable homeownership—with payment protection—to borrowers in every community we serve.

Finally, we are a color blind lender. In 1968, Great Western developed an explicit written policy against denying loans based on geographical considerations, a decade before the Community Reinvestment Act outlawed such practices. We are proud of our insistence that our people make their lending decisions based on the value of the property and the borrower's ability and willingness to repay.

Mr. Chairman, there are many other elements of Great Western's performance under the Community Reinvestment Act that are important. We know that we cannot meet all the needs of our communities through our lending activity and, therefore, we have been a pioneer supporter of a wide range of low-income and affordable housing programs through our community development activities. We would be happy to provide you with additional information on these efforts, as well as the full extent of our success in lending in low- and moderate-income and minority communities, if you wish.

But the heart of our success is our lending record. And the secret to that record is not special programs. It is not looking at certain neighborhoods as though they need special treatment by lenders. In fact, the deterrents to more active investment in all neighborhoods will never be overcome until they are seen as Great Western sees them: neighborhoods in which we can make good money by doing what—for us—is business as usual.

We have built this record because we felt it would be prudent and profitable and, therefore, in the interest of our shareholders to do business this way. Perhaps this is testimony to the kinds of incentives that would be most powerful and most effective in improving the Community Reinvestment Act. The carrot of profit-making or profit-enhancing incentives should be a far more powerful inducement for lenders to "do the right thing" than reams of paperwork or the threat of punitive regulation.

In closing, I want to make an admission, on behalf of the people who run our lending group. We feel as though we are playing with a double-edged sword today. The more our competitors adopt the Great Western formula, the more competition we will face. You can't entirely blame us for wanting to have the field "to ourselves." But in the long run, if our message is heard by you, by the regulatory community, and by other lenders, the results can only be good for communities like South-Central Los Angeles. That is why we are here today.

Thank you.

TESTIMONY OF SENATOR JOSEPH M. NEAL, JR. STATE OF NEVADA REPRESENTING THE LAS VEGAS ALLIANCE FOR FAIR BANKING

SEPTEMBER 15, 1992

SUMMARY

Scope of the Report

There were approximately 60 banks, savings and loans, credit unions, mortgage companies, and other lenders active in the Las Vegas area in 1990. In the aggregate, they made 10,658 loans on one- to four-family residences, with a value of $922.2 million. These loans consisted of home purchase mortgages, refinances, and home improvement loans.

Of the 60 active lenders, we found that just six (or 10 percent) made more than half of all loans. We examined the lending records of all lenders in the aggregate, as well as the top four deposit-taking institutions on this list: Citibank, Valley Bank and Valley Mortgage Company (hereafter "Valley"), First Interstate Bank of Nevada, and Primerit Bank.

Findings

1. Home loans to the Westside.

- Of 10,658 home loans made by all lenders in Las Vegas, only 59 went to the Westside.
- Just three-tenths of one percent of the nearly $1 billion in home loans in 1990 found its way to the Westside.
- Of the four leading lenders, First Interstate made only $59,000 in loans to the Westside; Citibank and Primerit each loaned $114,000; Valley loaned $564,000.

2. Deposits in branches close to or serving the Westside, compared with dollars loaned to the Westside.

- Evidence suggests that bank deposits originating in the Westside and other minority communities are siphoned off to be loaned or invested anywhere but in their communities of origin.
- Valley Bank's two branches close to the Westside had $96 million in deposits in 1990; Valley's home loans to the Westside came to $564,000.

- First Interstate's two branches close to the Westside had $94 million in deposits in 1990; the bank loaned just $59,000 to the Westside.

3. Denials of loan applications from African-American and white applicants.

- Las Vegas lenders rejected mortgage loan applications from blacks 1.5 times more often than from whites, even when applicants had similar incomes.
- A black applicant for a home loan with an income above $41,500 was as likely to be rejected as a white applicant with an income below $27,700.
- Among leading banks, First Interstate rejected middle income black applicants more than five times as often as middle income white applicants.

4. Home purchase loans to African-American borrowers throughout the Las Vegas area.

- African-Americans make up about 9 percent of Clark County's population but receive less than 3 percent of all home purchase loans.
- Valley and Primerit each made about 3 percent of their home purchase loans to blacks; First Interstate made only 1.6 percent of its loans to blacks.

5. The leading banks' market share of home purchase loans to African-American and white borrowers.

- First Interstate's market share of loans to blacks is half its market share of loans to whites.
- Valley and Citibank have a slightly greater market share of loans to blacks than loans to whites, while Primerit's market shares are almost equal.

6. Home purchase loans to all neighborhoods with predominantly minority populations.

- Of the 8,581 home purchase loans made by all lenders in Las Vegas, only 183 (2.1 percent) went to 15 Las Vegas census tracts with more than 50 percent minority residents.
- Eleven predominantly white census tracts (with less than 20 percent minority residents) each received more home purchase loans than the 15 predominantly minority tracts combined.

7. Home purchase loans in low- and moderate-income neighborhoods.

- Only 6.8 percent of the 8,581 home purchase loans in 1990 went to low- and moderate-income areas of Las Vegas.
- Primerit and Citibank made 10.6 percent and 8.5 percent, respectively, of their home purchase loans to low- and moderate-income neighborhoods, exceeding the aggregate distribution. Valley, at 6.7 percent, matched the aggregate.
- First Interstate made only 2.7 percent of its 563 home purchase loans in low- and moderate-income neighborhoods.
- Upper-income neighborhoods received more than 57 percent of the $811 million allocated for home purchase loans by all lenders in Las Vegas.

8. The leading banks' market share of home purchase loans in low- and moderate-income neighborhoods.

- Valley came close to having equal market shares, at about 8 percent, in all three HMDA income categories.
- Primerit had a 50 percent greater share of the low- and moderate-income market than it had of the upper income market.
- First Interstate's share of the upper income market, at about 10 percent, was not only the largest among the four leading bank lenders, but was also four times larger than its share of the low- and moderate-income market.

Recommendations:

- The appropriate regulatory agencies should investigate every Nevada financial institution with disproportionate denial rates between white and minority applicants.
- The Federal Reserve should not approve any application subject to CRA involving financial institutions with disproportionate denial rates between white and minority applicants until the institutions demonstrate to the satisfaction of regulators and the communities in which they operate that they have taken steps to correct such disparities.
- Regulatory agencies must take lending patterns in low- and moderate-income communities more fully into account in CRA evaluations. Financial institutions that show a clear preference for lending to upper income, predominantly white communities and applicants should not qualify for "Outstanding" or "Satisfactory" CRA ratings.
- State and local governments should develop legislation, after suitable review of policies in place in other communities around the country, to require banks to demonstrate a high standard of community reinvestment in order to qualify as depositories for public monies.

LAS VEGAS ALLIANCE FOR FAIR BANKING

CASHING OUT

A REPORT ON HOME MORTGAGE LENDING TO MINORITIES AND LOW- AND MODERATE-INCOME NEIGHBORHOODS IN LAS VEGAS

JUNE 1992

"A few miles and a world away from the blazing neon and flashing billboards where tourists stroll, this city's black neighborhoods have been wracked by mob violence almost every night since the riots began in Los Angeles."

—*New York Times,* May 19, 1992

"Local critics have warned gaming moguls that they need to worry less about image and more about the deteriorating, long-ignored west Las Vegas ghetto. . . ."

—*Los Angeles Times,* May 27, 1992

"By midnight, police had cordoned off the area around the Golden West and approximately 80 policemen remained in the area. Black community leaders had warned city officials last summer that trouble was brewing. . . ."
—*Las Vegas Review-Journal,* October 6, 1969

A. Introduction

Las Vegas's reputation through the 1980's as the fastest growing city in the Nation was not inaccurate. It was simply not the whole story. Some parts grew faster than others. Some parts grew very little if at all. By the end of the decade, in 1990, whole communities existed where a few years before there was open land. The Census Bureau carved 31 new tracts into Clark County in 1990, home to a largely white and largely affluent population, 50 percent greater in numbers than it had been 10 years earlier. The minority population, almost doubling in the same period, lived elsewhere: by 1990, nearly 40 percent in just 15 older, more centrally situated census tracts.

This report examines some of the ways in which Las Vegas's banks and other mortgage lenders have set the stage for Las Vegas's passage through the 1990's.

B. Scope of the report

Following the Federal Reserve's release of the 1990 Home Mortgage Disclosure Act reports in October, 1991, the Las Vegas Alliance for Fair Banking reviewed the aggregate data for all financial institutions that made home loans in Las Vegas in 1990.

There were approximately 60 banks, savings and loans, credit unions, mortgage companies, and other lenders active in the area in 1990. In the aggregate, they made 10,658 loans on one- to four-family residences, with a value of $922.2 million. These loans consisted of home purchase mortgages, refinances, and home improvement loans. (See Table 1, page 20 of this report.)

Of the 60 active lenders, we found that just six (or 10 percent) made more than half of all loans. These top lenders are listed in Table 2, page 20.

We examined the lending records of the top four deposit-taking institutions on this list: Citibank, Valley Bank and Valley Mortgage Company (hereafter "Valley"), First Interstate Bank of Nevada, and Primerit Bank. These institutions are subject to the 1977 Community Reinvestment Act (CRA), as amended, which imposes a responsibility on banks to meet the credit needs of all the communities they serve, including low- and moderate-income communities.

We looked at the following patterns, utilizing both aggregate data and data on individual leading lenders:

1. Home loans to the Westside.

2. Deposits in branches close to or serving the Westside, compared with dollars loaned to the Westside.

3. Denials of loan applications from African-American and white applicants.

4. Home purchase loans to African-American borrowers throughout the Las Vegas area.

5. The leading banks' market share of home purchase loans to African-American and white borrowers.

6. Home purchase loans in neighborhoods with predominantly minority populations.
7. Home purchase loans in low- and moderate-income neighborhoods.
8. The leading banks' market share of home purchase loans in low- and moderate-income neighborhoods.

C. Findings

1. Home loans to the Westside.

- **Of 10,658 home loans made by all lenders in Las Vegas, only 59 went to the Westside.**
- **Just three-tenths of one percent of the nearly $1 billion in home loans in 1990 found its way to the Westside.**
- **Of the four leading lenders, First Interstate made only $59,000 in loans to the Westside; Citibank and Primerit each loaned $114,000; Valley loaned $564,000.**

The Westside is defined by five census tracts: 2.01, 3.01, 3.02, 35 and 37 (see Figure 1, page 24, and Table 3, page 21).[1] In 1980, the Westside's population was 18,519. By 1990, the population had decreased to 16,204, of whom 13,796 (85 %) were African-Americans.

A description of the role of the Westside in the social and economic history of Las Vegas is beyond the scope of this report. It is worth noting, however, that the Westside's exclusion from the flow of credit and capital in the city extends to the 1930's and beyond. The concentration of African-Americans there began in the 1940's, determined by such measures as covenants restricting the sale of housing and land in Las Vegas to whites only, the refusal of landlords to rent to blacks, and conditions on the renewal of business licenses for blacks requiring them to move to the Westside.

A housing survey of the Westside in 1949 reported that 80 percent of the community's structures were substandard. Streets were unpaved well into the 1950's. By the early 1960's, as historian Eugene P. Moehring has observed, the redlining of the Westside had become a contentious political issue, and "it was well known that [First National Bank] had granted few home loans or mortgages to the zone."[2]

The practice continues, as do some of the players, although generally under new names. As Table 3 and Figure 1 show, the Westside received only *59* of the 10,658 purchase, refinance, and home improvement loan made by Las Vegas's sixty mortgage lenders in 1990—less than one loan per lender.

Of the $922 million of mortgage finance allocated to Las Vegas in 1990 by these multimillion- and multibillion-dollar lenders, just *three-tenths of one percent* found its way to the Westside.

Among the four leading home mortgage lenders, the aggregate pattern was replicated, with some variations. First Interstate, Primerit, and Citibank made three loans each to the Westside; Valley made 12 loans (1.3 percent of its total loans).

In monetary terms, First Interstate loaned *less than one-tenth of one percent* of its mortgage funds to the Westside: $59,000 out of more than $62 million in all of Las Vegas. Primerit and Citibank each loaned $114,000, out of $62 million and $73 million, respectively. Valley loaned $564,000 or about six-tenths of one percent of all its mortgage lending.

These patterns are neither accidental nor the result of some temporary economic fluctuation. As other data discussed below demonstrate, the flow of credit and capital for home loans follows deliberate courses. Financial institutions make and pursue decisions to penetrate existing as well as emerging markets. Products are developed and promoted, staff is encouraged to achieve defined goals, deposits are directed into carefully considered investments, and so on.

For lenders in Las Vegas as a whole, and for the leading lenders in particular, the *exclusion* of the Westside has been as deliberate as the *inclusion* of other parts of Las Vegas, whether old or new.

2. Deposits in branches close to or serving the Westside, compared with dollars loaned to the Westside.

- **Evidence suggests that bank deposits originating in the Westside and other minority communities are siphoned off to be loaned or invested anywhere but in their communities of origin.**
- **Valley Bank's two branches close to the Westside had $96 million in deposits in 1990; Valley's home loans to the Westside came to $564,000.**
- **First Interstate's two branches close to the Westside had $94 million in deposits in 1990; the bank loaned just $59,000 to the Westside.**

In 1990 there were no bank branches in the Westside.[3] There were, however, a number of branches of the major lenders near the Westside, and it is instructive to measure the deposits in these branches in relation to the value of home loans made in the Westside.

First Interstate Bank, Valley Bank, and Primerit Bank each have one or more branches that serve or are near the Westside.[4] Table 4 (page 21) lists these branches and their deposits in 1990, as well as the value of home purchase loans made by the banks in the nearby communities.

The rate of home mortgage lending to communities that may be presumed to make considerable use of these branches for personal as well as commercial deposits is quite striking.

Valley Bank's two branches close to the Westside, for example, had a total of $96 million in deposits in 1990; in the same year, Valley made 12 mortgage loans to the Westside, worth $564,000. First Interstate's two branches close to the Westside had a total of $94 million in deposits in 1990; in the same year, First Interstate put just $59,000 back into the Westside by way of three home loans.

Primerit's branch close to the Westside had about $15 million in deposits in 1990; in the same year, Primerit made 3 home loans to the Westside, worth $114,000.

For a standard of comparison, we looked at the same relationship in a wealthier, predominantly white community about five miles to the west of the Westside (see Table 4, page 21).

This community, bounded on the north and south by Vegas Drive and Charleston Boulevard, and on the east and west by Rainbow

Boulevard and Buffalo Drive (census tract 30.02), had a population in 1990 of some 11,000, of whom about 85 percent were white. Las Vegas's 60 lenders made 152 home loans, worth nearly $11.2 million, to tract 30.02 in 1990. Recall that the five tracts of the Westside, combined, received only 59 loans, worth $3.1 million, from these same lenders.

First Interstate, Valley, and Primerit each have a branch near the Rainbow Boulevard/Westcliff Drive junction, on the eastern boundary of tract 30.02.

First Interstate's Rainbow-Westcliff branch held nearly $58 million in deposits in 1990, about the same as the bank's North Las Vegas branch. In contrast to three loans worth $59,000 in the Westside, however, First Interstate made 23 loans, worth nearly $1.2 million, on properties in tract 30.02.

Valley Bank had approximately $32 million in deposits at its Rainbow-Westcliff branch, about one-third of the combined deposits at its two branches near the Westside. Valley Bank and Valley Mortgage made 17 loans, worth $925,000, in tract 30.02.

Primerit's Rainbow branch had some $28 million in deposits in 1990, about double the North Las Vegas branch. Primerit made 13 mortgage loans, worth $1,693,000, to tract 30.02, four times as many loans, and nearly 15 times as many dollars, as it loaned to the Westside.

In the absence of more precise data on the flow of deposits from specific communities to specific branches, the relationships examined here can only be suggestive of a capital movement out of minority and low- and moderate-income neighborhoods and into predominantly white and affluent neighborhoods. The point is that minority communities generate substantial deposits in bank branches in or close to their neighborhoods; there is nothing to indicate, however, that the dollars are returned to those neighborhoods at a rate at all comparable to what occurs in predominantly white neighborhoods.

Indeed, a recent 14-city study by the Association of Community Organizations for Reform Now (ACORN) found that, on average, for every dollar on deposit in predominantly white neighborhoods, banks and thrifts made eight cents in mortgages available locally. In minority neighborhoods, the ratio fell to four cents.[5]

3. Denials of loan applications from African-American and white applicants.

- **Las Vegas lenders rejected mortgage loan applications from blacks 1.5 times more often than from whites, even when applicants had similar incomes.**
- **A black applicant for a home loan with an income above $41,500 was as likely to be rejected as a white applicant with an income below $27,700.**
- **Among leading banks, First Interstate rejected middle income black applicants more than five times as often as middle income white applicants.**

The home mortgage information released by the Federal Reserve in October, 1991, marked the first time data on the disposition of applications by the race and income of applicants had been made publicly available.

One of the most consistent patterns disclosed by the data was the difference in the denial rates of applications from minority and white applicants. Across the nation, in institution after institution, applications from minorities were denied more often than for whites of similar income.[6]

Early in 1992, the Office of the Comptroller of the Currency disclosed that it was investigating more than 250 banks under its supervision whose rejection rates for minorities were disproportionately high, or which received fewer than 1 percent of their applications from minorities.[7]

As Figure 2.1 illustrates (page 25), among Las Vegas lenders in the aggregate, loan applications from blacks, regardless of where they may live, were denied 1.5 times as often as applications from whites.

The pattern persisted even when applicants came from the same income categories.[8] Middle income black applicants, for example, with incomes between $27,665 and $41,500, were 1.4 times more likely to be denied a loan than white applicants in the same income category.

Upper income black applicants (with incomes above $41,500, or 120 percent of the area median) were turned down at *exactly the same rate* (23.5 percent) as white applicants with low- to moderate-incomes (less than $27,665, or 80 percent of the area median).

The leading lenders among banks showed significant and dramatic variations in their patterns of loan rejections (see Figures 2.2–2.5, page 26).

First Interstate denied loan applications from blacks on the whole more than four times as often as front whites. Even within the same income categories, blacks were denied loans considerably more often than whites: up to *six times* more often in the case of middle income applicants, and nearly three times more often among upper income applicants. An upper-income black applicant (with an income of *at least* $41,500), was twice as likely to be denied a mortgage by First Interstate as a low- to moderate-income white applicant (with an income of no more than $27,665).

The pattern at Valley Bank and Valley Mortgage differed considerably from the aggregate as well as from the other leading lenders in that overall loan denial rates were very low, and there were no loan denials involving black applicants. Of the 34 applications Valley received from African-Americans, 32 resulted in loans and two were withdrawn.[9] Among white applicants, too, Valley's rejection rate, at 3.5 percent overall, was well below the other leading lenders.

At Citibank, middle income blacks were turned down nearly twice as often as middle income whites, although in the upper income category denial rates were approximately the same. On average, Citibank denied loans to blacks at just about the same rate as to whites.

At Primerit Bank, low- and moderate-income blacks were denied loans twice as often as whites in the same income category. For every two upper income white applicants denied a loan by Primerit, three upper income black applicants were rejected.

The fact that racial differences in the rate of loan application rejections in Las Vegas replicate findings in other cities is not surprising. The city's history partakes of a national history of legal and informal racial segregation in every area of life, including the pursuit of domestic tranquility. That blacks are more likely, and often much more likely, than whites to be denied access to credit mirrors other differences experienced in daily life by the two races, such as the mortality of their infants, violence at the hands of police, unemployment, incarceration, and life expectancy.

Despite the African-American community's persistent demands to be included in the definition of what constitutes a good and creditworthy market, financial institutions in Las Vegas, for the most part, conduct business as they do elsewhere: denying that race plays a role in their product development, marketing, credit extensions, or hiring, while compiling a record that demonstrates the opposite.

4. Home purchase loans to African-American borrowers throughout the Las Vegas area.

- **African-Americans make up about 9 percent of Clark County's population but receive less than 3 percent of all home purchase loans.**
- **Valley and Primerit each made about 3 percent of their home purchase loans to blacks; First Interstate made only 1.6 percent of its loans to blacks.**

Clark County's black population has increased by about 50 percent since the 1980 census, and is now close to 70,000, or 9 percent of the county's total population.[10]

It is a population, as well, with substantial assets in real property. The 1990 census estimates the aggregate value of owner-occupied residential property owned by blacks in Clark County at $592.4 million.

Nonetheless, the aggregate record shows that only 308, or less than 3 percent, of the 10,658 home loans made in 1990 went to African-American borrowers (see Table 5, page 22 and Figure 3.1, page 27).

Of the dominant bank lenders, only Valley and Primerit exceeded the aggregate share of loans to blacks, and in neither case by very much: Valley made 3.5 percent of its home loans to blacks, and Primerit made 3.2 percent. Citibank, on the other hand, made only 2.6 percent of its loans to African-Americans, while First Interstate, at a mere 1.6 percent of all its home loans, was well below the aggregate pattern (see Table 5, page 22, and Figures 3.2–3.5, page 28).

In monetary terms, Citibank, with $2.6 million in loans to blacks ($1.8 million of which took the form of conventional home purchase mortgages to upper-income borrowers) was the only major lender to exceed the aggregate average of 2.7 percent of dollars loaned. Primerit matched the aggregate average, while Valley, at 2.4 percent ($2.2 million) was somewhat below it. First Interstate, which loaned only $754,000 to African-American borrowers, or 1.6 percent of its total lending, was well below the aggregate's already unimpressive benchmark.

5. The leading banks' market share of home purchase loans to African-American and white borrowers.

- **First Interstate's market share of loans to blacks is half its market share of loans to whites.**
- **Valley and Citibank have a slightly greater market share of loans to blacks than loans to whites, while Primerit's market shares are almost equal.**

Market share is a useful indicator of the outcome, over time, of the priorities banks establish and pursue. By breaking the HMDA data down into submarkets by race or income of applicants, and then comparing the shares obtained by competing lenders, we begin to glimpse the "culture" prevailing in the individual lending institutions. Market share, after all, is to a great extent the result of conscious and deliberate actions on the part of lenders. An institution that more effectively penetrates the market of white borrowers than black borrowers, for example, or upper income as against low- and moderate-income borrowers, does so most likely because it intends to.

While no major bank in Las Vegas originates a significant portion of its loans among black borrowers, and blacks in any case obtain relatively few of the home loans originated, there are market share variations among leading banks worthy of note (see Figure 4, page 29).

Valley leads the four top bank lenders with a 10 percent share of the 267 home purchase loans made to blacks. This is 20 percent above Valley's share of loans to whites, and suggests, at the least, the inclusion of blacks as a "customary" component of Valley's corporately-defined marketplace.

Primerit, with a somewhat smaller overall market share than Valley, has about the same share among both black and white borrowers. Citibank, smaller still than Primerit, has approximately 1 percent more of the market among blacks than whites, about the same proportion as Valley.

First Interstate, on the other hand, has half the market share among blacks as it does among whites. While First Interstate's market share among white borrowers is almost as great as Valley's, Valley's share among black borrowers is three times First Interstate's.

6. Home purchase loans to all neighborhoods with predominantly minority populations.

- **Of the 8,581 home purchase loans made by all lenders in Las Vegas, only 183 (2.1 percent) went to 15 Las Vegas census tracts with more than 50 percent minority residents.**
- **Eleven predominantly white census tracts (with less than 20 percent minority residents) each received more home purchase loans than the 15 predominantly minority tracts combined.**

In 1980, there were nine census tracts out of 89 in Clark County with 50 percent or more minority residents. Their total population was 35,971, or 7.8 percent of the county population.

By 1990, the number of predominantly minority census tracts had increased to fifteen (out of 120 tracts in Clark County), with a population of 69,003, or 9.3 percent of the total in the county.

These tracts also contain approximately 8.2 percent of the county's single family residences (see Table 6, page 22).

It is worth noting that no census tract that was more than 50 percent minority in 1980 has dropped out of the list. Among those are the tracts that comprise the Westside: 2.01, 3.01, 3.02, 35 and 37.

There has been, in other words, a tendency not only for predominantly minority tracts to remain so over time, but for the proportion of the area's population living in predominantly minority neighborhoods to increase over time, as well.

Indeed, data from the 1990 census indicate, while the county's minority population has now reached 182,000, or almost 25 percent of the total (see Figure 5), nearly 40 percent of this population lives in the 15 predominantly minority tracts listed in Table 6.

The containment and concentration of minorities in certain sections of the city is one of the consequences of the patterns of bank lending discussed in this Report.

In 1990, as Table 6 shows, Las Vegas lenders made a total of 183 home purchase loans to the 15 predominantly minority census tracts. These loans had an aggregate value of $9,954,000. The loans to these tracts constituted 2.1 percent of the total loans made in 1990, and just 1.2 percent of the total dollars loaned by all mortgage lenders.[11]

By way of contrast, Table 7 (page 23) lists eleven 1980 census tracts (and their 1990 equivalents) that each received more home purchase loans than the 15 predominantly minority tracts combined.

These census tracts, now subdivided into 31 tracts, represent areas of Las Vegas that expanded rapidly in the 1980's. They include communities to the east, south and west of the city. The minority population in most of these tracts is between 10 percent and 15 percent on average.

Individually, in 1990, these tracts had about four times the population of the 15 predominantly minority tracts, but received nearly 30 times more home purchase loans (5,364 to 183), and 56 times the number of home purchase dollars ($557,194,000 to $9,954,000).

7. Home purchase loans in low- and moderate-income neighborhoods.

- **Only 6.8 percent of the 8,581 home purchase loans in 1990 went to low- and moderate-income areas of Las Vegas.**
- **Primerit and Citibank made 10.6 percent and 8.5 percent, respectively, of their home purchase loans to low- and moderate-income neighborhoods, exceeding the aggregate distribution. Valley, at 6.7 percent, matched the aggregate.**
- **First Interstate made only 2.7 percent of its 563 home purchase loans in low- and moderate-income neighborhoods.**
- **Upper-income neighborhoods received more than 57 percent of the $811 million allocated for home purchase loans by all lenders in Las Vegas.**

Financial institutions are required under the CRA to serve "the convenience and needs of the communities in which they are chartered to do business." Meeting the credit needs of low- and moderate-income neighborhoods in these communities is one of the criteria on which financial institutions are evaluated when applying for deposit insurance, a branch or deposit facility, a merger or acquisition, and other regulated activities. Low- and moderate-income neighborhoods, for HMDA reporting purposes, are those census tracts with a median family income below 80 percent of the area median.

In 1980, when the Las Vegas area median family income was $21,056, there were 27 tracts that met the low- and moderate-income definition. At that time, these tracts had a population of 117,934, or about 25 percent of the total population of the county. For 1990 HMDA reporting purposes, these tracts continue to define the universe of low- and moderate-income neighborhoods in Las Vegas.[12]

Of the 8,581 home purchase loans made in Las Vegas in 1990, only 6.8 percent went to low- and moderate-income neighborhoods (see Figure 6, page 31).

Among the leading bank lenders, Primerit made 10.6 percent of its loans in these neighborhoods, Citibank made 8.5 percent, and Valley effectively matched the area aggregate at 6.7 percent (see Figure 6). Only First Interstate fell below the aggregate, making just 2.7 percent of its 563 home purchase loans to low- and moderate-income neighborhoods.

By way of contrast, upper income neighborhoods received 53.1 percent of all home purchase loans, and 57 percent of the $811 million conveyed by those loans. Valley once again matched the area aggregate, making 53.1 percent of its loans to upper income areas. Primerit, too, was close to the area aggregate, at 54.0 percent, while Citibank was slightly above, at 58.7 percent.

First Interstate made a remarkable 83.3 percent of all its home purchase loans in upper income neighborhoods, *31 times greater* than its loans to low- and moderate-income neighborhoods.

8. The leading banks' market share of home purchase loans in low- and moderate-income neighborhoods.

- **Valley came close to having equal market shares, at about 8 percent, in all three HMDA income categories.**
- **Primerit had a 50 percent greater share of the low- and moderate-income market than it had of the upper income market.**
- **First Interstate's share of the upper income market, at about 10 percent, was not only the largest among the four leading bank lenders, but was also four times larger than its share of the low- and moderate-income market.**

As discussed in Section 5, above, market share in a competitive arena reflects the cumulative results of a bank's policies, objectives, products and financial commitments. It is not something that can be changed overnight or by directive. Thus it is a fairly discriminating indicator, in HMDA terms, of an institution's more durable priorities.

Of the four leading bank lenders in Las Vegas, Valley's market share of home purchase loans, by income of tract, was most consistent, at between 8 percent and 9 percent in each of the three income categories (see Figure 7, page 32). Citibank, with a somewhat smaller overall share of home purchase loans than Valley, had a slightly greater penetration of the market for loans to low- and moderate-income tracts than to middle and upper income tracts.

Primerit, as is often the case with S&Ls, whose commitment to home mortgage lending predates the aggressive entry of commercial banks into the market, has about a 50 percent greater market share in low- and moderate-income tracts than in middle and upper income tracts.

First Interstate, among the leading bank lenders, has the smallest share of the low- and moderate-income market (less than 3 percent), and the largest share (about 10 percent) of the upper-income market. The latter share is due in large measure to some 375 home purchase loans in just one census tract (1980 tract 32; 1990 tract 32.02, the Sun City development), a clear reflection of a major commitment by the bank to capture a specific market. The bank's small share of loans to the low- and moderate-income market reflects the opposite: little or no commitment to penetrate a market that is clearly underserved.

D. Conclusions

The Home Mortgage Disclosure Act data, which is the basis for this report, has been described as "the major vehicle for monitoring the results of an institution's [Community Reinvestment Act] efforts." [13] It is the only data banks are required to make public that objectively reflects the underlying principles on which the institutions base their operations, including their credit extensions. Nothing comparable is disclosed regarding consumer loans (other than home improvement loans), commercial or business loans, investments, or other uses of depositors' federally insured funds.

Our examination of the aggregate HMDA record of lenders in Las Vegas, and of four leading individual lenders, shows an entrenched and consistent set of patterns. Among them are the following:

- Minority and low- and moderate-income communities generate substantial cash flows into lending institutions, yet receive disproportionately little in the way of reinvestment.
- Minority borrowers, regardless of their income, are denied loans more often than white borrowers, in some cases four or five times more often.
- Lenders compete aggressively for market share in predominantly white, upper income communities, but generally do not compete at all for market share in minority and low- and moderate-income communities.

The 1990 HMDA data confirm that financial institutions in Las Vegas, as in other cities of the United States, continue to play the lending game by rules they write themselves.

The consequences of this one-sided practice are extensive and not quickly remedied. Urban riots and attacks on property are but a signal of what happens when entire communities are kept under a financial chokehold.

The Las Vegas Alliance for Fair Banking will work with other groups and individuals in Las Vegas, as well as with the financial institutions that operate here, to address the patterns of inequity and discrimination reflected in this report.

E. Recommendations

The Las Vegas Alliance for Fair Banking makes the following recommendations:

- The appropriate regulatory agencies should investigate every Nevada financial institution with disproportionate denial rates between white and minority applicants.
- The Federal Reserve should not approve any application subject to CRA involving financial institutions with disproportionate denial rates between white and minority applicants until the institutions demonstrate to the satisfaction of regulators and the communities in which they operate that they have taken steps to correct such disparities.
- Regulatory agencies must take lending patterns in low- and moderate-income communities more fully into account in CRA evaluations. Financial institutions that show a clear preference for lending to upper income, predominantly white communities and applicants should not qualify for "Outstanding" or "Satisfactory" CRA ratings.
- State and local governments should develop legislation, after suitable review of policies in place in other communities around the country, to require banks to demonstrate a high standard of community reinvestment in order to qualify as depositories for public monies.

NOTES

1. The trade names and marks used in Figure 1 are owned by Citibank, First Interstate Bank, Primerit Bank, and Valley Bank.

2. The details cited here are from Eugene P. Moehring, *Resort City in the Sunbelt: Las Vegas 1930–1970* (Reno & Las Vegas), 1989, pp. 176–179 and 185. First National Bank later became First Interstate Bank. Moehring's chapter, "Civil Rights in a Resort City," examines the history of the Westside with considerable attention to housing and living conditions.

3. In the context of its acquisitions of Valley Bank and Security Pacific Bank, and following negotiations with the Southern Nevada Reinvestment and Affordable Housing Committee, Bank of America plans to open a branch in the Westside in 1992. *Las Vegas Sun*, November 20, 1991.

4. Data on branch deposits of First Interstate Bank and Valley Bank are from the FDIC's *Operating Banks and Branches Data Book*, v.6, and reflect deposits as of June 30, 1990. Data on branch deposits of Primerit Bank are from the Office of Thrift Supervision's *Survey of Branch Deposits*, as of June 30, 1990.

5. ACORN, "Take the Money and Run: The Siphoning of Deposits from Minority Neighborhoods in 14 Cities," Washington, DC, June 4, 1992. See also Paulette Thomas, "Minority-Area Lenders Faulted in Acorn Study," *The Wall Street Journal*, June 5, 1992, A2. A comparable examination of the ratio of deposits to lending in Las Vegas for First Interstate, Valley, and Citibank produces much greater disparities. Using total deposits reported for all Clark County branches, and the dollar value of all home loans made in tracts with less than 20 percent minority population and tracts with more than 50 percent minority, the following ratios result:

DEPOSIT TO LOAN RATIOS—LAS VEGAS/CLARK COUNTY

	Citibank	First Interstate	Valley
Total Deposits Clark County ($'000)	906,383	1,613,322	1,614,380
Loans to White Neighborhoods ($,000)	69,426	60,483	75,928
Amount Loaned per Dollar of Deposits	8 CENTS	4 CENTS	5 CENTS
Loans to Minority Neighborhoods ($,000)	131	176	771
Amount Loaned per Dollar of Deposits	.01 CENT	.01 CENT	.04 CENT

6. Summaries of the application denial patterns may be found in several articles by Paulette Thomas in *The Wall Street Journal:* "Mortgage Rejection Rate for Minorities Is Quadruple That of Whites, Study Finds," October 21, 1991, A2; "U.S. Examiners Will Scrutinize Banks With Poor Minority-Lending Histories," October 22, 1991, A2; "Federal Data Detail Pervasive Racial Gap In Mortgage Lending," March 31, 1992, A1.

7. "U.S. Probing Banks' Records For Race Bias," *The Wall Street Journal*, May 19, 1992, A2. First Interstate Bank was the only Nevada institution under OCC supervision identified by *The Journal* as a potential target for investigation. See also Bill Atkinson, "250 Banks Probed for Race Bias in Lending," American Banker, May 14, 1992, 1; Paulette Thomas, "U.S. Intensifies Its Investigation Of Lending Bias," *The Wall Street Journal*, May 15, 1992, A3; and Phil Roosevelt, "Banks Face Long Heat Wave over Loan Bias," *American Banker*, June 5, 1992, 1.

8. For 1990 HMDA reporting purposes, the median family income for the Las Vegas MSA was $34,582 (data provided by the Federal Financial Institutions Examination Council). This was an adjustment upward by a factor of 1.6424 from the 1980 median family income of $21,056. The applicant income categories for 1990 HMDA purposes, therefore, were as follows:

—Low- and moderate-income (< 80 percent median): $27,665 or less
—Middle income (80 percent–120 percent median): $27,665 to $41,500
—Upper income (> 120 percent median): $41,500 or more

9. Valley Bank published a correction notice to its 1990 HMDA data stating that an additional 30 loans were declined by the bank (not the mortgage company) that were not originally reported. The breakdown of the additional denials by gender, race, or income was not available.

10. The 1990 census category of "Hispanic origin" includes persons of different ethnicity, including whites and blacks. For purposes of this section, and later discussions of demography, references to "white," "black" and other ethnicities apply to persons not of Hispanic origin.

11. In 1980, tract 36 was classified for HMDA purposes as more than 80 percent minority. By 1990, tract 36 had been divided into 36.02, the southern portion, and tract 36.01, the northern portion. Tract 36.02 remains a predominantly minority tract (96 percent); tract 36.01, on the other hand, is not (23 percent minority). Aggregate and individual institution HMDA data for 1990 reports loans to tract 36 as if it were still a high-minority tract, when it is reasonable to assume that most if not all loans reported were actually made in the section that is now 36.01. To avoid skewing the data in this report, we either exclude tract 36 or count no loans there. We will gladly adjust the calculations if any lender provides evidence that loans reported for 1980 tract 36 were made in the section that is now 36.02.

12. The 1990 census data on income are only now being made available. Thus, changes in median tract income over the 1980–1990 period will not be reflected in HMDA categories until the release of 1992 HMDA reports, in the latter part of 1993. Applicant income, on the other hand, as described in Note 8 above, has been adjusted to 1990 levels.

13. Fannie Mae, "Investing in Your Community," Washington, DC, 1990, p. 5.

TABLE 1.
HOME LOANS IN LAS VEGAS, 1990. ALL LENDERS.

TYPES OF LOANS	*# OF LOANS*	*$ (MILLIONS)*
Home Purchase		
FHA, FmHA, VA	3333	279.0
Conventional	5248	532.0
Refinance	653	73.5
Home Improvement	1424	37.7
TOTAL	10658	922.2

TABLE 2.
TOP MORTGAGE LENDERS IN LAS VEGAS, 1990

LENDER	*# OF LOANS*	*MKT SHARE (%)*	*$ (MILLIONS)*
Weyerhaeuser Mtg Co	1907	17.9%	192.7
Citibank NV	1020	9.6%	73.0
Valley Bank/Valley Mtg Co	908	8.5%	91.9
First Interstate Bank NV	754	7.1%	62.2
Primerit Bank	689	6.5%	61.7
Margaretten & Co	674	6.3%	65.6
TOTAL	5952	55.8%	547.1

TABLE 3.
LOANS TO THE WESTSIDE, 1990. ALL LENDERS AND FOUR LEADING BANKS.

		AGGREGATE		CITIBANK		FIRST INTERSTATE		PRIMERIT		VALLEY	
TRACT	% BLACK	LOANS	$('000)	LOANS	$('000)	LOANS	$('000)	LOANS	$('000)	LOANS	$('000)
37	96	12	738	0	0	1	32	1	63	3	114
3.02	91	6	301	0	0	0	0	0	0	3	188
35	88	9	520	1	38	0	0	0	0	1	62
3.01	88	10	381	2	76	0	0	0	0	1	10
2.01	62	22	1135	0	0	2	27	2	51	4	190
WESTSIDE TOTAL		59	3075	3	114	3	59	3	114	12	564
AGGREGATE/BANK TOTAL		10658	922114	1020	72988	754	62220	689	61762	908	91898
WESTSIDE AS % OF TOTAL		0.6%	0.3%	0.3%	0.2%	0.4%	0.1%	0.4%	0.2%	1.3%	0.6%

Note: Population percentage based on 1990 census.

TABLE 4.
BRANCH DEPOSITS AND HOME LOANS - FIRST INTERSTATE BANK AND VALLEY BANK
THE WESTSIDE AND WESTERN TRACT 30.02

BANK & BRANCH	*BRANCH DEPOSITS $('000)*	*BANK LOANS IN AREA #*	*BANK LOANS IN AREA $ ('000)*
NEAR THE WESTSIDE			
FIRST INTERSTATE BANK		3	59
Twin Lakes	38,125		
North Las Vegas	56,021		
VALLEY BANK		12	564
Rancho Lane	50,130		
North Las Vegas	46,365		
PRIMERIT BANK		3	114
North Las Vegas	15,249		
NEAR TRACT 30.02			
FIRST INTERSTATE BANK		23	1,172
Rainbow-Westcliff	57,671		
VALLEY BANK		17	925
Rainbow-Westcliff	31,557		
PRIMERIT BANK		13	1,693
Rainbow	28,461		

SOURCE: FDIC, Operating Banks and Branches Data Book, 6/30/90; 1990 HMDA Reports; OTS, Survey of Branch Deposits, 6/30/90

TABLE 5.
APPLICATIONS FROM BLACKS AND LOANS TO BLACKS - LAS VEGAS 1990
ALL LENDERS AND FOUR LEADING BANKS

	ALL LENDERS	CITIBANK	FIRST INTERSTATE	PRIMERIT	VALLEY
ALL APPLICANTS	16960	1433	1004	1226	963
BLACK APPLICANTS	569	48	26	48	34
% BLACK APPLICANTS	3.4%	3.3%	2.6%	3.9%	3.5%
ALL LOANS	10658	1020	754	689	906
LOANS TO BLACKS	308	27	12	22	32
% LOANS TO BLACKS	2.9%	2.6%	1.6%	3.2%	3.5%

TABLE 6.
HOME PURCHASE LOANS TO TRACTS WITH MORE THAN 50% MINORITY POPULATION
RANKED BY % MINORITY
LAS VEGAS - 1990

TRACT	POP'N	% MIN	% BLACK	% HISP	HOUSING UNITS	LOANS #	LOANS $ ('000)
37	3223	97	96	2	996	9	503
36.02	3992	96	95	1	1155	0	0
3.02	4193	94	91	4	1619	5	266
35	2458	93	88	6	809	8	510
3.01	3452	90	88	5	1450	8	349
38	3865	75	39	36	1385	21	937
2.01	2878	71	62	9	1209	16	1024
46	6023	66	51	12	2032	12	539
44	5612	66	41	23	1821	22	1111
43	5637	66	18	45	1955	18	1167
5.04	6304	65	20	40	2529	9	347
11	4867	62	7	49	2452	2	250
45	4134	59	31	23	1253	15	775
5.03	5478	51	8	38	2240	25	1305
4	6887	50	12	32	3263	13	851
TOTAL	69003				26168	183	9954
% TOTAL	9.3%				8.2%	2.1%	1.2%

SOURCE: 1990 Census; 1990 HMDA Report Las Vegas Aggregate

TABLE 7.
TRACTS RECEIVING MORE HOME PURCHASE LOANS IN 1990
THAN ALL PREDOMINANTLY MINORITY TRACTS COMBINED

1980 TRACT	*1990 TRACTS*	*TOTAL HP LOANS #*	*TOTAL HP LOANS $ ('000)*	*POP'N 1990*	*AVG % MIN*	*NON-HISP WHITE POP'N*
55	Tract 55.01-.02-.03-.04	199	18392	12567	5.8%	11840
29.02	Tract 29.08-.09-.11-.12	215	15584	22311	16.8%	18560
49	Tract 49.01-.02-.03	242	19193	26394	22.0%	20594
29.01	Tract 29.05-.07	249	31060	13030	13.2%	11307
36	Tract 36.01-.02*	290	37782	2736	22.7%	2114
29.04	Tract 29.06-.10	344	49915	16934	13.7%	14615
58	Tract 58.01-.02	464	54007	21095	16.3%	17650
34.02	Tract 34.03-.04-.05-.06-.07	505	47387	41129	15.4%	34804
28.02	Tract 28.03-.04	512	49049	12123	12.2%	10640
53	Tract 53.01-.02	618	62002	18977	10.7%	16947
51	Tract 51	725	74169	19373	11.9%	17061
32	Tract 32.01-.02	1001	98654	13626	10.3%	12221
	TOTAL	5364	557194	220295	14.5%	188353

* See Note 11 in text for treatment of Tracts 36.01 and 36.02

LAS VEGAS — REDLINING THE WESTSIDE

First Interstate Bank

Number of purchase, refinance and home improvement loans:
754

Number of loans to Westside:
3 (0.4%)

Value of purchase, refinance and home improvement loans:
$62,200,000

Value of loans to Westside:
$59,000 (0.09%)

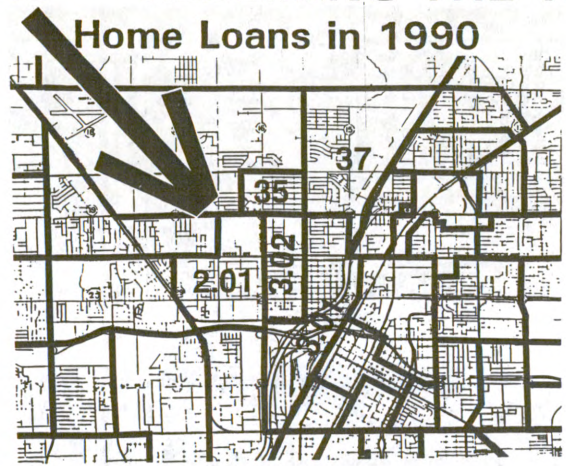
CITIBANK

Number of purchase, refinance and home improvement loans:
1020

Number of loans to Westside:
3 (0.3%)

Value of home purchase, refinance and home improvement loans:
$73,000,000

Value of loans to Westside:
$114,000 (0.2%)



10,658 home loans in Las Vegas
59 to the Westside

$922,100,000 worth of loans in Las Vegas
$3,100,000 to the Westside

Valley Bank of Nevada

Number of purchase, refinance and home improvement loans:
908

Number of loans to Westside:
12 (1.3%)

Value of purchase, refinance and home improvement loans:
$91,900,000

Value of loans to Westside:
$564,000 (0.6%)

PRIMERIT BANK

Number of purchase, refinance and home improvement loans:
689

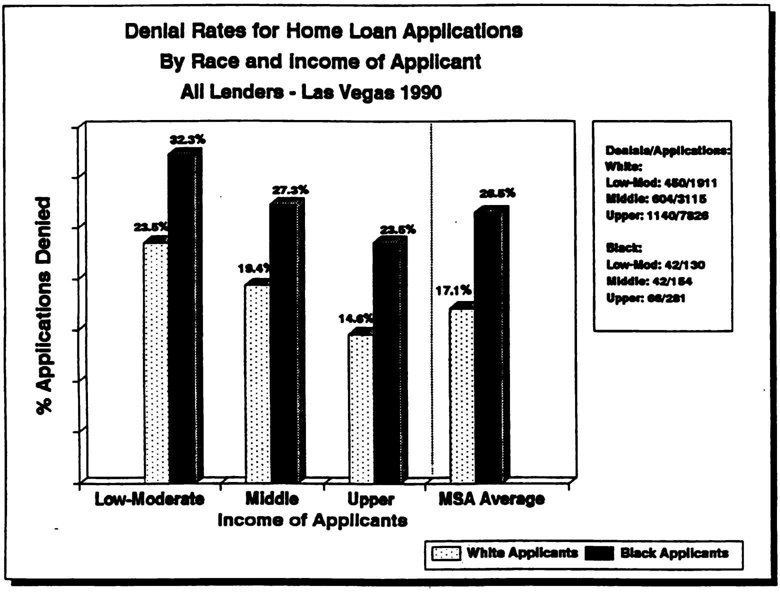
Number of loans to Westside:
3 (0.4%)

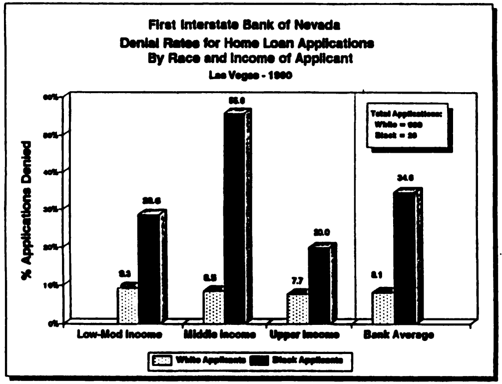
Value of purchase, refinance and home improvement loans:
$61,800,000

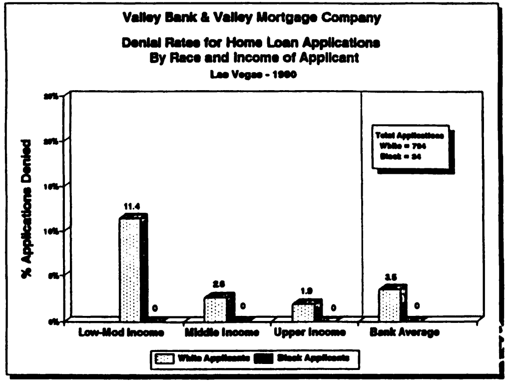
Value of loans to Westside:
$114,000 (0.2%)

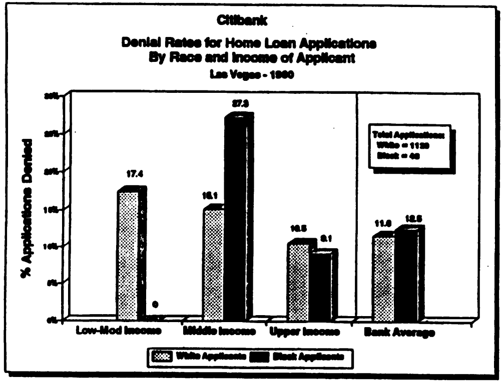
Figure 1

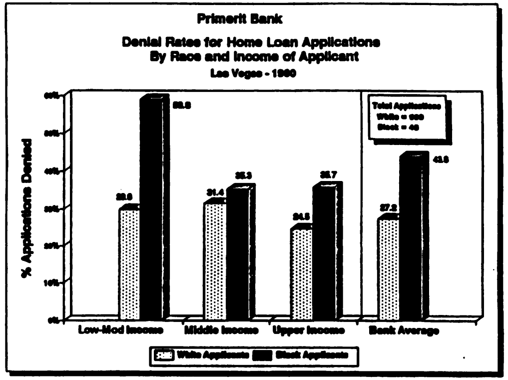
Figure 2.1


Denial Rates for Home Loan Applications
By Race and Income of Applicant
All Lenders - Las Vegas 1990
% Applications Denied
23.5%
32.3%
19.4%
27.3%
14.6%
23.5%
17.1%
28.5%
Low-Moderate
Middle
Upper
MSA Average
Income of Applicants
Denials/Applications:
White:
Low-Mod: 450/1911
Middle: 604/3115
Upper: 1140/7826
Black:
Low-Mod: 42/130
Middle: 42/154
Upper: 66/281
White Applicants
Black Applicants



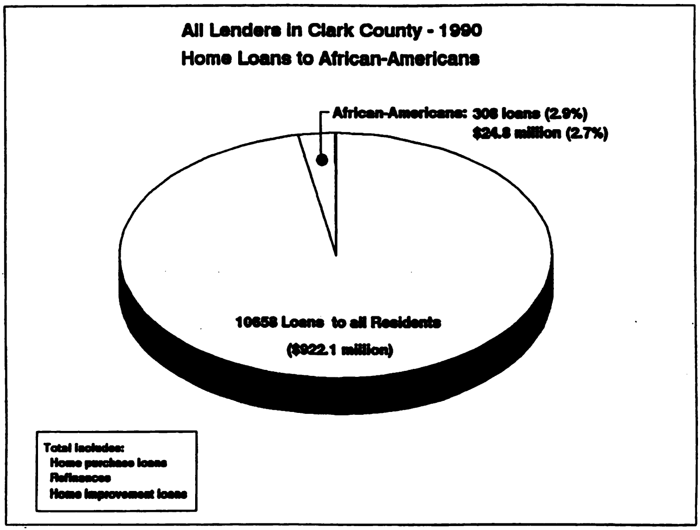


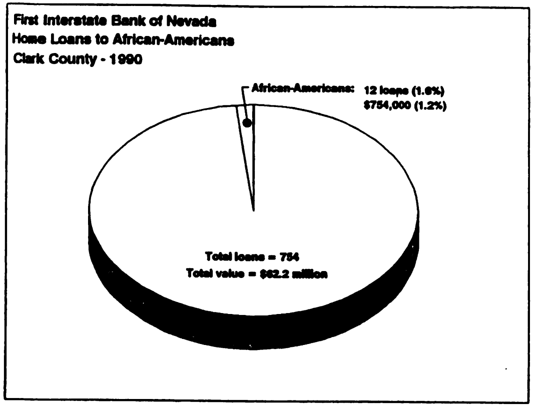


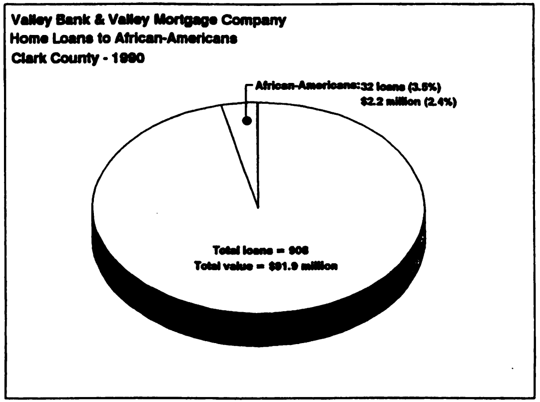


Figures 2.2-2.5

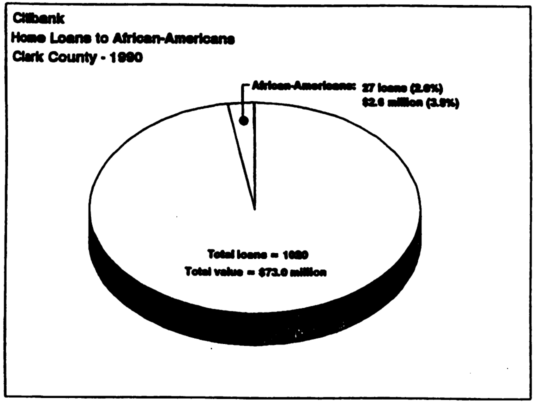
Figure 3.1

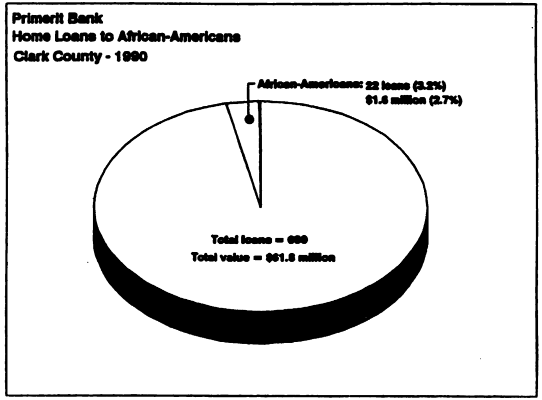

All Lenders in Clark County - 1990
Home Loans to African-Americans
African-Americans: 308 loans (2.9%)
$24.8 million (2.7%)
10658 Loans to all Residents
($922.1 million)
Total includes:
Home purchase loans
Refinances
Home improvement loans





28





Figures 3.2-3.5

Figure 4

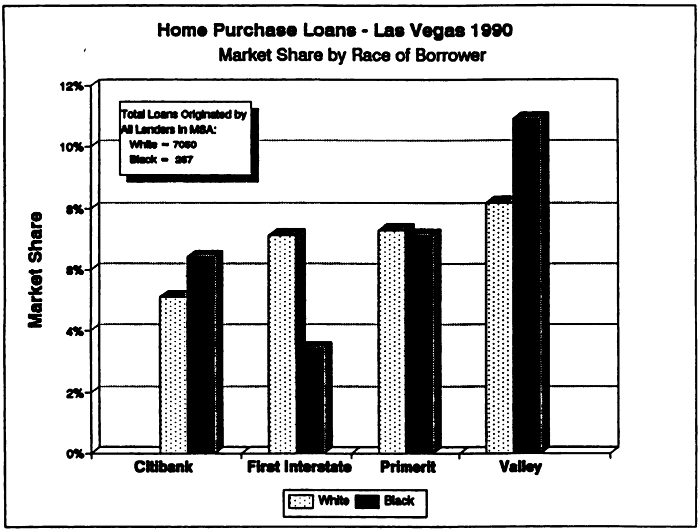

Home Purchase Loans - Las Vegas 1990
Market Share by Race of Borrower
Total Loans Originated by All Lenders in MSA:
White = 7060
Black = 267
Market Share
12%
10%
8%
6%
4%
2%
0%
Citibank
First Interstate
Primerit
Valley
White
Black

Figure 5

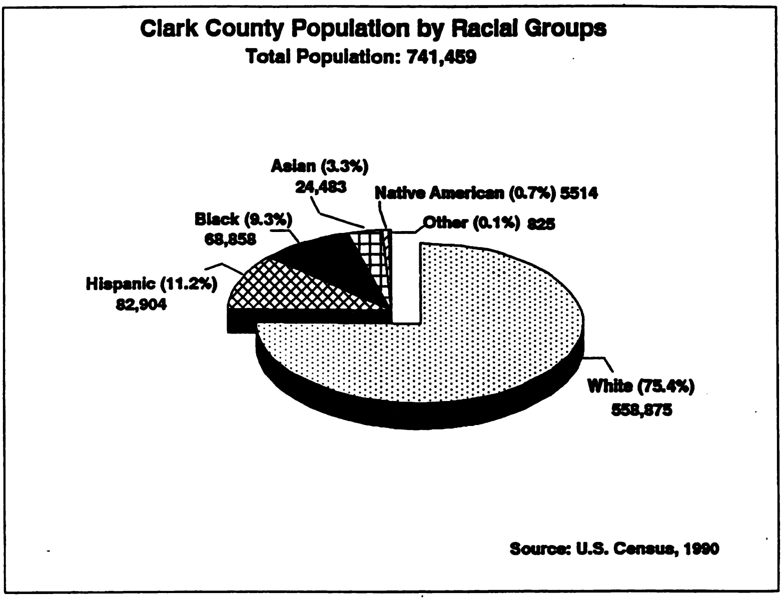

Clark County Population by Racial Groups
Total Population: 741,459
Asian (3.3%)
24,483
Native American (0.7%) 5514
Black (9.3%)
68,858
Other (0.1%) 825
Hispanic (11.2%)
82,904
White (75.4%)
558,875
Source: U.S. Census, 1990

Figure 6

All Lenders and Leading Banks

Distribution of Home Purchase Loans

By Income of Tract

Las Vegas - 1990

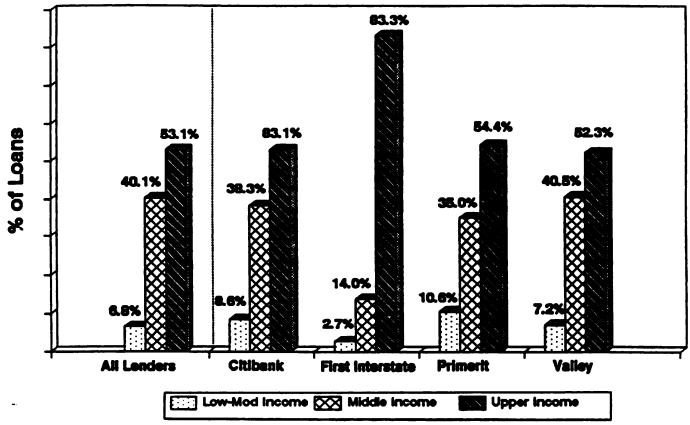
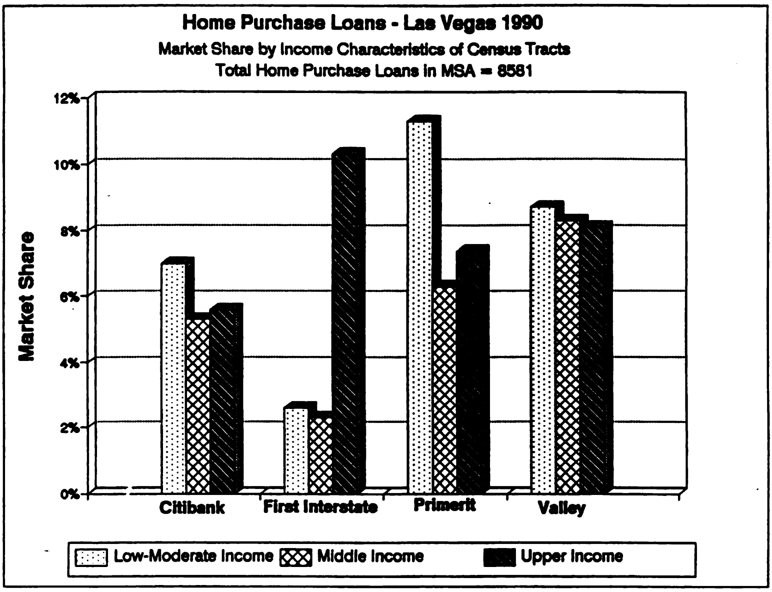


Figure 7


Home Purchase Loans - Las Vegas 1990
Market Share by Income Characteristics of Census Tracts
Total Home Purchase Loans in MSA = 8581
Market Share
12%
10%
8%
6%
4%
2%
0%
Citibank
First Interstate
Primerit
Valley
Low-Moderate Income
Middle Income
Upper Income

The Comptroller's letters of inquiry note specifically that the government isn't presuming that racial discrimination is behind the lending patterns it is scrutinizing. And bankers are quick to note that the Federal Reserve's mortgage data doesn't take into account credit history or debt load.

Nonetheless, government examiners are using the data to help them investigate whether banks are lending to all areas where they accept deposits, as is required under law. If the banks don't comply with that law, they can be barred from mergers or opening new branches. Indeed, Federal Reserve approval of the several big bank mergers last year was made contingent upon an increase in lending to low-income neighborhoods. The government may also refer lenders to the Justice Department for prosecution, as it has in two cases in the past year.

In response to this new federal interest, banks across the country are re-examining their lending records, and many are aggressively promoting lending in low-income areas. Many also are offering credit counseling programs through local community groups and churches. Others have altered their loan approval standards, allowing, for instance, rent payments to be examined for credit history for a borrower who never had a credit card.

"I think the image is getting around that banks are totally thumbing their noses at this data, and that is not totally true," says John Popovich, senior vice president for public affairs at First Interstate of California, a sister unit of one of the targeted banks.

Many banks contend that the record compiled as part of last year's Federal Reserve study distorts the true lending picture. Most importantly, it doesn't include a borrower's credit history, the No. 1 reason for loan rejections, banks say. "The only criterion we apply in making credit-granting decisions is the credit-worthiness of individual borrowers," said Jim Lestelle, a spokesman for Hibernia. "That would be the reason for the difference in those figures."

Credit Standards

Other institutions, such as Merchants National Bank and Premier Bancorp, say that they are additionally restrained by the requirements of the secondary markets, such as Fannie Mae and Freddie Mac, that buy the mortgages they originate. "The standards we use are the credit standards required in the national marketplace to sell mortgage paper," said Lee Griffin, chairman and chief executive officer of Premier.

Ironically, a high rate of rejections of minority applicants may also result from aggressive marketing to low-income neighborhoods. "We've made six times as many [of these] loans as any other financial institution in our community," said Norman J. Tice, executive vice president of Boatmen's National Bank of St. Louis, which didn't indicate whether it was under scrutiny by the Comptroller. If a bank seeks to make low-income loans in volume, "you'll just get more turndowns," he said.

Similarly, a spokeswoman for Deposit Guaranty National Bank said that when the Federal Reserve study was being conducted in 1990, the bank was promoting mortgages with below-market rates and easier qualifying standards, and made about $25 million in loans to low-income applicants. "We don't pre-screen, we welcome everyone in," said a spokeswoman. "The law of averages says a high number will be turned down."

'Credibility Gap'

The government is also spotlighting lenders who may have unremarkable approval rates, but a low number of minority applicants, which can indicate pre-screening – that is, turning away borrowers before they can even apply. But some of the banks being targeted say that they simply have few minorities in their customer areas. At Los Alamos National Bank, for example, an official said that because his customer population is 95% white, he believes his bank in fact is doing a good job of making loans to credit-worthy minorities.

At NationsBank Corp., one official said the bank had suffered a "credibility gap" with minorities. Although 13% to 14% of its applicants are minorities, the bank finds that unacceptably low because "we serve markets [with] three times those numbers of minorities," said Cathy Bessant, senior vice president. She said she was unaware of any current government scrutiny of the bank's lending record. NationsBank said that the Comptroller's office looked closely at its lending records last year, when it merged NCNB Corp. with C&S/Sovran Corp. NationsBank has earmarked $10 billion for low-income lending over the next 10 years.

It remains to be seen what the Comptroller will do with the data. Last week, officials from the Comptroller's office noted that it is difficult to prove "subtle discrimination" in lending. Two years ago, the Office of Thrift Supervision conducted a similar targeted study of some Georgia institutions following a series of stories by the Atlanta Journal and Constitution about discrimination in lending, but little regulatory action followed. "We found some things that made us raise questions with management," an OTS official said, "but nothing we considered real evidence of discrimination."

TUESDAY, MAY 19, 1992

U.S. Probing Banks' Records For Race Bias

Group of Lenders Confirms Scrutiny of High Level Of Minority Rejections

A WALL STREET JOURNAL *News Roundup*

More than a dozen banks confirmed that their lending records, which show far higher rejections for minorities than for whites of similar income, have been targeted by the government for scrutiny.

Nearly all the banks, including such superregional bank holding companies as **Banc One Corp.** of Columbus, Ohio; **Hibernia Corp.** of New Orleans; and **First City Bancorp. of Texas Inc.**, were asked early last month by the Comptroller of the Currency to explain the big racial disparities in their 1990 mortgage lending records. At least one other large lender, First Interstate Bank of Texas, was informed within the past six months, said a spokesman for the bank's parent, **First Interstate Bancorp.** Some of the banks said they have been told to respond to the government inquiry by Friday.

The mortgage industry is under unprecedented pressure to narrow the racial gap in lending, following a Federal Reserve Board study last fall that showed that blacks are more than twice as likely to be rejected for mortgages as are whites of similar income. Recently, the Comptroller's office said it targeted 266 banks that it supervises for further investigation; it didn't identify those banks. Most of the banks are being reviewed because of apparent disparities in their lending patterns, while a few dozen others are being looked at because minorities represented fewer than 1% of applicants.

"We are not taking this thing lightly," said James Hunter, senior vice president of **First National Bank, Orangeburg, S.C.**, one of the banks being targeted. The bank has already submitted its inch-thick analysis to the Comptroller's office, he said.

Others who confirmed that their lending records are being examined are: **Merchants National Bank, Vicksburg, Miss.**; **Riverside National Bank of Florida**, Fort Pierce; Deposit Guaranty National Bank, Jackson, Miss.; **Premier Bancorp Inc.**, Baton Rouge, La.; **Los Alamos National Bank**, New Mexico; **National Republic Bank of Chicago**; and Gainer Bank, Gary, Ind.

Banks With Lending Disparities

Listed below are banks and mortgage companies where the rejection rate for black and Hispanic mortgage applicants was more than twice that for whites in 1990.

The list covers only lenders under the supervision of the Office of the Comptroller of the Currency, which has said it is focusing special scrutiny on lenders whose minority rejection rate is double that for white applicants.

This state-by-state list was compiled by The Wall Street Journal from 1990 data collected on computer tape by the Federal Reserve under the provisions of the Home Mortgage Disclosure Act of 1989. The list excludes applications that were incomplete or subsequently withdrawn, those where race or gender weren't provided to the Fed, or those that didn't seek a mortgage on a one- to four-family home. As a result, the list may differ from the roster of lenders that federal regulators developed for their inquiry.

The numbers after the names of certain lenders indicate the following:

(1) Confirmed it has been contacted by regulators.

(2) Disputed the data compiled by the Journal.

(3) Declined to comment on whether its lending record is being reviewed by regulators, or couldn't be reached for comment.

(4) Attributed its disparity to an aggressive effort to attract minority applicants.

Alaska
- National Bank of Alaska (3)

Alabama
- AmSouth Mortgage Co. (3)
- Southtrust Mortgage Corp. (3)
- AmSouth Bank (3)

Arizona
- First Interstate Bank (3)
- Valley National Bank

Arkansas
- One National Mortgage Co.
- Simmons First Natl. Bank
- Worthen Mortgage Co.
- National Bank of Commerce
- Union Modern Mortgage Corp.

California
- Mineral King National Bank

Florida
- Barnett Bank Jacksonville (3)
- Citizens & Southern Natl. Bank
- Riverside National Bank (1)
- Sun First National Bank
- Barnett Bank of Manatee Co. (3)
- Barnett Bank of South Fla. (3)
- First Union Natl. Bank of Fla.
- BancBoston Mortgage Corp.
- Barnett Bank Central Fla. (3)

Georgia
- Wachovia Bank of Georgia
- C&S Real Estate Services Inc.
- C&S National Bank
- Trust Co Bank of South Georgia
- First South Bank

Idaho
- First Security Bank of Idaho

Illinois
- Natl. Republic Bank of Chicago (1,2)
- First Natl. Bank of Chicago

Indiana
- Gainer Bank (1,2)

Kentucky
- Liberty National Bank & Trust
- First National Bank Louisville
- Bank One, Lexington (1)

Louisiana
- City National Bank
- Calcasieu Marine Natl. Bank
- Premier Mortgage Co. (1)
- Hibernia National Bank (1)
- First Natl. Bank of Commerce

Maryland
- First National Bank

Massachusetts
- Bank of New England

Michigan
- First of America Bank-Southeast (2)
- Manufacturers National Bank
- Independence One Mortgage (3)

Mississippi
- Merchants National Bank (1)
- First National Bank of Vicksburg
- Deposit Guaranty Mortgage Co. (1,4)
- Trustmark National Bank

Missouri
- Mercantile Bank of St. Louis
- Boatmens Natl. Bank of St. Louis (4)

New Jersey
- Chemical Bank New Jersey (2)
- CoreStates New Jersey Natl. Bank
- United Jersey Bank/Central (4)

New Mexico
- Los Alamos National Bank (1,2)
- First National Bank Albuquerque

New York
- Chase Lincoln First Bank (2)

Nevada
- First Interstate Bank of Nevada (3)

North Carolina
- First Union Natl. Bank (2)
- Wachovia Bank of N.C. (2)
- Southern National Bank
- NCNB Natl. Bank
- Firstier Bank
- First National Bank of Omaha

Ohio
- Central Trust Co. Cincinnati
- National City Bank Akron (3,4)
- First National Bank Dayton (3,4)
- AmeriTrust Co.Cleveland
- Mid-American National Bank
- Bank One Cleveland (1)
- Society National Bank (4)

Oklahoma
- BancOklahoma Mortgage Corp.

Oregon
- First Interstate Bank Oregon (3)

Pennsylvania
- Commonwealth Natl. Bank (2)
- Mellon Bank
- Provident Natl. Bank Bryn Mawr (4)

Rhode Island
- BancNewEngland Mortgage Co.
- Fleet National Bank

South Carolina
- Citizens & Southern Natl. Bank
- South Carolina Natl. Bank
- National Bank of S.C. (3)
- First National Bank (1)

Tennessee
- National Bank of Commerce
- First American National Bank (4)
- American National Bank & Trust
- First Tennessee Bank
- First City National Bank
- Union Planters National Bank

Texas
- First National Bank
- NCNB Texas National Bank
- First City Texas-Houston (1,2)
- NCNB Mortgage Corp.
- Bank One Texas (1)
- Lone Star Natl. Bank
- First City Texas Beaumont
- First National Bank of Texas
- Frost National Bank
- Texas Commerce Mortgage Co.
- Amarillo National Bank
- Bank One Mortgage Co. (1)
- NCNB Texas Mortgage Corp.
- Harlingen National Bank
- Western Natl. Bank of Amarillo
- First Interstate Bank of Texas (1)

Utah
- First Security Bank of Utah

Virginia
- Dominion Bankshares Mortgage Corp
- Jefferson National Bank

Washington
- First Interstate Bank Wash. (3)
- Security Pacific Bank Wash.

The Wall Street Journal
May 19, 1992, A2

TESTIMONY OF MICHELLE C. WHITE, EXECUTIVE DIRECTOR, FAIR HOUSING CONGRESS OF SOUTHERN CALIFORNIA REGARDING COMMUNITY REINVESTMENT ACTIVITIES, REGULATORY SUPERVISION AND PAPERWORK RAMIFICATIONS OF REPORTING REQUIREMENTS RELATED TO THE FAIR HOUSING, EQUAL CREDIT OPPORTUNITY AND COMMUNITY REINVESTMENT ACTS

Thank you for this opportunity to comment on the respective values of activities under the Community Reinvestment Act, regulatory responses to bank activities and the reporting produced pursuant to the Home Mortgage Disclosure Act [HMDA] and Community Reinvestment Act [CRA]. The Fair Housing Congress of Southern California ["The Congress"], presents this testimony from the prospective of a non-profit fair housing enforcement agency responsible for investigating complaints under the California and Federal fair housing and fair lending laws. The Congress is also responsible for advocating under the Community Reinvestment Act on behalf of persons affected by illegal forms of discrimination. The Congress is a member of a number of local, regional and national agencies which advocate for the effectiveness enforcement of said laws. Among the organizations which the Congress is a member are: 1) Communities for Accountable Reinvestment [CAR], a Southern California multi-racial and multi-ethnic coalition of advocates promoting the banking, housing and economic development interests of low- and moderate-communities in Los Angeles, Riverside and Orange Counties; 2) the Southern California and California Civil Rights Coalitions, coalitions formed to restore California as a leader in the protection of civil rights and to ensure that California comes into substantial equivalency with the Federal Government on housing and other issues; and 3) the California Reinvestment Committee, a statewide network of community reinvestment advocates responsible for negotiating statewide agreements with large financial institutions, such as a $5 billion CRA commitment with Bank of America to invest in ventures designed to benefit low- and very low-income persons.

To assist the Committee in understanding the Congress' perceptive, I provide the following demographic and related information related to the City and the region.

Los Angeles is a City of 3.4 million residents. Los Angeles County now has 8.7 million residents. The City and the County represent a multiplicity of racial and ethnic groups. In the last decade there has been a significant shifting in the Los Angeles' population. The 1990 census confirmed the fact that persons of color—Latinos, African-Americans, and Asians—now constitute a majority of the City's residents. Latinos, who now constitute 1.4 million or 40 percent of the City's population, grew by 119 percent in the last decade. On the other hand, African-Americans, 488,000 in number, declined in numbers and now make up only 13 percent of the City's population. Asians—Filipinos, Chinese, Japanese, Koreans, Vietnamese, Indians, Cambodians, Thais and others—now constitute 320,000 of the City's population. The numbers of Asians migrating to the City are expected to increase dramatically during the next decade.

The immigrant population in the City exploded during the last decade. In 1980, foreign born residents constituted 27 percent of the official census tally. In 1990, this number increased to 62 percent of the census count. The impact on City and other social services is compelling, for according to the 1990 census data:

—Nearly one million City residents stated they did not speak English very well;
—One half of the City's 3.5 million residents reported that they do not speak English at home;
—Between 1980 and 1990 alone, 750,000 individuals migrated to the City of Los Angeles.

Unlike the socialization patterns of the 1990's, Los Angeles of the 1990's can no longer be viewed as a melting pot where foreign born residents eagerly do everything feasible to become integrated into the mainstream American culture. According to James P. Allen, professor of geography at California State University at Northridge, ". . . [The residents of Los Angeles] are moving into ethnic communities which are divided by language, and it's a potentially divisive force."

According to the Los Angeles County Human Relations Commission, housing discrimination is on the rise, in part, because of the "surge in immigrants from Asia and Central America." Commission Says Housing Bias On The Rise In County, The Daily Breeze, April 22, 1986, page B1. The Commission estimated that discrimination complaints which are filed only represent 15 percent to 25 percent of the actual incidents of discrimination.

In general, there is less information available on the Southeast and Pacific Asian communities than is desirable to operate a comprehensive fair housing program for these communities. In the most publicly available information on 1990 census, counts concerning Southeast Asians, such as Vietnamese and Cambodians, are not differentiated. This lack of differentiation is significant because of language and cultural differences.

As evidenced by the targeting of Korean businesses during the disturbances, friction between African-American and Korean residents have been running high. African-Americans chafe at what they perceive to be a pattern of Koreans and Korean Americans taking money out of communities previously identified as African-American, but not hiring African-Americans or participating in African-American functions. It is also a source of anger to African-Americans that some Korean landlords and business owners advertise only in Korean, thereby creating a major impediment for those who do not speak or read Korean to apply for housing or shop in these establishments. The impression created is that only Koreans need apply or shop in these establishments.

The repair and rebuilding of Asian owned businesses and rental stock in the riot torn neighborhoods Long Beach, Mid-Wilshire and South-Central, is a matter of substantial controversy. Asian business owners are, of course, seeking to recover for the damage done their businesses damaged or destroyed during the riots. "But African-American leaders . . . [believe] the rebuilding efforts offers a new opportunity for African-Americans to take control of businesses in their own neighborhood." Daily News [May 18, 1992].

Racial/national origin tension are exacerbated by the differential economic gains made by African-Americans and Latinos one hand, and Asians and Anglos on the other. As noted in a August 17, 1992 Los Angeles Times article:

> Prosperity blessed Southern California during the 1980's, but it was not colorblind, leaving Latinos and blacks at the bottom of region's economic ladder and keeping whites and Asians at the top. . . . The [Los Angeles] figures bear out national trends that . . . buttress claims that the rising tides of the 1980's failed to lift all boats equally, underscoring concerns that race, ethnicity and wealth in America are tightly bound.

The perception of many African-American residents is that immigrant Asians have gained a disproportionately larger portion of the pie after only short time in the region, and that blacks remain underprivileged in a nation where they have lived for more than two centuries. The effect on race relations is discouraging.

The Federal regulators are changed with the responsibility of identifying and correcting lending policies and practices which violate the Fair Housing and Equal Credit Opportunity Acts, and for ensuring that banks and savings and loans do their share to meet the credit needs of low- and moderate-income areas pursuant to their responsibilities under the Community Reinvestment Act. Congressional oversight hearings before Senator Dixon regarding the supervision exercised by the financial regulators and hearings held in conjunction with passage of the Savings and Loan Bailout legislation, revealed that the regulators have never found discrimination in any of the facilities they supervise. These hearings also revealed that findings of discrimination have been made in at least twenty cases against banks and savings and loans throughout the Nation.

In addition, the financial regulators admit that it is their practice to shield lenders even when the regulators discover that discrimination has occurred. For example, it is the practice of the Office of Thrift Supervision to correct any illegal lender policy or practice, but not to inform the applicant/borrower who suffered discrimination. The regulators maintain this practice, even in those cases where the applicant suffered out of pocket losses, such as increased interest rates or additional application or appraisal fees.

Two of the financial regulators developed monitoring systems to determine whether there are significant deviations from lending norms of interest rates, terms of loans, down payment amounts and other conditions on the basis of race, sex, age or marital status. These monitoring systems were used extensively ten [10] years ago, but are rarely, if ever, utilized by the present administration. The failure to utilize these systems to their full advantage makes it impossible for the agencies to realistically determine whether a lender is discriminating. None of the regulators have instituted similar systems to determine whether discrimination in small business and other loans is occurring.

Based on these circumstances, it is apparent that the supervisory activities of the financial regulatory agencies are inadequate to protect the interests of victims of lending discrimination. The role of fair housing organizations and community groups is essential in this effort. This is especially true in the Southern California region where there is much lender activity acquiring smaller institutions and opening lucrative branches.

One result of the unavailability of traditional and regulated credit is that there has developed a thriving "hard money," industry in low-income neighborhoods of color. The term "hard money" financing is applied to funding which is only available under onerous terms, such as with excessive interest rates, or with exceedingly short payment schedules. A typical "hard money" loan would have a reasonable payment schedule for the first three months of the loans and then a balloon payment, pursuant to which the entire balance of the principle becomes due and owing.

Another result has been increased prevalence of home equity scams in low-income African-American and Latino neighborhoods. The elderly are the typical targets for such scams. The victims are lured into contracts for home improvements which are never performed. Only when the victim stops paying for the work which was not completed does he/she come to realize that the work was secured by the victim's home and the note sold to another entity, which is protected under the law assuming the entity purchasing the note did not have knowledge of the scam that was ran on the victim.

Los Angeles is largely a population of renters. African-Americans and Latinos are much less likely to own than to rent. In 1986, the rate of home ownership in Los Angeles among African-Americans was 45 percent; the rate for Anglos was 70 percent. In 1987, one quarter [25 percent] of the renting population spent 50 percent or more of its disposable income on housing. The percentage spent on housing will escalate dramatically because of the State authorized cuts in General Relief and Aid to Families with Dependent Children. According to a report produced by the University of California at Los Angeles [UCLA], these cuts will also lead to a increase in overcrowding and homelessness among families with children, a protected group under the federal and state fair housing laws.

A 1986 University of Michigan study of Los Angeles living patterns found that "whites are twice as willing to live alongside Hispanics and Asians than they are blacks . . ." Id. at Bl. The study revealed that even when African-Americans attain high levels of education and economic status comparable to Anglos, the two groups remain separate. High income blacks in Los Angeles live in segregated well to do areas separate from white well to do residents. Given the treatment of high income blacks in Los Angeles, it is not surprising that received by low-income blacks is even more harsh.

The patterns of racial separation, especially of African-Americans and Hispanics from Anglos in the Los Angeles region, are apparent in lending and appraisal practices. For decades, lending underwriting experts contended race was an appropriate characteristic to take into account in appraisals. Appraisers contended that certain races brought reduced the value of property. One of the early authorities ranked persons of English and German extraction as the most desirable neighbors and "Negroes" and "Mexicans" as the least desirable neighbors. Such principles were incorporated into the instructional materials of the National Association of the Real Estate Brokers and the American Institute of Real Estate Appraisers. The Federal Housing Administration identified areas in the City where it would not insure, and lenders followed suit by refusing to lend in the areas of high minority concentration. All of these practices have special relevance when poverty issues are coupled with race.

The Los Angeles is now very much divided into "haves" and "have not," with persons of color largely falling into the second category, especially African-American and Latinos. The housing and other needs of these populations have largely unmet and the frustrations that resulted in the April, 1992 have been largely unaddressed. Until these issues are addressed the potential for another upheaval remains.

> I read that report . . . of the 1919 riot of Chicago, and it is as if I were reading the report of the investigating committee on the Harlem riot of 1935, the report of the investigating committee on the Harlem riot of 1943, the report of the McCone Commission on the Watts riot.—Dr. Kenneth B. Clark's testimony to the Kerner Commission quoted at the conclusion of the Commission report of 1968.

Those familiar with the April-May, 1992 disturbance will make the same observations, giving new relevance to George Santayana's statement "Those who cannot remember the past are condemned to repeat it."

The areas most heavily involved in the recent disturbances—South-Central Los Angeles, "Koreatown" and Inglewood—reveal patterns of poor neighborhoods which have grown even more impoverished over the last decade and displacement of African-Americans by a massive influx of Latino and Asian populations, many of whom are immigrants. Watts' African-American population reduced by one third between 1960 and 1990, while the Latino population increased from 17.7 percent in 1980 to 45 percent in 1990. The poverty rate went from 45 percent to 38 percent and the housing vacancy rate from 8 percent to 4 percent during this period.

Another part of South-Central, the Florence and Normandie area which was depicted in much of the camera coverage during the disturbances was 88 percent African-American a decade ago. The 1990 census figures reveals that the area is now only 73 percent African-American. The Latino population in the Florence Normandie area increased from 10 percent to 28 percent in the last decade, while the number of habitable residences reduced from 6,622 to 6,300 units.

The number of African-American homeowners increased during the decade from 1980–1990 in Inglewood, a community just west of South-Central L.A., while the number of Anglos declined in the City. Three decades ago the area was 98 percent Anglo; according to the 1990 census, Inglewood is now 84 percent African-American.

The City income statistics for the last decade reveal an ever widening divide between the "haves" and the "have nots" in Los Angeles. They also revealed that individuals living in affluence tended to be Anglo, and those doing without for the most part are African-American and Latino. The median family income in the City rose

96 percent from $15,746 to $30,925. The number of families making more than $75,000 rose by 496 percent.

Los Angeles City and County reveal some the sharpest contrasts between the richest and poorest residents. For example, in South-Central the economic gains were minuscule at best and lagged behind the rest of the county. In South-Central, one half of the unemployed 16 and older have given up looking for working indicating despair at the prospects of finding jobs, as compared with 37 percent for the county. In 1990, the per capita income in South-Central was $7,023, as compared with $16,149 in the county. Although there was much displacement of African-Americans in South-Central, the population has increased only 6.5 percent, while the County has grown 16 percent. In the County, the median family income of rich communities grew 63 percent, but that of the poor communities such as Vernon, South Los Angeles and Lynwood grew less than 5 percent of median.

> Adding to the hardships in the poorest urban communities, many of people who live there arrived during the last decade, a time of inflationary housing costs, and in some areas, fewer jobs and declining public assistance.—Los Angeles Times, Page 1 [May 11, 1992].

At the same time, the number of families living in poverty grew by 35 percent, and the number of children living below the poverty line grew by 32 percent. Across California, the proportion of children under 18 years of age living below the poverty line grew by 41 percent, resulting in 1.3 children statewide living in poverty. The number of poor families increased by 28 percent statewide, and single female headed household increased by 32 percent. The number of elderly living below the poverty line in California increased to 228,000 or 21 percent. During this period the State's population grew by 26 percent to 29,760,021.

The Rodney King upheaval damage that forced the closure of hundreds of stores and businesses may result in as many as 10,000 jobs being lost permanently. Many of these lost jobs were service oriented positions which paid minimum wages and offered little hope of advancement. Many of the individuals who filled these positions were two paychecks away from homelessness according to a Rand study conducted before the rebellion. As a result of the disturbances, City officials and advocates are bracing for a substantial increase in the Los Angeles City homeless population, which is estimated to be 59,000 on a given night. Many of the newly unemployed are at risk of becoming permanently homeless. Of the homeless in Los Angeles, children are the fastest growing component.

Impoverished homeseekers spend between 50 percent and 70 percent of their income on housing. According to a 1988 report produced by the Los Angeles Blue Ribbon Committee for Affordable Housing, 60 percent of the 1.2 million housing units are renter occupied.

> Housing costs [in Los Angeles] currently exceed 50 percent of the incomes of one quarter of renters households. Rent burden, overcrowding and slum conditions strip away personal dignity an opportunity for economic improvement.

Housing Los Angeles—Affordable Housing for the Future. Report of the City of Los Angeles Blue Ribbon Committee for Affordable Housing, November, 1988. ["The Blue Ribbon Report".] Units which are affordable to the poor are being demolished at the rate of 4,000 a year. Eighty percent of these units require earthquake retrofitting are the type affordable to the poor.

This crisis in affordability affects working poor and middle class persons alike. Average rents in Los Angeles increased 110 percent in 8 years; from $250 in 1980 to $525 in 1988, or 70 percent of the monthly salary of a minimum salary worker. In Los Angeles the median price of a home rose to $224,000 in 1990; by comparison, the median price of a home in the United States was $90,000 in 1990. [The State of the Nation's Housing 1990.] Only 17 percent of Los Angeles residents, and only 3 percent of minorities, can afford to purchase median priced housing. [Blue Ribbon Report at page 13.] As a result of this housing crises, the availability of rental units in Los Angeles on an equal basis is extremely important.

In the context of the Los Angeles situation, the Congress has formed opinions as to the effectiveness of the various fair housing and fair lending laws, as well as the administrative and regulatory structures used to enforce these laws which we are happy to share with the Senate Committee on Banking, Housing, and Urban Affairs.

In 1991, the Congress published a study analyzing the practices of lending institutions doing business in the City of Los Angeles. In conducting this study, the Congress analyzed: 1) Home Mortgage Disclosure Acts Statements of Los Angeles lenders; 2) results of surveys sent to lenders regarding their lending activities and types of services provided; 3) results of surveys of community groups designed to determine their perceptions of critical credit needs; 4) Community Reinvestment Act Statements made by lenders setting forth their activities; and, to the extent available, 5) the underwriting guidelines of lenders. The following conclusions were drawn from publicly available information.

1. Lenders do not make home loans in minority and low-income communities of the City, even when the income levels of these areas meet or exceed the white neighborhoods in which substantial commitments are made.

2. Loans are made in white neighborhoods, notwithstanding the fact that these communities have higher crime rates than the minority neighborhoods in which loans are not extended.

3. There are significantly fewer bank and savings and loan branches in areas of high minority concentration than in white areas, even taking into consideration comparable income demographics.

4. A significant number of lending institutions have minimum loan amounts of $250,000 and $300,000 which far exceed that the cost of housing in African-American and Latino sections of the City where the median cost of housing is approximately $125,000.

The following findings were made with respect to Los Angeles lenders:

- Los Angeles financial institutions make fewer and smaller residential loans in low- and moderate-income areas and minority neighborhoods than in Anglo neighborhoods of the City.
- Los Angeles financial institutions make fewer and smaller loans in African and Latino neighborhoods than in Anglo neighborhoods whose residents have comparable incomes.
- Approximately 94 percent of Los Angeles banking institutions do not allow non-depositors to cash Government checks, and fewer than 50 percent offer low-cost checking accounts to non-elderly poor persons. The result of these practices is to divide equally poor persons into the deserving and the undeserving.
- Financial institutions provide only inadequate banking services, financing [or small businesses, economic development lending or financing of multifamily units which is designed to meet the needs of low-income persons in poor and distressed areas and minority neighborhoods of the City.
- Financial institutions make approximately 50,000 residential loans in the City of Los Angeles. Thrifts and mortgage companies make almost all of the single-family, Government backed single-family, and multifamily first money mortgages and commercial facilities make most of the home improvement loans which are financed through regulated lenders.
- Government backed loans, which most benefit low-income persons and first time homebuyers, are the type which are least frequently made in Los Angeles.
- Fewer than 5 percent of the HMDA reporting facilities in the Los Angeles area report making loans to first time homebuyers.
- Savings and loans, which undertook nearly 15 percent of all residential lending during the period studied, have closed or merged with other facilities.
- Approximately 2.5 loans per residence are made in upper income areas for every one [1] loan per residence in low-income neighborhoods. Almost $4 in residential credit is extended in upper income areas for every $1 in residential credit extended in low- and moderate-income areas.
- Lenders extend nearly 3 single family purchase money loans per residence in Anglo areas for each such loan in minority areas. The facilities lend almost $8 for single family home loans per residence in Anglo areas for every $1 loaned in minority neighborhoods.
- The lower a neighborhood's median income, the fewer and smaller the residential loans it receives. The higher the concentration of minority residents in a neighborhood, the fewer and smaller the residential loans made.
- For the period studied, at least twice as many loans were made per building in Anglo areas than minority areas whose residents have comparable median incomes.
- Approximately one [1] in seven [7] lending institutions do not conduct CRA-mandated assessment of credit needs.

- Excluding commercial areas, there are three times as many branches in high income/and Anglo areas as exist in low- and moderate-income/minority neighborhoods.
- Fewer than 50 percent of the financial institutions allow general relief recipients to direct deposit their benefit checks. Nearly 95 percent of the institutions refuse to allow non-depositors to cash Government benefit checks.
- Very few financial institutions extend credit for predevelopment or land costs for multifamily projects which are affordable for low- and moderate-persons. Financing of predevelopment and land costs are most identified credit need.

Based on the findings of our 1991 study, the City of Los Angeles adopted a linked deposit ordinance which encourages lenders to extend credit in low- and moderate-income areas. This ordinance is administered by the Treasurer's Office. But for the availability of HMDA and CRA data which we analyzed, the City would not have adopted this ordinance.

A recently published analysis of the 1990 HMDA statistics reveals that the home approval rates for ethnic groups in Los Angeles ranges from 62 percent [for African-Americans], to 69.4 percent [for Anglos], to 69.6 percent [for Latinos], to 71.6 percent [for Asians]. In addition, African-Americans, no matter which income bracket they occupy, are rejected for loans more often than their white counterparts. At the $100,000 or more annual income bracket, Anglos were approved for loans 68.1 percent of the times, while African-Americans were approved only 58.4 percent of the times.

The reason cited most often by lender for loan rejection of applications submitted by African-Americans is "credit history." This reason was cited for the rejection of 26. 9 percent of the African-American, 19.9 percent Latino, 17.9 percent Anglo and 12.9 percent Asian applications. There is no definition of the term "credit history." The term includes everything from being 30 days late on a loan payment to the charging off of a loan. In the first instance the result is of little consequence to the lending institution, for the applicant's late fee is designed to cover the administrative costs associated with the collection of the payment. The result is that the lender is made whole. In the second instance, the lender is required to absorb the loss. These situations should not be treated in the same by the lender.

The result of combining these disparate conditions under the one rejection category "credit history" has a marked more negative impact on African-Americans than on other ethnic groups. Having discerned this negative impact, lenders have an obligation to differentiate based on the actual business ramifications to lenders. It may well be that if lenders refrained from considering instances involving the payment of a late fee for being 30 days overdue as a "credit problem," the rejection rates for African-Americans and Latinos in the Los Angeles area may well be brought into conformance with Anglos and Asians.

Another recommendation the Congress has is for the Federal regulatory agencies to establish formal procedures for the acceptance and processing of fair housing and fair lending complaints, similar to the system which HUD has. Pursuant to such systems, the bank regulatory agencies should receive and process complaints in a timely and consistent manner. Remedies for infractions should be handled in a similar manner by all regulators. For example, the Office of Thrift Supervision should adopt an approach similar that which the Federal Reserve reportedly has i.e. one of making the victim of discrimination whole, where discrimination is found and not just correcting prospectively the policy or procedure which lead to the discrimination. Financial regulatory agencies must begin to take their obligations to consumers as seriously as they take their obligations to institutions to insure that these operations are "safe and secure."

It has been suggested that it is a conflict of interest to require which are responsible for insuring the safe and sound operations of financial institutions to also enforce the rights of consumers who have suffered from illegal discrimination or other violations of the law. While I do not agree that this is actual conflict of interest, I do agree that it is perceived as such by examiners, the personnel principally responsible for enforcing the laws. The years of lack enforcement of discrimination and community reinvestment laws by federal financial regulators have shown this to be the case. I recommend that these agencies be relieved of all or at least some of the responsibility of enforcement of said consumer laws.

The obligations should be shared with state banking and thrift officials, for the failure to provide adequate credit has its most serious consequences on the state and local economies. As shown above, communities which do not have access to traditional credit sources have to rely upon "hard money lenders" whose primary intent is to foreclose on individuals and acquire the property and are especially vulnerable to scam artists.

Also needed are better mechanisms for private individuals to challenge the activities of lenders. The trend in this administration appears to be just the opposite. Previously, lenders had to seek permission before they could close branches. At that point consumers were permitted to challenge the closure. Today, such closure can accomplished by giving notice to the regulatory agency. This approach is at best inadequate.

Our 1991 study showed that in Los Angeles residential areas of comparable affluence, there is a much higher incidence of branches in Anglo areas as minority areas. The same was shown to be the case when comparing the incidence of branches in low-income and high-income areas. Public transportation is typically a problem in low-income and minority areas of Los Angeles and such communities often have less access to private transportation. These conditions suggest the need for more, rather than fewer branches. The present system of allowing lenders to close down branches on the basis of mere notice to regulatory agencies has had a disproportionately more negative effect on poor and minority neighborhoods. There are 2.9 branches per 10,000 persons in affluent and Anglo areas of the City, while there are only 1.3 branches for the same number of persons in poor and minority areas.

Although federal financial regulatory agencies have an affirmative obligation to "further fair housing choices" in the administration of their programs, they apparently do not assess the effect branch closures on fair housing choices. If they have made such assessments, the regulators apparently do not believe that the racial and national origin disparities set forth above require any corrective action on their parts.

Any correction of these conditions will have to come as a result of community action, either in the form of protests at the time of proposed closures or suits brought against the lending institutions and the regulators to enforce the fair housing and lending laws in an effective manner.

Community groups need the assistance in achieving equal access to credit and banking services for racial and ethnic minorities and poor persons. Only thrifts are required to make available to the public their underwriting criteria. All institutions should be required to make available such information. Having access to such information is essential to determine whether lenders are complying with their own standards in awarding credit, and to determine whether these criteria have the effect of discriminating on an illegal basis.

Recent HMDA reports reveal that the portfolios of secondary lenders consist of very few loans from minority and low-income areas. Only 3 percent of FNMA loans are purchased from minority areas and approximately 9 percent from low-income neighborhoods. In California most of the single and multifamily loans made by lenders are done so with the expectation that the loans will be sold to FNMA or other traditional secondary market lenders. These lenders must be made to purchase loans on a non-discriminatory basis, so that primary lenders will be encouraged to write loans in minority and poor areas.

The Congress is in the process of negotiating an agreement pursuant to which 396 low-income public housing families, 84 percent of whom are Latino, living in dilapidated housing will receive redeveloped housing. As a result of Congress intervention, the public housing tenants are guaranteed the right to return to newly constructed units, and will be fully integrated into the new project, which will include higher income persons, be racially integrated and double the number of units on the 35 acre site. In addition, the tenants will offered job opportunities during construction and in the management of the redeveloped units. The tenants will also be named the managing general during the first fifteen [15] years of the project.

This deal meets the objectives of the Bush Administration by promoting home ownership by public housing tenants, and will result in what is now a 84 percent Latino public housing site becoming more racially and economically integrated. Unless it is clear to lenders that the 80 million dollar loan package that is needed to finance this deal will be purchased on the secondary market, the deal will not be financed.

Similarly, many units of subsidized housing which are a principal source of low-income and integrated housing may well convert to market rate housing unless lenders are convinced that they will not be criticized by regulators for using five [5] project based certificates as security for refinancing loans. These units were built in the 1960's and 1970's and are now subject to prepayment of their low-interest HUD and Farmers' Home mortgages unless refinancing and incentives for the owners not to convert can be arranged.

Commercial lenders and thrifts play an important role in this process. If conversion is permitted to occur, the impact of such a conversion on low-income and minority families would be a disaster in California. Such projects provide over 100,000 units of housing.

Testing is one of the tools which the private fair housing groups use to determine whether a lender is providing credit in a non-discriminatory manner. Testing is a method of investigation which has been approved of by the United States Supreme Court as a means to determine whether illegal acts are occurring. At present, there is legal proscription against providing bankers with false information as part of a written application. Arguably, testers would be covered by this proscription and subject to prosecution. This proscription has created a disincentive for certain fair housing groups to test lenders. This proscription should be lifted for testing to determine whether illegal acts are occurring.

At present, the Community Reinvestment Act statements which Lenders are required to post are not presented in a consistent format. Some statements are one page long, others are 25 pages long. In monitoring the activities, policies and practices of lenders, it would be very helpful if the information provided were reported in a consistent format.

It has also been a problem that information on business and other loans are not available in the same format as home loans. Less information is available on multifamily loans than is desirable, since this is a primary sources of housing for low-income and minority persons in Los Angeles. Multifamily loans are often handled by the commercial, as compared with the residential real estate, department of lenders. The number of multifamily loans reported under HMDA and the number of loans reported by lenders in their meetings with community groups as part of their CRA obligations suggest that not all multifamily loans may be reported as part of HMDA.

The Congress was not able to compare the ratings it gave to lenders as part of its study with those CRA ratings awarded by financial regulatory agencies. At the time the study was being conducted very few agency ratings were public. A limited survey of the ratings which were available revealed that the ratings which the agencies awarded were much different from those given under our study. In rating facilities the Congress divided the institutions by size and were limited to publicly available information. Nonetheless, these stark differences in rating suggest that the federal agencies are out of touch with the communities to be served, and that there is a role to played by state and local regulators in assessing whether lenders have met the credit needs of their communities or have violated fair housing/lending laws.

Regulators at a state or local level have more immediate access to how lenders are operating and whether they are meeting the needs of their communities. They should be part of the system that assesses the performance of these lenders. Once involved, local and State regulators could monitor the extent to which the lending activities have assisted in creating new job and economic development opportunities or engaged in activities which discriminate against applicants or communities or an illegal basis. In light of the Federal regulatory lack of performance to date and the need of consumers to be protected, I believe the approach should be attempted. Preemption of the field has not resulted in satisfactory performance by banks and thrifts. The States should be given the opportunity to adopt stronger fair lending enforcement measures, in the same way they are permitted to adopt stronger fair housing laws. Lending institutions have been given a "safe harbor" for many years. There seems to be little justification for continuing a system of Federal exclusivity which has not shown itself to be working.

South-Central Los Angeles does not have adequate banking services. This community is not unique. It happens to be in the news at this point, and is, as a result, receiving more attention and somewhat more resources. Other communities, such as Pacoima, a largely Latino low- and moderate-income community, where banking services are even more limited are quietly deteriorating because of the unavailability of banking services. Addressing the banking needs of community should not have to depend on the kinds of displays of frustrations exhibited during April and May, 1992.

Where there are inadequate banking services the lenders and regulators should act proactively to correct the situation. Multibank branches is one answer. Assisting community groups who wish to establish community based credit unions is another. In addition, lenders which cannot afford to build branches in these areas should send representatives into community centers or schools to provide services. Vans should be dispersed to communities where branches have not been established.

For those communities which have been affected by the April, May, 1992 disturbances, additional services are still needed. Individuals still are unable to cash checks. The Congress has reports of lending institutions being unwilling to cash Government checks and requiring forms of identification, typically not used by poor persons who do not drive or do not have credit cards. Another practice which was reported was one of disallowing persons outside the particular branch's service area to cash checks. Clearly lenders must discontinue such practices. All government checks should be cashed, whether or not the individual is a customer. Where alternative forms of identification are available, lenders should permit their use.

In general, lender should seize upon this period of "rebuilding" as an opportunity to redefine their presence in the Los Angeles community. It should no longer be business as usual. One lender should begin the process by advertising using live models of various races and national origins. This is a positive sign of inclusion. It should be followed by evidence of additional extensions of credit in previously under served areas, and other lenders adopting a similar approach.

The information reported pursuant to HMDA and CRA is essential to assist the Congress and other community groups in determining these approaches bear actual fruit and whether the rights of victims of discrimination are being protected under the Fair Housing and Equal Credit Opportunity Acts. The Congress has made extensive use of this information, and believes that HMDA and CRA data is essential to analyzing the patterns of bank activity and determining whether these patterns are discriminatory on a prohibited Fair Housing and Equal Credit Opportunity basis.

Based on our study and other findings, the Congress joined with other consumer and advocate groups to enter into agreements with Wells Fargo, Bank of America, Security Pacific, Union and other large financial institutions in California which designed to improve services to low- and moderate-areas and to minority applicants. These agreements are directed at providing services and housing to the most needy persons in Los Angeles, the largest majority of whom are persons of color.

The recent disturbances in Los Angeles have given greater significance to our 1991 findings which were grounded in the HMDA and CRA data. The author has been interviewed by numerous media personnel, primarily because the study constituted the only compilation of relevant data of its type. If the HMDA and CRA data had not been available the analysis set forth above would have been impossible.

The Congress' 1991 analysis, although useful, was, however, limited. It only considered where loans were placed; nothing was taken into effect with respect to applicant characteristics. The study did not also include a consideration of the effects of small business and consumer lending patterns. Information related to applicant characteristics was not available at the time we conducted the study. The 1990 HMDA information will reflect a portion of this information, and more will become available in the years to come. Only with this type of information will advocates and consumers have a better understanding of the banking, thrift and mortgage broker industry.

More, rather than less, information is necessary about the lending industry, so that consumers can exercise their judgment as to which facilities should be given business. More information is also needed to determine which lending institutions are complying with the fair lending and consumer laws.

When civil rights and low-income advocates discussed the reasons for the high rates of denials of loans to African-Americans, Latinos and others, as compared with Anglos, the bankers stated that the most prevalent reason for rejections of African-Americans was because of "bad credit." When we asked for a definition of "bad credit" we were told that the term included everything from being 30 days late on one occasion to the charge off of loans. Obviously the charge off of loans raises safety and soundness issues of very significant proportions. To classify being 30 days late once in the same way invites further examination to determine whether such a classification has a disproportionate effect on minorities. As a result of discussion with one major lender such an analysis is underway. Without public access to the HMDA information advocacy groups are robbed of the ability to even address such questions with lenders.

Access to the Community Reinvestment Act Statements is also very important to the public. By comparing these statements to the needs the non-profit and for profit affordable housing developers and small businesses revealed to us, we found that the lenders are highly responsive to certain needs and totally unresponsive to others. The results of our study showed that much more attention must be paid to the expression of low- and moderate-community needs by bankers. The recent turmoil in Los Angeles reflects what the continued failure to address-these needs will produce.

The HMDA information also helped focus attention on the secondary lenders. With approximately 3 percent of FNMA loans being purchased from African-American areas and less than 10 percent from low-income areas, it becomes clear that revision of this Agency's guidelines is appropriate. Civil rights and low-income advocates, banks, thrifts and other lenders can join hands to seek appropriate adjustments in this arena. Without the reporting of the secondary market statistics, we would not have any way to monitor the activities of this important affordable housing market.

For the reasons stated, the Congress believes that the reporting of HMDA, CRA and other consumer information is essential to protect the rights of victims of discrimination and to promote fair housing choice. In light of the very stringent financial privacy laws which exist, the data reported under HMDA and CRA is often the only method to determine which lending facilities are complying and which are falling short of meeting their community reinvestment responsibilities. On balance, we believe that whatever paperwork burdens which are associated with CRA and fair lending compliance is both necessary and appropriate.

TESTIMONY OF MICHAEL BODAKEN

SEPTEMBER 15, 1992

Good Morning. My name is Michael Bodaken. I serve as Housing/ Community Reinvestment Coordinator for Mayor Tom Bradley in Los Angeles, California. Today, I intend to discuss how the Community Reinvestment Act and the evaluation process can be strengthened to accomplish its original intent; and how Congress can make the CRA more useful for the credit needs in neglected communities, such as South Los Angeles.

My overall theme is that the Act cannot be abandoned, especially in these difficult times. As I note below, the amount of banking activity in a community is directly related to the economic health of that community. CRA is an indispensable tool in promoting neighborhood and community vitality.

CRA's Original Goal: Providing Meaningful Access to Capital to Everyone in the Community

The adoption of the Community Reinvestment Act by Congress in 1977 made clear that financial institutions have a continuing, affirmative obligation to serve the public. Financial institutions with certain privileges, including charters, deposit insurance and access to special borrowing from the Federal Reserve and Federal Home Loan Bank, must serve everyone.

15 years later, the question remains as to what such community service entails. The Senate Committee on Banking, Housing, and Urban Affairs is properly concerned about how CRA can be used to provide meaningful access to capital for all members of the community. The Act itself lays the groundwork for this question. Ac-

cording to the Act, each financial institution must be assessed according to the following criterion:

". . . the institution's record of *meeting* the credit needs of the entire community, including low and moderate income neighborhoods, consistent with the safe and sound operation of such institutions."[1]

Moreover, CRA examination regulations provide that simply making *available* a credit program to everyone is not necessarily sufficient. According to the regulations, a CRA examination should include:

—the institution's participation, including *investments,* in local community development and redevelopment projects or programs.

—the institution's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community, or the purchase of such loans originated in its community.

—the institution's participation in governmentally insured, guaranteed, or subsidized loan programs for housing, small businesses or small farms.[2]

Nevertheless, the regulations do not *require* that a satisfactory rating be withheld from financial institutions which actually have inadequate lending *performance*. Indeed, an entity need only demonstrate that it has a "satisfactory or better performance record under these (12) factors, *taken as a whole.*"[3] According to guidelines published by the Federal Reserve Bank of San Francisco, an institution may receive a "Satisfactory" rating even though CRA is not an integral part of the institution's planning process and without aggressive marketing of special credit products to the community.[4] Instead, it is enough that the institution has delineated community needs, "occasionally involve(d) the board of directors and senior management in CRA-related activities," maintained a "satisfactory" level of involvement in the community and generally participated in economic revitalization.[5]

This same nod and wink approach is contained in the CRA Statement which financial institutions are required to submit and make available to the public. The Statement need only delineate the local community it serves on a map, list the types of credit offered (not actually originated) and a copy of the CRA Notice explaining the purpose of CRA. The Federal Financial Institutions Examination Council has determined that it can only "encourage" institutions to document in their CRA Statements how well such institutions are actually satisfying the credit needs of all segments of the community.[6]

Evaluation results confirm this view. Recently, the Federal Deposit Insurance Corporation released its ratings of 279 institutions

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[1] *Community Reinvestment Act,* Section 804 (1) (emphasis added).

[2] Federal Financial Institutions Examination Council, *A Citizens Guide to CRA* (1986), p. 3 (emphasis added).

[3] Federal Financial Institutions Examination Council, *Community Reinvestment Act Performance Evaluations* (December, 1990), p. 5 (emphasis added).

[4] Jeffrey Marshall, *Staying Ahead of CRA: What Financial Institutions Must Know to Win at Community Investment* (Business One Irwin, 1992), pp. 217–218.

[5] *Ibid.*

[6] Federal Financial Institutions Examination Council. *A Citizens Guide to CRA* (1926), p. 2.

nationwide for the month of July, 1992. A total of 18 such institutions, or 6.5 percent of those surveyed received "Needs to Improve" or "Substantial Noncompliance" ratings. Thus, 93.5 percent of those institutions surveyed received a satisfactory rating or better![7] For the years July 1, 1990–July 31, 1992, here is the following breakdown for evaluations by the FDIC:

Total	Outstanding	Satisfactory	Needs to Improve	Subst. Nonc.
5288	493	4336	419	40
100 Percent	9.3%	81.9%	8%	.7%[8]

Thus, over the last 2 year period, the FDIC has judged that well over 90 percent of its institutions are actually meeting their Community Reinvestment Act responsibilities. This constitutes *prima facie* evidence that the current evaluation system skews favorably toward financial institutions and unfavorably toward low and moderate income neighborhoods' credit needs.

The blurring of process and result reinforces the view that CRA activity is marginal to other lending and banking activity. Until ratings reflect actual performance, banks will continue to marginalize community reinvestment activity.

Fortunately, there are exceptions. Some banks actually treat community reinvestment as a new marketing opportunity. When actual performance is the criteria for evaluation, it becomes clear that financial institutions which treat community reinvestment as a line business item tend to do better. For example, Great Western Savings and Loan's home mortgage record, with a market share of 16.2 percent in South Los Angeles, exemplifies a *market approach* which happens to result in benefit to low and moderate income neighborhoods:

> "This is something we have targeted long before it was the fashionable thing to do. . . . We tend to finance shelter more than expensive homes. We felt we could do a good job of inner city lending if we were there with the people who are part of the community, who know the community."[9]

Great Western's view is confirmed by other bankers who have received "outstanding" ratings from regulators. They also observe that a bank cannot treat CRA as a special lending program. Instead, it should be viewed as part and parcel of a bank's regular, daily business.[10]

CRA evaluation regulations therefore need to be modified to fulfill the original intent of the Act: no institution should receive a passing grade unless that institution has actually marketed credit products to all members of the community *and* substantially dem-

[7] The July, 1992 results are attached hereto as Exhibit "A."

[8] Based on conversation with FDIC Office of Corporate Communications, September 8, 1992.

[9] Robert A. Rosenblatt, et al., "Home Loan Gap: Banks are Behind S&L's in Lending to Minorities," *Los Angeles Times*, September 8, 1992, Section D, p. 9, quoting James Montgomery, CEO of Great Western Bank. The article is attached as Exhibit "B".

[10] Marshall, *Staying Ahead of CRA*, p. 220.

onstrated that such products have resulted in a significant benefit to low and moderate income communities that institution serves. This will help make the community reinvestment activity more "mainstream" and demonstrate much more clearly who in fact is lending in low and moderate income neighborhoods in this country.

Beyond HMDA: The Need for Better and More Complete Data

Financial institutions are now required to "geocode" home mortgage loans to provide evidence of meeting the housing credit needs in communities which they serve.[11] Home Mortgage Disclosure Act data will obviously continue to be central to any CRA exam. Data published by the *Los Angeles Times* as recently as last week reveals that larger banks are still not fulfilling their obligation to provide home mortgage loans to certain minorities, especially African Americans.

According to the *Times*, home mortgage lending in South Los Angeles by major banking institutions in Los Angeles is very poor. Two large institutions, Bank of America and Wells Fargo, ranked 11th and 43rd in home mortgage lending in South Los Angeles.[12] Interestingly, both of these banks were most recently rated "outstanding" by the Office of Comptroller of the Currency.

This data performs at least two important functions: First, it provides meaningful information to the public about banking activities of various financial institutions by neighborhood. Second, and just as critical, it monitors banking activities in such neighborhoods to determine whether banks are making community reinvestment an activity central to their everyday business. Recently, Bank of America dramatically expanded its marketing efforts for home loans in South Los Angeles in direct response to criticism of its 1990 HMDA performance.

But home lending is not necessarily the whole picture. The question posed by this Committee is whether such data on small business or consumer loans should also be generated and made public. I believe the answer must be in the affirmative. Community reinvestment cannot occur without small businesses flourishing. Small businesses cannot flourish unless they have meaningful access to credit.

There is evidence that small businesses are in fact denied such credit. For example, a furniture manufacturer in business for more than 10 years and with excellent financial statements has always banked with one of California's largest financial institutions. That bank holds a first mortgage on his factory building. The manufacturer wanted to restructure his debt and requested the bank to refinance the building. He was told by a mid market group at the bank that the bank was not interested in business refinancing.

An owner of three community markets, two of which are in middle income areas and one in a low income area of the city of Los Angeles reported that he was able to obtain construction financing much easier in the middle income areas than in the low income

[11] The term "Geocode" refers to adding census tract, state, metropolitan statistical area, county and block group codes to a customer's loan record.

[12] Robert A. Rosenblatt, et al., "Home Loan Gap," p. D1, Exhibit "B". In 1991, Wells Fargo made but 5 home loans in the entire South Los Angeles area. *Ibid,*

area. All three were financed within a fairly short period of time and the financials in all three were similar. Banks mentioned nebulous "risk" in their assessment of the low income area. No mention of such risk was mentioned for the markets in the middle income areas.

Accounts such as these led Mayor Bradley and Councilman Mark Ridley Thomas, Chair of the Community Economic Development Committee, led an effort to adopt a Linked Banking Ordinance which will require from those institutions which wish to do business with the city to make complete disclosures of small business and consumer loans.[13] Both the Mayor and the councilman are particularly concerned that banks that do business with the city demonstrate that they are lending to residents and businesses located in the city of Los Angeles. Our $4 billion investment in local financial institutions will hopefully make this invitation for more information appealing to most banks. You should also note that we have formed a committee to implement this ordinance with the specific provision that the particular needs of small banks not be ignored and that the program be fair and reasonable.

But this local linked banking ordinance, by definition, solely involves those who desire to do business with the city of Los Angeles. Only Congress can enact legislation or require federal agencies to adopt regulations which require complete lending information to be disclosed by all financial institutions.

Thus, I believe financial institutions should geocode small business and consumer loans.[14]

Further, this information should be widely disseminated to community groups and local governments. Currently, CRA evaluations are held by the institution and the regulators. It is obviously important that the public receive access to these evaluations. I would urge that the regulators be required to deposit CRA evaluations with local libraries and clerks of local governments so the public can have greater access to this information.

The Proposal to Exempt Banks Which Have Received Outstanding or Satisfactory Evaluations from Protest

For the reasons set forth above, it is clear to me that the current evaluation process has serious problems. In particular, I believe that the current process leads to grade inflation because banks are not necessarily required to demonstrate actual origination of loans to low and moderate income neighborhoods to receive a better than passing grade. I would ask you to reject any notion that banks with outstanding or satisfactory evaluations be exempted from community protest at a time of merger, acquisition or bank closing.

It is precisely at the point of merger, acquisition or branch closing that financial institutions should receive the greatest scrutiny.

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[13] *See* attached Exhibit "C."

[14] Many banks have taken an additional step and incorporated computerized loan mapping in their presentations. According to the Office of Thrift Supervision: "Mapping provides two specific advantages. One is more effective presentations to senior managers and board members. The maps make a case very clearly. The other is, it improves the efficiency of the examiners." Marshall, *Staying Ahead of CRA*, p. 229. I would argue that the third advantage is that such mapping can describe to local government and community groups how well an institution is doing, merely by simply reviewing the map. Computerized mapping, which once required a mainframe, now can be performed on a desktop computer. *Ibid.* Any slight burden occasioned by such a requirement on larger institutions is obviously outweighed by the public interest in such disclosure.

The recent experience of the Bank of America/Security Pacific merger is a case in point. Prior to the merger, Bank of America had received an "outstanding" rating from the Federal Reserve; Security Pacific had received a "satisfactory" rating. Yet, as a consequence of extensive negotiations between communities and local groups, Bank of America, whose community reinvestment record had previously been adjudged "outstanding," committed itself to an additional, unprecedented $12 billion community reinvestment program over the next 10 years: a condition of its merger. BofA also agreed to maintain all of Security Pacific's loan programs targeted for low and moderate income neighborhoods. If BofA or Security Pacific had a "safe harbor" provision, as suggested by some, I do not believe this would have taken place.

How CRA Can Be Used More Effectively to Provide Access to Capital in Areas like South Los Angeles

I would argue that the Act has already had an impact on access to capital in South Los Angeles. For example, after a release of 1990 HMDA findings (which is usually central to a CRA review) placed Bank of America in a somewhat unfavorable light, BofA arranged to provide a bonus to agents who originated a loan in South Los Angeles, and required a review of any declined loan at a higher level. It appears that Bank of America is now increasing its market share of such loans in South Los Angeles, thus fulfilling the intent or the Act.[15]

Further, the Community Reinvestment Act has helped form the parameters of local community reinvestment activity in many of this Nations major urban centers. Against the backdrop of the Community Reinvestment Act, we have formed a Los Angeles Community Reinvestment Committee. That committee was established in December, 1990 to "develop a comprehensive plan to help revitalize depressed areas of Los Angeles with the initial target area in South-Central Los Angeles." Approximately 6 months later, it provided the city a report, attached as Exhibit D to these materials. This committee meets on a monthly basis and provides an important forum for community groups and local government people to discuss investment ideals and problems with local banks.

It was this committee which identified one critical problem in getting access to capital in places like South Los Angeles. The study in Exhibit D noted that there were 133 check cashing institutions covering the same geographical area as 19 banks (See pp. 30–33 of Exhibit D). Obviously, without geographical proximity to local branches, it is difficult for persons in South Los Angeles to acquire capital from local lending institutions. Lack of access to traditional capital will definitely lead to reliance on lenders who are more expensive and possibly unscrupulous. The lesson is that banks must have geographical proximity to low and moderate income neighborhoods for those neighborhoods to have access to their credit products and services. Fortunately, the Act takes branch location into account in evaluating banks.

Still, problems remain. For example a company which manufactures shopping carts and shelving for supermarkets has been in business in Watts for more than 40 years and has excellent credit.

[15] Rosenblatt, et al., "Home Loan Gap, etc.", p. D9, Exhibit "B".

The company had an opportunity to increase its market share when two of its competitors ceased operations. The company wanted to acquire a new building in Watts to expand. A local major bank sent two middle market loan officers to inspect the company and the new site. The project was rejected immediately after the visit based on perception or risk due to the location and surrounding neighborhood.

This type of problem has led local policymakers to demand formation of a Bank Community Development Corporation (CDC). Using a statewide housing consortium as a model, a multi-bank Community Development Corporation is being developed. Mayor Tom Bradley and Councilman Mark Ridley-Thomas have asked that the CDC's purpose be small business loans for operation and expansion of small businesses within the pilot area. The target area will be the same target area in South Los Angeles as identified by the Community Reinvestment Committee in Exhibit D. The bank CDC intends to provide "gap financing" of amounts between $25,000 and $250,000. The initial capitalization will be somewhere between $5–10 million. First Interstate Bank Chairman Bruce Willison has agreed to lead the effort. The Federal Reserve has encouraged the establishment of this Bank CDC as a type of special program that financial institution can undertake to provide additional credit to neglected communities. We expect that banks will utilize their participation in this CDC as a means to impress regulators of their intention to make investments in low and moderate income neighborhoods. Again, without the Community Reinvestment Act, I doubt that this activity would take place.

CONCLUSION

The Community Reinvestment Act is worth saving. To both preserve it and implement its most fundamental purpose, the Senate Committee on Banking, Housing, and Urban Affairs can take the following steps:

1) No institution should receive a passing grade unless that institution has actually marketed credit products to all members of the community and substantially demonstrated that such products have resulted in a significant benefit to low and moderate income communities that institution serves;

2) Require financial institutions to geocode business and consumer as well as home loans; and

3) Do not dilute the Community Reinvestment Act. In particular, do not provide "safe harbor" provisions to banks with outstanding or satisfactory records until such time as it is demonstrated that these evaluations more clearly implement the intent of the CRA, i.e., meeting the credit needs of all communities that financial institution serves.

TESTIMONY BY GILDA HAAS

COMMUNITIES FOR ACCOUNTABLE REINVESTMENT

SEPTEMBER 15, 1992

INTRODUCTION

Communities for Accountable Reinvestment (CAR) is a coalition of grassroots community organizations and one municipality who are committed to advocacy for responsible banking practices in their communities. CAR and its members are particularly concerned that the banking institutions doing business in Los Angeles and other Southern California communities meet their responsibilities under the Community Reinvestment Act. CAR is a member of the National Community Reinvestment Coalition.

CAR's member organizations are ethnically diverse, representing African-American, Asian-American, Latino, and White constituencies. They are also diverse in terms of the day to day focus of their work—some are non-profit housing developers, some represent tenant unions, and others work in the fair housing arena. Some of our organizations are based in churches and others in labor organizations. As a coalition we come together at the conjuncture of civil rights and economics, sharing a long term view that economic justice will not be won for any of our communities until it is won for all of our communities.

It has been our experience that, for the most part, neither banks nor regulators have yet delivered the promise of the Community Reinvestment Act. In Los Angeles and neighboring Orange, San Bernardino, and Riverside Counties drastic disparities in lending persist by race and class and minority and working class communities still do not have banking services and credit that meet their needs. As bank mergers and consolidations escalate, branch closures have been concentrated in minority and working class communities. Today the experience of redlining does not only mean that people do not have access to credit from conventional financial institutions. Today many communities simply do not physically have access to banks.

There are very few people who live in Los Angeles today who do not understand the relationship between historic disinvestment and the underdevelopment of our inner city communities. There are very few people who do not recognize the relationship between disinvestment by banks and the accelerated immiseration of people who live in those communities. And, there are very few people who experienced the shock of the recent civil unrest who do not see a relationship between the destabilizing forces of disinvestment and the conditions of disenfranchisement which allow riots to occur at all.

We are thus angered by and fearful of efforts to weaken or dismantle the Community Reinvestment Act. It has been our experience that the voluntary initiatives of banks have been entirely insufficient to address fair access to credit. Regulators have also been undependable in enforcing the Community Reinvestment Act in a manner that creates meaningful changes in bank lending practices. We are thus asking for your support in assuring that these changes will occur by vigorous and serious enforcement of the Community Reinvestment Act.

To support this request I will document the persistent problem of redlining as it occurs in our communities and the need for a vigorously enforced Community Reinvestment Act using case examples from CAR's experience and research. These case examples will show that:

- Enormous disparities in lending persist by race and class of borrower community even among large financial institutions which have "excellent" Community Reinvestment Ad ratings. This point will be illustrated by a market share analysis of the Los Angeles MSA, focusing on comparisons between major financial institutions.
- The trend of branch closures resulting from bank mergers and consolidation disproportionately impacts minority and low-income communities. This problem and its ramifications will be illustrated by America and Security Pacific's branch closures between 1980 and 1989 and by an analysis of the impact that reduced banking services has had on South-Central Los Angeles.
- A wide gap exists between the way that regulators and communities evaluate CRA performance. Over the past fifteen years, banks and regulators alike have managed to institutionalize Commun1ity Reinvestment as a marginal aspect of the business of banking. Most bankers and regulators do not see CRA as central to the strategic objectives of the bank or its business plan. Instead, CRA is perceived as a side issue, analogous to corporate philanthropy. Grassroots community groups, on the other hand, focus on how banks perform in meeting basic community needs in concrete terms, such as the number of loans made in minority and low-income areas, and other objective criteria. CAR's "CRA Performance Self-Examination" will be used as one example of community criteria for evaluating CRA performance.
- The single most effective tool in improving the accountability of banks to community needs has been the vigorous and persistent use of provisions of the Community Reinvestment Act by community groups, including intervention in bank mergers and acquisitions. However, we find that these efforts have shown limited results towards the goal of eradicating redlining and racial and class disparities in lending. The evidence presented here shows that the Community Reinvestment Act needs to be strengthened and more conscientiously enforced.

CREATING A MARKET CONTEXT FOR EVALUATING CRA PERFORMANCE

CAR has conducted considerable, research to objectively document the persistent racial and income disparities in lending that are the common experience of our grassroots constituencies. One primary issue in analyzing lending data is the need to construct the context in which the analysis is taking place. The most commonly used framework for analyzing various aspects of bank performance is the "market." An objective description of the market provides local relevance to the analysis and permits a study of relative performance between banks. In the research presented below, CAR uses aggregate HMDA data, the location of buildings, and census population demographics to create such a context.

Major Banks and the Los Angeles Lending Market

CAR's first study attempts to define the Los Angeles lending market in terms of County-wide aggregate lending patterns. To accomplish this, the number of all 1–4 unit home mortgage loans made by all lenders in the Los Angeles MSA in 1990 were analyzed to establish a baseline description of the market. These 67,643 mortgages were then broken down into sub-markets defined by income characteristics and racial composition of census tracts. The study then positioned three major lending institutions—Bank of America, Wells Fargo, and Great Western—within these markets.

Racial and Income Disparities in Lending

Figure 1 shows that although Bank of America, First Interstate and Wells Fargo control different shares of the 1–4 unit mortgage market in L.A., they display very similar lending patterns which consistently decline as communities become less affluent. Both Bank of America's and Wells Fargo's market shares also drop dramatically as communities become increasingly minority. By using the example of Great Western Bank—one of the largest and healthiest lenders in the State—the study also shows an alternative and profitable approach to the L.A. market. For example, Figure 1 shows that like Bank of America, Great Western's market share of home loans to high income census tracts is about 9 percent. But in stark contrast to Bank of America, Great Western's market share increases to 24 percent in low- and moderate-income census tracts while B of A's drops to 3.5 percent.

Similarly, Bank of America and Wells Fargo's lending falls precipitously as communities become increasingly minority (See Figure 2). For example, Bank of America, which has a 6.6 percent share of the overall County home mortgage market, has an 11 percent share of lending to communities that are primarily white (having less than 10 percent minority residents). In communities with 80 percent or more minority populations, B of A's market share is a negligible 2.7 percent—less than one-fourth its share of home loans in overwhelmingly white communities. Wells Fargo has a smaller market share in all categories, but its lending patterns virtually mirror those of Bank of America. This performance is even more unacceptable when compared to the current demographic composition of Los Angeles County, which according to the 1990 census is now 60 percent minority (See Figure 3).

Great Western provides an example of profitable lending which is more consistent with the region's demographics, an important market indicator. Here, Great Western's 6.2 percent share in neighborhoods which are almost entirely white jumps to 29.4 percent in communities that are overwhelmingly minority.

Comparing Where Loans Were Made to Where They Could Be Made

A second study was conducted which defined the market in terms of how one to four unit buildings were distributed across Los Angeles census tracts categorized by income and racial composition.

In this study, a comparison was first made between the distribution of all lending to one to four unit buildings and the distribution of those buildings in census tracts categorized by racial and income characteristics. As indicated in Figures 4 and 5 there is a surprisingly good fit between the location of buildings and the distribution of lending across census tracts classified by income, and to a somewhat lesser degree across census tracts classified by racial composition. The greatest gap is found in census tracts which are 80–100 percent minority. Approximately 19 percent of the one to four unit buildings are located in these census tracts which receive only about 12.5 percent of the loans.

Figure 1

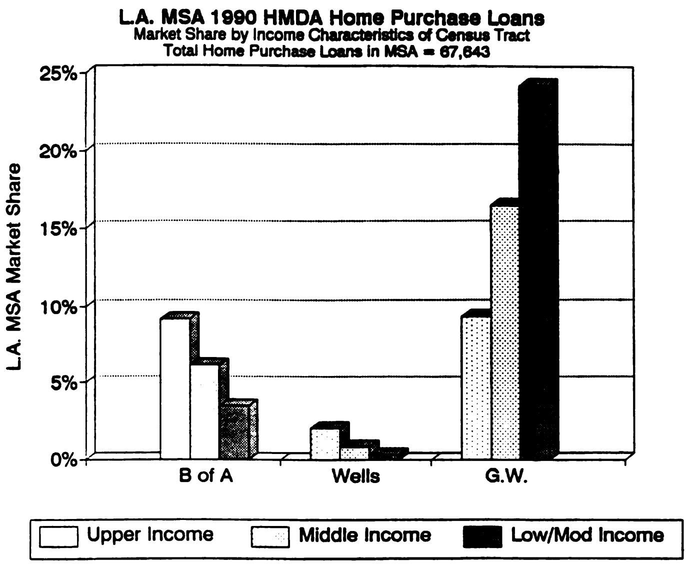

L.A. MSA 1990 HMDA Home Purchase Loans
Market Share by Income Characteristics of Census Tract
Total Home Purchase Loans in MSA = 67,643
L.A. MSA Market Share
25%
20%
15%
10%
5%
0%
B of A
Wells
G.W.
Upper Income
Middle Income
Low/Mod Income

Figure 2

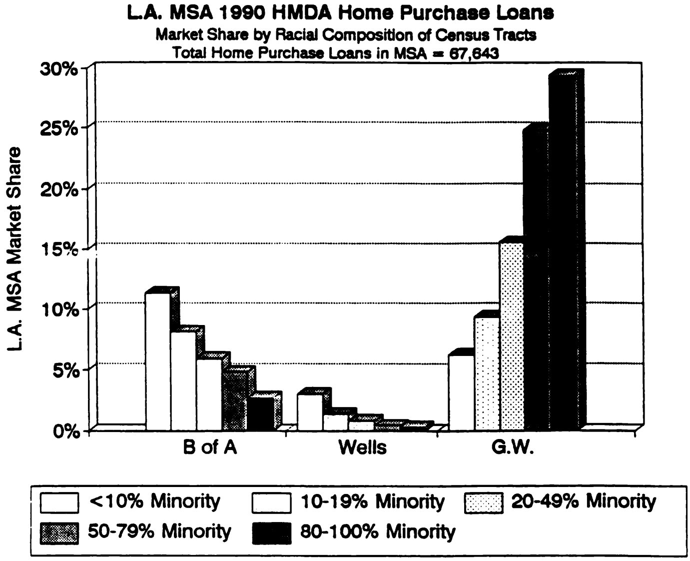
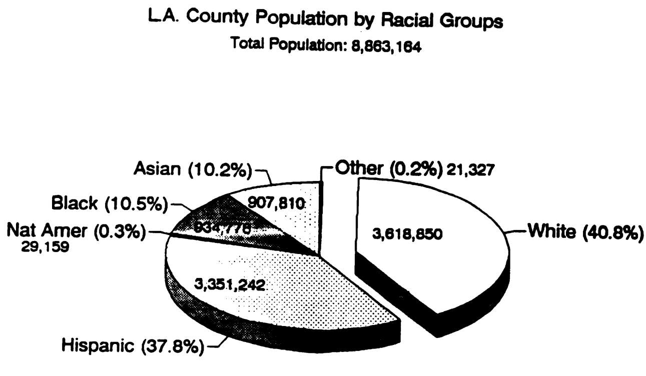

L.A. MSA 1990 HMDA Home Purchase Loans
Market Share by Racial Composition of Census Tracts
Total Home Purchase Loans in MSA = 67,643
L.A. MSA Market Share
30%
25%
20%
15%
10%
5%
0%
B of A
Wells
G.W.
<10% Minority
10-19% Minority
20-49% Minority
50-79% Minority
80-100% Minority

Figure 3



Source: U.S. Census, 1990

Figure 4

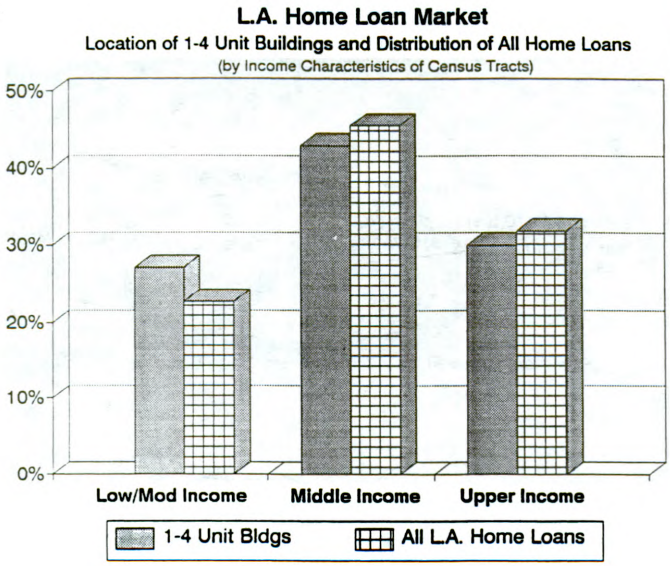
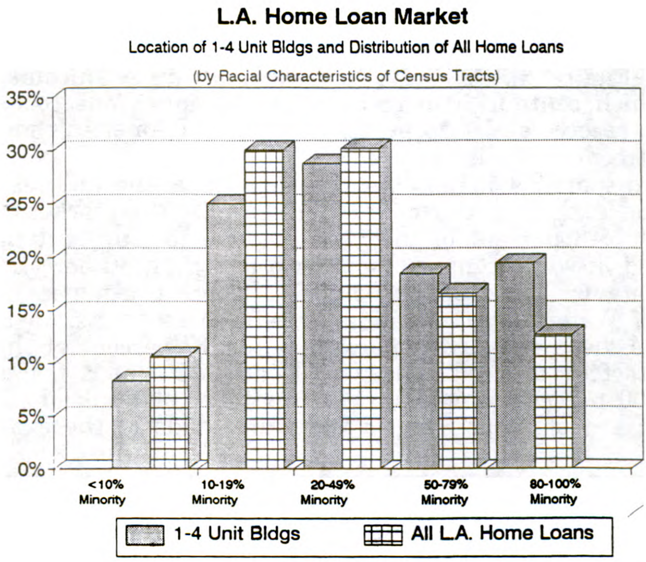

L.A. Home Loan Market
Location of 1-4 Unit Buildings and Distribution of All Home Loans
(by Income Characteristics of Census Tracts)
50%
40%
30%
20%
10%
0%
Low/Mod Income
Middle Income
Upper Income
1-4 Unit Bldgs
All L.A. Home Loans

Figure 5


L.A. Home Loan Market
Location of 1-4 Unit Bldgs and Distribution of All Home Loans
(by Racial Characteristics of Census Tracts)
35%
30%
25%
20%
15%
10%
5%
0%
<10% Minority
10-19% Minority
20-49% Minority
50-79% Minority
80-100% Minority
1-4 Unit Bldgs
All L.A. Home Loans

These inconsistencies are, however, negligible when compared to the manner in which Bank of America and Wells Fargo distribute loans across the market. Here, again, it is found that low- and moderate-income census tracts receive disproportionately small and upper income census tracts receive disproportionately large numbers of loans from these three banks. For example, while twenty-seven percent of the one to four unit buildings are located in low- and moderate-census tracts, these tracts receive only about 12 percent of Bank of America's home loans and 7 percent of Wells Fargo's (See Figure 6). At the other extreme, upper income census tracts, which contain 30 percent of the County's one to four unit buildings, receive about 45 percent of Bank of America's mortgages and 58 percent of Wells Fargo's.

Racial disparities in lending are also apparent in these banks when their lending, patterns are juxtaposed to the market (See Figure 7). Only 8 percent of the County's one to four unit buildings are located in white census tracts with less than 10 percent minority populations. However, 18 percent of Bank of America's and 30 percent of Wells Fargo's lending goes to these tracts. In minority tracts, the disparities are reversed. While 19 percent of the County's one to four unit buildings are located in census tracts which are 80–100 percent minority, only 5 percent of Bank of America's and 3 percent of Wells Fargo's loans are made in these neighborhoods.

The principle of reinvestment also includes some concept of the flow of cash into communities. For this reason, it is also useful to look not only at the number of loans made by banks, but at their dollar value as well. As shown in Figure 8, here the disparities are the most dramatic. Low- and moderate-income neighborhoods which contain 27 percent of L.A.'s one to four unit buildings, receive only 6 percent of Bank of America's loans and 4 percent of Wells Fargo's. In stark comparison, upper income census tracts, which contain 30 percent of the subject buildings, receive 63 percent of Bank of America's loans and 72 percent of Wells Fargo's.

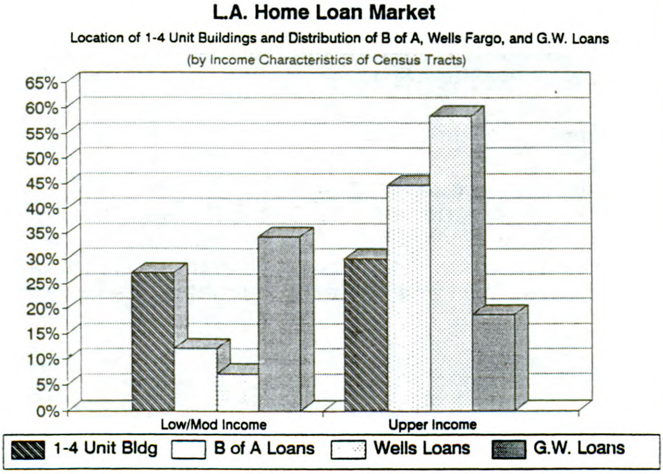
Racial disparities in lending in this example are equally dramatic. As shown in Figure 9, white neighborhoods—those with less than 10 percent minority populations—contain 8 percent of the one to four unit buildings, yet receive 32 percent of Bank of America's loan dollars and 44 percent of Wells Fargo's. Minority neighborhoods—those with 80 percent–100 percent minority populations—contain 19 percent of the building market. However, these census tracts receive only 2 percent of Bank of America and Wells Fargo's loan dollars.

Arguments will be made to dismiss these huge disparities as evidence that these banks help keep poor communities poor and minority communities underdeveloped. The fact is, given the population demographics of Los Angeles and the distribution of homes within the L.A. market, these banks have to work hard to find and penetrate that many white and affluent neighborhoods to place the bulk of their loan dollars. Some may argue that, of course, real estate in higher income neighborhoods costs more, and that is why the disparities in loan dollars are so high. A response more consistent with the Community Reinvestment Act and with the Los Angeles market would be to create and sell products which result in the origination of more, smaller loans in lower income communities. But this has not been the response of Bank of America and Wells Fargo.

This approach is, however, consistent with the more equitable, yet profitable lending patterns of Great Western Bank. Great Western's dollar lending patterns, shown in Figure 8, are very consistent with how buildings are distributed across income categories of census tracts. Low- and moderate-income neighborhoods contain 27 percent of the building market and receive 29 percent of Great Western's loan dollars. Upper income tracts contain 30 percent of the buildings and receive 24 percent of Great Western's loan dollars. Here, any inconsistencies are in favor of communities that need loans the most, and are less favorable to affluent communities.

Figure 9 shows that a similar fit exists between the distribution of Great Western's loan dollars and the distribution of buildings by racial composition of census tracts. 8 percent of the buildings are found in white tracts with less than 10 percent minority populations. Here, Great Western places 6 percent of its loan dollars.

Figure 6



L.A. Home Loan Market
Location of 1-4 Unit Buildings and Distribution of B of A, Wells Fargo, and G.W. Loans
(by Income Characteristics of Census Tracts)
65%
60%
55%
50%
45%
40%
35%
30%
25%
20%
15%
10%
5%
0%
Low/Mod Income
Upper Income
1-4 Unit Bldg
B of A Loans
Wells Loans
G.W. Loans

Figure 7

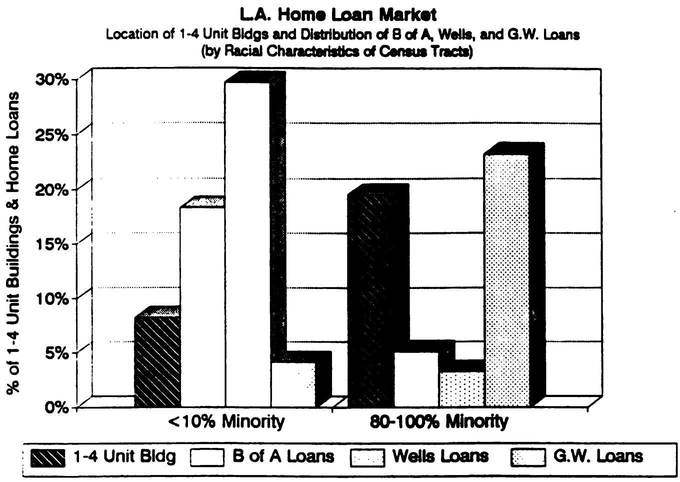

L.A. Home Loan Market
Location of 1-4 Unit Bldgs and Distribution of B of A, Wells, and G.W. Loans
(by Racial Characteristics of Census Tracts)
% of 1-4 Unit Buildings & Home Loans
30%
25%
20%
15%
10%
5%
0%
<10% Minority
80-100% Minority
1-4 Unit Bldg
B of A Loans
Wells Loans
G.W. Loans

Figure 8

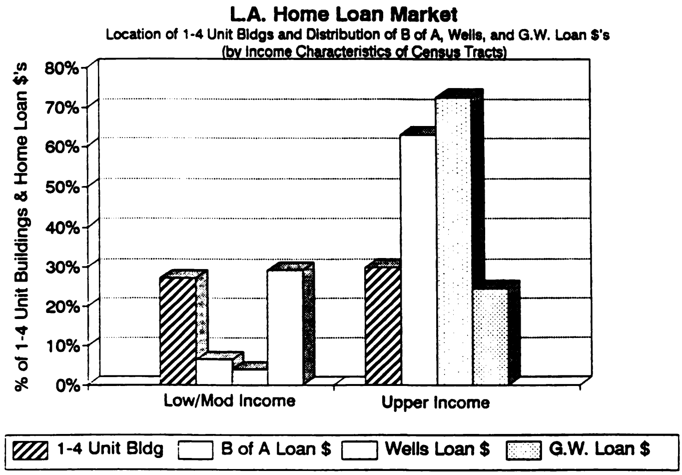
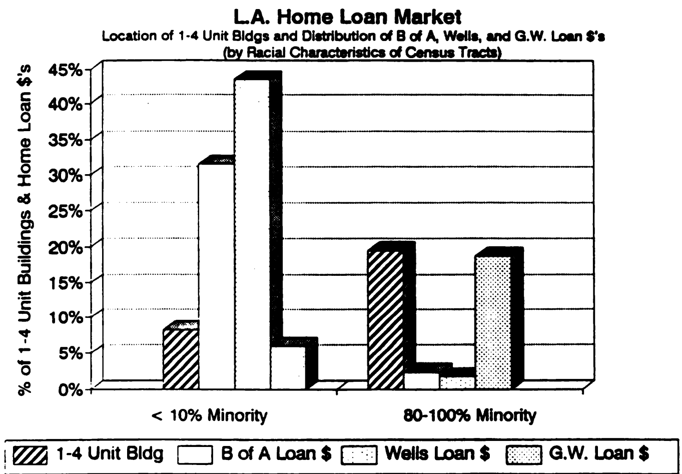

L.A. Home Loan Market
Location of 1-4 Unit Bldgs and Distribution of B of A, Wells, and G.W. Loan $'s
(by Income Characteristics of Census Tracts)
% of 1-4 Unit Buildings & Home Loan $'s
80%
70%
60%
50%
40%
30%
20%
10%
0%
Low/Mod Income
Upper Income
1-4 Unit Bldg
B of A Loan $
Wells Loan $
G.W. Loan $

Figure 9


L.A. Home Loan Market
Location of 1-4 Unit Bldgs and Distribution of B of A, Wells, and G.W. Loan $'s
(by Racial Characteristics of Census Tracts)
% of 1-4 Unit Buildings & Home Loan $'s
45%
40%
35%
30%
25%
20%
15%
10%
5%
0%
< 10% Minority
80-100% Minority
1-4 Unit Bldg
B of A Loan $
Wells Loan $
G.W. Loan $

And, in tracts with 80–100 percent minority populations, which contain 19 percent of the County's one to four unit buildings, Great Western has invested about 19 percent of its loan dollars.

BRANCH CLOSURES AND OPENINGS ARE INEQUITABLY DISTRIBUTED

A 1991 survey commissioned by the City of Los Angeles asked banks throughout the City of L.A. how many branches they had opened and how many had they closed since January 1, 1987.[1] The results—27 branch openings and 416 branch closings—are indicative of the heavy consolidation and cost-cutting trends in the banking industry. What is important to note here, is that branch closures are inequitably concentrated in low income and minority communities.

CAR's review of branch closures by Bank of America and Security Pacific provides a good example of this problem. Using FDIC records of insured depositories, CAR conducted a study of Bank of America and Security Pacific branch closures in the City of Los Angeles between 1980 and 1989, and found patterns of discrimination similar to those presented in our lending studies. During this period, Security Pacific closed 21 branches and Bank of America closed 30. 71 percent of Security Pacific closures and 67 percent of Bank of America's were in low- and moderate-income communities. None of Security Pacific's closures and only four of Bank of America's closures were in upper income neighborhoods. 52 percent of Security Pacific's branch closures and 30 percent of Bank of America's occurred in neighborhoods which are 80–100 percent minority, while only 10 percent and 7 percent respectively of Security Pacific and Bank of America's closures took place in communities that have less than 10 percent minority populations. Charts which depict the results of this study are provided in Figures 10 and 11.

Bank of America officials defend the closures during the 1980's as "economic imperatives" to address "enormous competitive pressures" which required cost cutting measures. CAR does not dispute the fact that these were valid concerns at the time. What CAR does assert, though, is that these closures were conducted inequitably. This is evident from the data, but made even more clear by the experience of CAR members.

In 1988, when Bank of America closed the last bank branch in the Vernon-Central neighborhood of South-Central, they left a community with no banking services for a three mile radius. At the time, bank analysts estimated that the branch would require a deposit base of about $20 million to operate profitably. According to newspaper accounts, the cloned branch had maintained a steady $31 million dollar deposit base over the past seven years. Thus, the closed branch was very likely, very profitable.

The same year that the Central Avenue branch was closed, Bank of America opened a "Private Banking Center" in Beverly Hills for customers with a net worth of four million dollars and a deposit of one million. Access to the Center was by invitation only, and these privileged customers were provided with a complete range of free banking, investment, real estate, trust and other services.

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[1] "Taking it to the Bank: Poverty, Race, and Credit in Los Angeles," a report to the City of Los Angeles prepared by the Western Center on Law and Poverty, June, 1991.

Figure 10

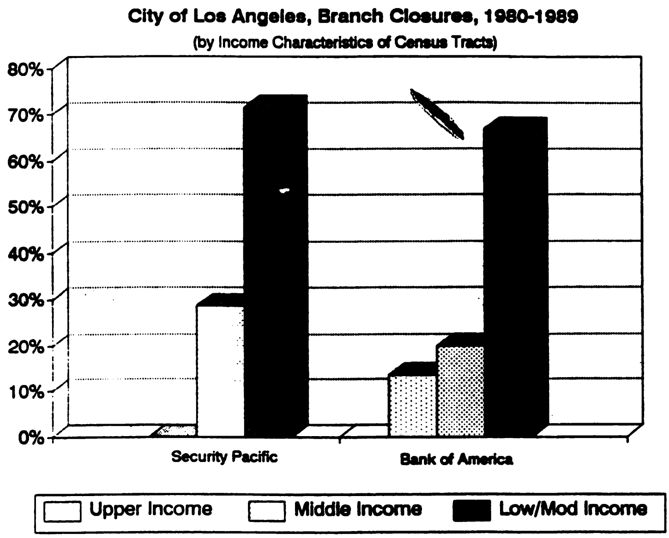
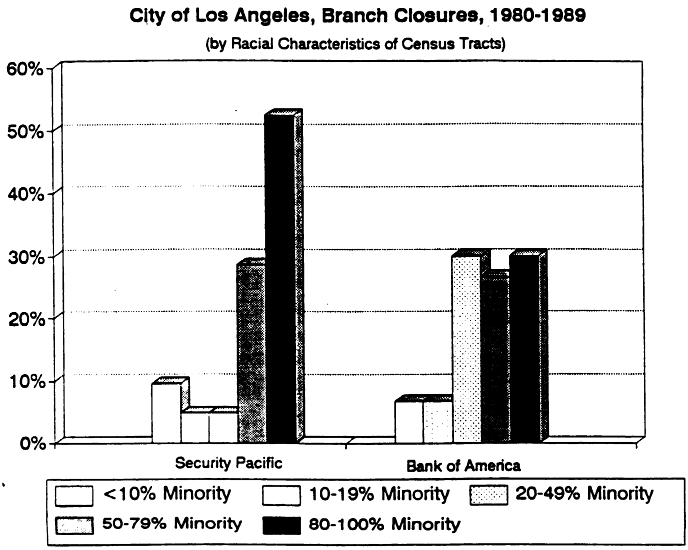

City of Los Angeles, Branch Closures, 1980-1989
(by Income Characteristics of Census Tracts)
80%
70%
60%
50%
40%
30%
20%
10%
0%
Security Pacific
Bank of America
Upper Income
Middle Income
Low/Mod Income

Figure 11


City of Los Angeles, Branch Closures, 1980-1989
(by Racial Characteristics of Census Tracts)
60%
50%
40%
30%
20%
10%
0%
Security Pacific
Bank of America
<10% Minority
10-19% Minority
20-49% Minority
50-79% Minority
80-100% Minority

Low-Income and Minority People Pay More for Financial Services

As bank branches are closed in low income and minority communities they are replaced by check cashing establishments. Today, according to a June, 1991 study by the Los Angeles Community Reinvestment Task Force, South-Central Los Angeles has 19 remaining bank branches and 133 check cashing establishments (See Figures 12 and 13). This means that check cashing businesses currently outnumber banks in the community seven to one.

Check cashing businesses are filling a service vacuum that has been created by banks which have abandoned inner city and rural communities—but not entirely. A basic bank account costs less than cashing two paychecks a month and buying five money orders to pay bills. Check cashing businesses also do not provide a safe place to keep money, opportunities to earn interest, or access to credit. Further, money order vendors that do business with check cashing establishments are not insured or protected as banks are. Last year, two L.A. money order companies went bankrupt and as a result the money orders that low-income people had purchased with cash to pay rent and utility bills simply bounced.

The Relationship Between Redlining and Predatory Lending

As we have seen, when banks pull branches out of communities, other businesses, such as check cashing establishments will jump in to serve the market. Similarly, when credit is not offered by conventional lending institutions, other businesses will take advantage of the market. For example, a 1989 study of mortgage lending in South-Central showed that only 3 percent of home loans were made banks, 35 percent by savings and loans, and the majority by mortgage and finance companies.[2]

Unfortunately, not all of these companies are reputable. Many unscrupulous lenders have a strong street knowledge of the data that I have presented today, and target the very credit starved communities that financial institutions have historically undeserved. The most insidious of these lenders are those who use fraudulent strategies to obtain the deed to unwary borrowers' homes. This form of predatory lending has increased three fold over the past several years in Los Angeles. It has undermined community stability by stripping low income and minority communities of their only wealth—the equity in their homes—and selling it to absentee owners who do not invest in the community's well-being.

Many of the victims of predatory lenders are the people who show up in the high denial rates for minorities that the Federal Reserve has discovered in its recent HMDA study. In Los Angeles, consumers who have been either denied loans by major lenders or whose historical experience has led them to believe that it is a waste of time to even apply, often end up as victims in equity rip-off scams.

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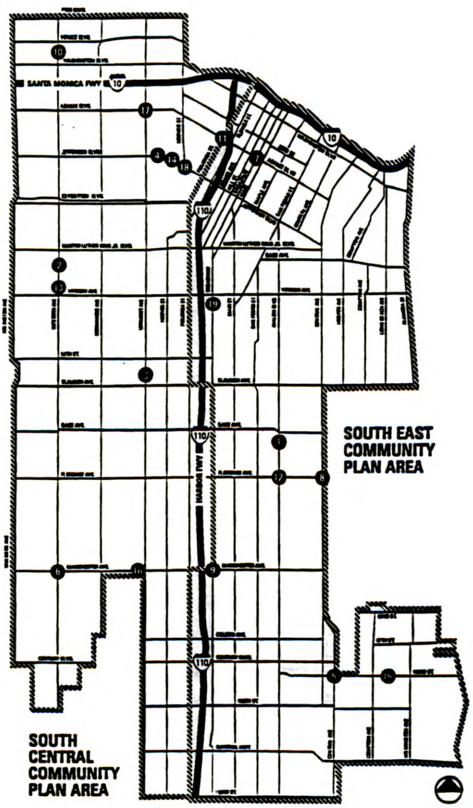
[2] Rzepinski David. South-Central Home Loan Study. Masters Thesis. UCLA Graduate School of Architecture and Urban Planning. June 8, 1989. The study area is bounded by Martin Luther King Jr. Boulevard on the North, Imperial Highway on the South, Van Ness on the West, and Alameda on the East. This area has been most heavily impacted by historic redlining in L.A. as well as by the recent civil unrest in the City.

CAR has found that banks that are reticent to lend in low income and minority communities are nevertheless willing to finance the companies that engage in unscrupulous practice in those same communities. For example, both Home Budget Loans and Metmor Financial are lenders who have been repeatedly sued by Legal Aid for their unfair business practices, improvident and unconscionable lending, and fraud. The owners of both companies have shared business interests and one has purchased past enterprises by the other. Research into Uniform Commercial Code documents filed with the Secretary of State's office shows that Home Budget Loan has received loans from Security Pacific and Metmor has received loans from Bank of America. It seems as though some of the worst offenders in predatory loan schemes have found it easier to get loans from major lenders than honest, working people who simply want to repair a roof or paint their house.

Figure 12

Banks and Savings & Loan Associations

in the Los Angeles Community Reinvestment Committee's South Central Demonstration Project Area:



Banks:

Bank of America

1. Industrial Branch
   6400 South Avalon Blvd. 291.053C
2. Martin Luther King Jr. Branch
   4103 South Western Ave. 291.0503
3. Slauson-Vermont Branch
   5700 South Vermont 291.0530
4. University Village Branch
   985 West Jefferson 291.0530
5. Watts Branch
   10340 South Central Ave. 291.0503
6. Western & 87th St. Branch
   8701 S. Western Ave. 291.0503

First Interstate Bank of California

7. Adams & Broadway Branch
   141 West Adams 614.3786
8. Florence & Central Branch
   1144 East Florence Ave. 589.6911

Security Pacific National Bank

9. Broadway & Manchester Branch
   8564 South Broadway 753.1721
10. 18th & Western Branch
    1819 South Western Ave. 734.9324
11. Figueroa & Adams Branch
    2703 S. Figueroa 746.1383
12. Florence & Avalon Branch
    501 E. Florence Ave. 753.3501
13. 43rd & Western Branch
    4277 South Western Ave. 294.6171
14. University Village
    821 West Jefferson Blvd. 746.4189

Savings & Loan Associations

California Federal Savings & Loan Assoc.

15. South Central Los Angeles Branch
    1601 East 103rd St. 564.5991

Great Western Bank

16. 1027 Manchester Ave. 852.3552

Home Loan Counseling Center

17. 1115 West Adams Blvd. 747.0807

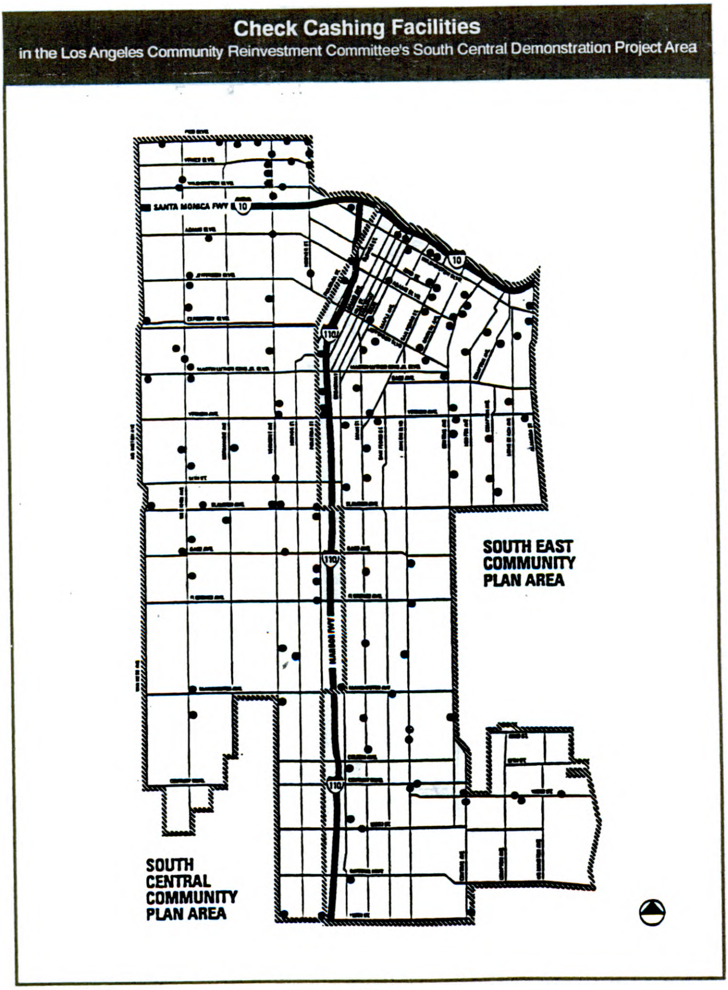
Western Federal Savings & Loan Assoc.

18. USC Branch
    3301 South Hoover 746.5727

Broadway Federal Savings & Loan Assoc.

19. 4501 South Broadway 232.4271

Figure 13


Check Cashing Facilities
in the Los Angeles Community Reinvestment Committee's South Central Demonstration Project Area
SANTA MONICA FWY
10
110
SOUTH EAST
COMMUNITY
PLAN AREA
SOUTH
CENTRAL
COMMUNITY
PLAN AREA

CRA, COMMUNITY VIGILANCE, AND IMPROVED BANK PERFORMANCE

When Bank of America closed the last branch in the Vernon-Central community in 1988, merchants and residents fought back by exposing Bank of America's poor lending record in L.A.'s historically Black communities and charging that the banks performance was inconsistent with the tenets of the Community Reinvestment Act. This pressure lead to discussions between the bank and the grassroots Concerned Citizens of South-Central L.A. organization. One result of these discussions was the development of the "Neighborhood Advantage Program," a first time homebuyers mortgage program which features lower downpayments and more flexible underwriting criteria. Neighborhood Advantage also targets low- and moderate-income census tracts. The program was piloted in South-Central Los Angeles. The program has been held out as a model of responsible banking practices by the bank's own public relations and it most likely contributed to Bank of America's "outstanding" CRA rating.

Concerned Citizens of South-Central Los Angeles is one of the founding members of CAR, which was formed in 1989. Last year, CAR revisited the Neighborhood Advantage Program, by investigating complaints by our members that Bank of America does not make home loans in their communities. To accomplish this, the service areas of five CAR member organizations, three of which are located in South-Central Los Angeles were delineated. 1990 census data on population and race were compiled along with HMDA data for the subject census tracts. Since Neighborhood Advantage is exclusively a home mortgage product, CAR limited its research to single family home loans. The results of the study are in Figure 14.

The only surprise to our membership was that the historically undeserved neighborhood represented by Concerned Citizens of South-Central actually received two mortgages from Bank of America. We later discovered that the real estate broker who facilitated the two loans is a staff member of Concerned Citizens, who is familiar with Bank of America's program only because of her relationship with that organization.

FIGURE 14

Bank of America
Home Purchase Loans in CAR Communities

Riverside, East Side
Population: 9,887
15% White
85% Minority
Total Home Purchase Loans: 0

Santa Ana, Civic Center Barrio
Population: 8,158
3% White
97% Minority
Total Home Purchase Loans: 0

Los Angeles, Ward EDC/Esperanza CHC
Population: 35,348
16% White
84% Minority
Total Home Purchase Loans: 0

Los Angeles, Concerned Citizens
Population: 63,346
1% White
99% Minority
Total Home Purchase Loans: 2 **$137,000**

Sources: 1990 Census—Bank of America HMDA data

CAR members felt that it was important to have a standard of comparison of the data regarding CAR communities. For this reason, Bank of America's mortgage lending in Encino, a large predominantly white, middle class neighborhood in the San Fernando Valley was also examined. The difference between Encino and CAR communities, shown in Figure 14, is substantial:

FIGURE 15

Bank of America Home Purchase Loans in Encino

Encino, Los Angeles
Population: 56,945
87% White
13% Minority

Total Home Purchase Loans: 61 **$25,286,000**

Sources: 1990 Census—Bank of America HMDA data

Thus in CAR communities, Bank of America made .17 home loans per 10,000 residents. In Encino, the bank made 10.7 loans per 10,000 residents, a ratio of *69 to 1.*

Prior to this study, CAR had just completed a year of negotiation with Security Pacific which began out of a contentious CRA challenge, but grew into a mutually beneficial relationship. By working together, three new products were developed, marketed and piloted—a first time homebuyers Program (Smart Start); a low cost checking account for people who receive government assistance (Basic Checking), and a series of related small business products for smaller and minority owned businesses (Business Advantage). There is no doubt in anyone's mind that these economically viable improvements to Security Pacific's community lending and service portfolio would never have occurred without the leverage provided by the Community Reinvestment Act. Further, the bank and the community alike were enriched, figuratively and literally, by the results.

However, soon after the agreement was completed, the acquisition of Security Pacific by Bank of America was announced. Although Bank of America made vague assurances that Security Pacific's commitments to CAR would be honored by Bank of America, later discussions with bank officials revealed that they were a lot less concerned about the details of our negotiated agreements than CAR members found acceptable. This uneasiness, exacerbated by Neighborhood Advantage's poor performance in our communities, the enormous disparities found in the market share analysis, and the threat of additional branch closures led CAR to file a challenge against the merger. In conjunction with Bank of America's application, the Federal Reserve Board held public hearings on issues relevant to the merger. In Los Angeles, City officials and community groups presented concerns regarding the banks performance to an overflow crowd. Although the merger was approved, the message from Los Angeles was clear—that despite B of A's outstanding rating, the bank had a strong need to improve its lending performance, particularly in minority and low-income communities.

Recently, in the wake of the L.A. riots, Bank of America has begun to show some improvement—offering, for example, a $25 million dollar loan initiative to businesses impacted by the civil unrest. And, the bank has begun to recognize that one reason that Neighborhood Advantage never performed in South-Central and other minority communities is because it had never been marketed in those communities. Today, South-Central billboards advertise the product, and Black newspapers carry Neighborhood Advantage ads.

According to Bank of America, these and others corrective efforts are beginning to pay off. While in 1991, Bank of America reported only 48 loans in South-Central Los Angeles, the bank claims that in the first six months of 1992 these figures have already been exceeded.[3]

Although this is hardly a staggering amount of loans from the nation's second largest bank to one of the largest minority communities in the country, the fact that concrete improvements are occurring is encouraging. But there is no way that these improvements would ever have been considered by the bank if Bank of America's "outstanding" CRA rating had exempted it from public scrutiny, or if CRA had been weakened or eliminated. They simply never would have occurred.

DISPARITIES BETWEEN REGULATOR AND COMMUNITY ASSESSMENTS OF CRA PERFORMANCE

There are three areas of frustration that most community activists face in their attempts to monitor and encourage enforcement of the Community Reinvestment Act. The first is the frequent gap between actual lending performance in our communities and the ratings made by regulatory agencies. The second is the fact that there are important areas, such as small business lending, in which good data is simply unavailable to substantiate community experience and knowledge. Finally, and perhaps most important, is the growing tendency of banks and regulators to institutionalize Community Reinvestment as a marginal aspect of the business of banking. Most bankers and regulators do not see CRA as central to the strategic business objectives of the bank. Instead, CRA is perceived as a side issue, analogous to corporate philanthropy. It is CAR's position that as long as community needs are a marginal aspect of the business of banking, the health of banks along with that of communities will be seriously jeopardized.

The Gap Between CRA Performance and Regulatory Ratings

The gap between real performance and regulatory ratings becomes obvious when we the CRA ratings of Bank of America and Great Western Bank are compared. As presented earlier, CAR's analysis of HMDA and other data found very large racial and income disparities in Bank of America's lending patterns in Los Angeles. Conversely, using the same methods and measures, CAR found that Great Western Bank's lending is entirely consistent

[3] L.A. Times. 9/8/92.

with the make-up of L.A. communities. Yet, both banks have identical, "outstanding" Community Reinvestment ratings.

Other problems occur when relevant data is not publicly available. For example, many banks make inconsequential numbers of home loans because they are primarily commercial lenders. Mitsui Manufacturers Bank (MMB), whose CRA record CAR (and other community organizations throughout California) has protested through a CRA challenge with the Federal Reserve; through an administrative complaint filed with the FDIC; and through picket lines in front of the bank insists that it is primarily a business lender. Thus, at minimum, MMB's CRA record should be evaluated on the bank's ability to serve the small business credit needs of its entire service community, including those of low income and minority neighborhoods. It is the experience of CAR's diverse constituencies that MMB does not make loans to businesses in our communities. In fact, of the nineteen community organizations from throughout the State of California which testified before the Federal Reserve at a hearing on the MMB application, all were critical of the bank. Nevertheless, MMB received a "satisfactory" rating from its regulator, the FDIC. Although the FDIC has never responded in writing to CAR's administrative complaint, CAR did meet with FDIC staff to provide input into two separate CRA examination processes for MMB. In our second meeting, the FDIC made it clear to CAR members that it understood that, in contradiction to our experience, MMB did make business loans to our communities. We knew that this was not possible, but we could not prove it.

In light of the outstanding ratings awarded to Bank of America and Wells Fargo, one would imagine that the Office of the Comptroller of the Currency would also insist that these banks do not have discriminatory lending patterns, also in contradiction to our experience. However, at least in this case, CAR can substantiate at feast one aspect of our experience—home lending—through an objective analysis of HMDA and other data that can be easily replicated by regulators as well as the bank.

With respect to business lending, community organizations like CAR are at a considerable disadvantage because there is no disclosure of business loan data by banks. Surveys of small businesses are few and far between and have generally resulted in very general, and thus less compelling, information. Finally, small businesses, for the most part, simply will not speak out because they are afraid of reprisals from the bank. This issue came up in the testimony of speakers at the MMB Federal Reserve hearing who were representing small business people from their communities.

It is CAR's experience that these fears are well-founded. CAR member organizations have been essentially blackmailed by banks which have been targets of CRA protest actions. CAR, however, is a political advocacy coalition whose mission is devoted to eliminating red lining and making banks more accountable to community needs. We recognize the divide and conquer strategies that banks have used to undermine our organization because we have experienced them before. CAR members understand the risks as well as the benefits of our struggle. Small businesses, on the other hand, are not political organizations and are struggling to compete with other small businesses. This well-founded fear of reprisals by banks keeps many small businesses quiet regarding their experiences.

We are also very concerned about regional disparities in evaluations and the implications that trends towards interstate banking have for community reinvestment. Analysis by the Las Vegas Alliance for Fair Banking of First Interstate Bank provides a useful example of the problem.

In September 1987, the Federal Reserve Board took the CRA record of First Interstate Bancorp's subsidiary banks into account in determining its position on First Interstate's application to acquire Allied Bancshares of Texas. Although the Board noted that First Interstate's subsidiary banks had satisfactory CRA ratings, it nevertheless required that First Interstate submit semi-annual reports on the progress of its subsidiary banks in implementing First Interstate's newly adopted corporate CRA policy statement as a condition of approval.[4]

Since the Federal Reserve Board's Order, the CRA ratings of First Interstate Bank subsidiaries in four states have dropped from satisfactory to "needs to improve" ratings.[5] In California, where First Interstate is headquartered, the bank has an "outstanding" CRA rating.

It would be very useful for this Committee, the Federal Reserve, and other regulatory agencies to further investigate the meaning of these disparities, as interstate banking trends accelerate. There are several possibilities. First, as many community activists suspect, First Interstate's outstanding California rating may be inflated in the same way that CAR asserts that Bank of America's outstanding California rating is. Secondly, it may also be the case, as suggested in the recent study by the House Banking Committee that the parent company is draining deposit dollars from First Interstate subsidiaries and that performance by those subsidiaries has consequently dropped.[6] If this is the case, then the diminished ratings may accurately reflect the negative community impacts of First Interstate's mergers and acquisitions.

What is definitely apparent, however, is that the CRA monitoring system failed. Between 1987 and 1990 semi-annual reports of CRA progress by First Interstate subsidiaries were to be submitted to the Federal Reserve. One would assume that feedback and intervention by regulators could have prevented the drop in ratings and/or performance. This clearly did not occur.

Marginalizing Community Needs

Since the inception of the Community Reinvestment Act fifteen years ago, it is hard to find major increases in lending to minority and working class neighborhoods. Data on lending inequities, such as that which I have presented today abound, as do newspaper ac-

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[4] Federal Reserve Board Order of September 28, 1987.

[5] Oregon (examination date: August 13, 1990); Colorado (September 30, 1990); Arizona (August 31, 1990); and Washington (January 7, 1991).

[6] "Analysis of Banking Industry Consolidation Issues," staff report to the Committee on Banking, Finance and Urban Affairs, House of Representatives, One Hundred Second Congress, March 2, 1992. This study found that 40 percent of the interstate operations of the 15 largest banks with substantial interstate banking activities had drained funds from communities in their host states. The report indicates that First Interstate Bancorp has operations in 11 satellite states and has drained funds from four of these states. The report does not indicate which four states these are, although it is very possible that they are the same states where First Interstate has received "needs to improve" ratings.

counts of loan rejection rates and their relationship to the quality of life of many Americans. While Community Reinvestment has been growing as a profession made up of regulators, consultants, and banking officials, its basic principle may be diminishing. That principle is that all credit-worthy individuals should have access to loans regardless of their race or class or of the race of class which predominates in the neighborhood where they live or own a business. That principle includes the idea that basic banking services and credit products—checking and savings accounts, consumer loans, home loans, small business loans—are for everybody, and not just the well-to-do.

Decades of disinvestment have created problems for inner city communities that simply cannot be addressed by conventional lending instruments. CAR has fought for underwriting criteria that more realistically assesses the credit-worthiness of low income and minority consumers, businesses, and homeowners. We also recognize that affordable housing projects have specialized lending needs which may be addressed by equity funds and lending pools. We understand that historical barriers to wealth in minority communities may be tackled with special entrepreneurial programs, micro-loans, and/or bank community development corporations. We respect these efforts, applaud their successes, and advocate for their expansion. However, we do not believe that these relatively small, specialized programs can substitute for the basic responsibility of banks to service their communities directly—by offering loan products which meet the needs of consumers, homeowners, and small businesses in minority and working class communities.

This is common sense. For example, Bank of America has provided construction loans to several of CAR members efforts to construct affordable housing at the same time it has neglected to invest in single family home and small business loans in the same communities, thereby undermining the impact of their own good program. A more effective community lending program would complement basic community needs with more specialized efforts such as investments in affordable housing or small businesses.

When lending institutions fatten their CRA program statements with participation in various intermediaries, multi-bank cdc's, and specialized community development banks *without also changing the basic way that they invest in communities at the branch level,* their overall impact on community lending will remain marginal. But there is evidence that regulators encourage and reward this very practice. Otherwise, how could banks with a marginal lending presence, and often minimal physical presence in minority and working class communities receive excellent CRA ratings? It is CAR's position that CRA ratings should judge the banks' overall performance in communities by using objective standards for measuring such performance.

CAR'S CRA PERFORMANCE SELF-EXAMINATION

In addition to developing mutual respect and trust, a major key to the success of CAR's negotiated agreements with Security Pacific was that on various occasions the bank-provided CAR with objective data that was not publicly available regarding loan loss ratios, loan sizes, and loan distribution so that discussions would be grounded in a common base of information. CAR's questions were often different than those that the bank asked of itself. Thus the bank's responses were sometimes as edifying to bank staff as to CAR. With this effective experience in mind, CAR has begun to request that discussions with other banks also be grounded in a common base of information.

To facilitate this sort of discussion with banks, CAR has developed a "CRA Performance Self-Examination" form, a copy of which is provided in Appendix A. The questions posed in the guide are indicative of the basic banking services and credit areas that are important to CAR constituents, and the charts provide simple ways to measure performance in CAR communities. The questions are also geared to elicit information about the specific products discussed in the bank's own CRA plan, testing performance by geographic area and number and amount of loans. CAR is in the process of distributing "Self-Examination" booklets to the 25 largest banks in L.A.

CONCLUSIONS AND RECOMMENDATIONS

In conclusion, it is CAR's position that any attempt to weaken CRA will undermine the health and future of our communities, as well as the long-term health and future of the nation's banks. It is our position that CRA should be clarified, strengthened, and vigorously enforced. A few recommendations toward these objectives are provided below:

a) A commercial lending disclosure requirement analogous to the Home Mortgage Disclosure Act should be established in order to assist in objective assessments of bank performance in small business lending.

b) Regulators should use consistent, objective standards in assessing CRA ratings of banks, such as the market share analyses presented above or the CAR's CRA Performance Self-Examination. These objective findings should be included in the public evaluation document.

c) Regulators should focus their assessments on performance rather than plans and closely monitor the results of plans. There needs to be more consistency and communication between regulatory agencies.

d) Regulators should require banks to repair past damage to communities caused by past and persistent patterns of discrimination. Banks that have historically not served minority and low-income communities are partially responsible for those communities' underdevelopment; the export of capital from those communities; and the proliferation of expensive and often disreputable financial institutions. The CRA programs of these banks should incorporate restitution to these communities. For example, regulators may require banks to implement careful and appropriate marketing and capacity building training as well as develop products which are designed to meet the needs of low-income communities which have been historically denied banking services. Or, as in the case of Bank of America and Security Pacific, when historic branch closures have been inequitably distributed, regulators may see that these banks have an affirmative obligation to open or re-open branches in underserved communities, using the consolidation process of a merger as an opportunity for a more equitable reorganization of resources. Finally, in many cases, such as South-Central Los Angeles, communities which have been abandoned or ignored by banks have struggled to develop their own community controlled financial institution. Financial support to these institutions by banks might serve as an alternative form of restitution.

e) Finally, equal treatment of financial institutions is an important prerequisite for effective community reinvestment. It is appalling that jumbo c.d.'s are protected by federal insurance and that money orders used by millions of low-income people are not. Across the country low income and minority communities are being served by financial service institutions that have different protections and regulations (in many cases, none at all) than banks do. As long as these are the primary financial institutions of low income and minority people, their unequal treatment results in unequal treatment of these populations.

Appendix A

CRA Performance Self-Examination

CRA
Performance
Self-Examination

This form will assist us in establishing the extent to which your bank is meeting the community credit needs of Communites for Accountable Reinvestment's grassroots constituencies. Census tracts and zip codes which define the specific geographic areas referred to in this form are provided in the enclosed "Community Definition Guide: Census Tracts and Zip Codes."

1. Please indicate the following information on the chart below by geographic area.

Geographic Areas	Number of branches currently in the area	Number of branches closed in area between 1980-1992	Number of branches opened in area between 1980-1992
Crenshaw			
East Los Angeles			
Encino			
Exposition			
Hollywood			
Koreatown			
Northridge			
Pacoima			
Pico-Union			
Riverside			
San Bernardino			
Santa Ana			
Vernon-Central			
Watts			
West Hollywood			

General Questions (cont'd)

2. Does your bank cash government checks for non-depositors at no cost?

Yes ______ No _______

Comments:

3. Has your bank invested in any community controlled and/or minority lending institutions? A community controlled lending institutions is one that has a democratic structure and non-profit structure, such as a community development credit union. A minority owned lending institution is one in which the majority of shares of the institution are owned by people of color.

Yes _____ No _____

If yes, please specify the institution, type of investment, and amount of investment below:

Name of institution, location	Grant	Deposit	Equity Investment

4. Please indicate on the chart below the number and percentage of women and people of color on your Board of Directors and in staff positions of Executive Vice President and higher.

	Women		African-Americans		Asian		Latinos		Other (please specify)	
	#	%	#	%	#	%	#	%	#	%
Board of Directors										
Staff positions: Executive V.P. and above										

5. Please indicate on the chart below the number and dollar amount of loans made directly to local congregations by area and year.

Geographic Areas	1989		1990		1991	
	#	$	#	$	#	$
Crenshaw						
East Los Angeles						
Encino						
Exposition						
Hollywood						
Koreatown						
Northridge						
Pacoima						
Pico-Union						
Riverside						
San Bernardino						
Santa Ana						
Vernon-Central						
Watts						
West Hollywood						

SPECIFIC QUESTIONS

The following questions have been designed specifically for BANK OF AMERICA.

BANKING SERVICES

6. Please indicate on the chart below the number of Limited Checking Accounts which have been opened by geographic area and year.

Geographic Areas	1989	1990	1991
Crenshaw			
East Los Angeles			
Encino			
Exposition			
Hollywood			
Koreatown			
Northridge			
Pacoima			
Pico-Union			
Riverside			
San Bernardino			
Santa Ana			
Vernon-Central			
Watts			
West Hollywood			

HOME LOANS

7. Please indicate on the chart below the number and dollar amount of Neighborhood Advantage loans originated by area and year.

Geographic Areas	1989		1990		1991	
	#	$	#	$	#	$
Crenshaw						
East Los Angeles						
Encino						
Exposition						
Hollywood						
Koreatown						
Northridge						
Pacoima						
Pico-Union						
Riverside						
San Bernardino						
Santa Ana						
Vernon-Central						
Watts						
West Hollywood						

HOME IMPROVEMENT LOANS

8. Please indicate on the chart below the number and dollar amount of home improvement loans that have been originated by area and year.

Geographic Areas	1989		1990		1991	
	#	$	#	$	#	$
Crenshaw						
East Los Angeles						
Encino						
Exposition						
Hollywood						
Koreatown						
Northridge						
Pacoima						
Pico-Union						
Riverside						
San Bernardino						
Santa Ana						
Vernon-Central						
Watts						
West Hollywood						

CONSUMER LOANS

9. Please indicate on the chart below the number and dollar amount of BASIC loans that have been originated by area and year.

Geographic Areas	1989		1990		1991	
	#	$	#	$	#	$
Crenshaw						
East Los Angeles						
Encino						
Exposition						
Hollywood						
Koreatown						
Northridge						
Pacoima						
Pico-Union						
Riverside						
San Bernardino						
Santa Ana						
Vernon-Central						
Watts						
West Hollywood						

STUDENT LOANS

10. Please indicate on the chart below the number and dollar amount of Student Loans made by area of the applicant's home or permanent residence and year.

Geographic Areas	1989		1990		1991	
	#	$	#	$	#	$
Crenshaw						
East Los Angeles						
Encino						
Exposition						
Hollywood						
Koreatown						
Northridge						
Pacoima						
Pico-Union						
Riverside						
San Bernardino						
Santa Ana						
Vernon-Central						
Watts						
West Hollywood						

BUSINESS LOANS

11. Please indicate on the chart below the number and amount of WORKING CAPITAL LOANS FOR MINORITY BUSINESSES that have been originated by area of the site where the loan is to be used and year.

Geographic Areas	1989		1990		1991	
	#	$	#	$	#	$
Crenshaw						
East Los Angeles						
Encino						
Exposition						
Hollywood						
Koreatown						
Northridge						
Pacoima						
Pico-Union						
Riverside						
San Bernardino						
Santa Ana						
Vernon-Central						
Watts						
West Hollywood						

Business Loans (cont'd)

12. Please indicate on the chart below the number and amount of SMALL BUSINESS ADMINISTRATION LOANS that have been originated by area of the site where the loan is to be used and by year.

Geographic Areas	1989		1990		1991	
	#	$	#	$	#	$
Crenshaw						
East Los Angeles						
Encino						
Exposition						
Hollywood						
Koreatown						
Northridge						
Pacoima						
Pico-Union						
Riverside						
San Bernardino						
Santa Ana						
Vernon-Central						
Watts						
West Hollywood						

13. Please indicate on the charts below the number and amount of conventional small business loans that have been originated by area of the site where the loan is to be used, by size of loan, and by year..

	1989									
Geographic Areas	$<10,000		$10,000-$24,999		$25,000-$49,999		$50,000-$99,999		>$100,000	
	#	$	#	$	#	$	#	$	#	$
Crenshaw										
East Los Angeles										
Encino										
Exposition										
Hollywood										
Koreatown										
Northridge										
Pacoima										
Pico-Union										
Riverside										
San Bernardino										
Santa Ana										
Vernon-Central										
Watts										
West Hollywood										

Business Loans (cont'd)

	1990									
Geographic Areas	$<10,000		$10,000-$24,999		$25,000-$49,999		$50,000-$99,999		>$100,000	
	#	$	#	$	#	$	#	$	#	$
Crenshaw										
East Los Angeles										
Encino										
Exposition										
Hollywood										
Koreatown										
Northridge										
Pacoima										
Pico-Union										
Riverside										
San Bernardino										
Santa Ana										
Vernon-Central										
Watts										
West Hollywood										

Business Loans (cont'd)

	1991									
Geographic Areas	$<10,000		$10,000-$24,999		$25,000-$49,999		$50,000-$99,999		>$100,000	
	#	$	#	$	#	$	#	$	#	$
Crenshaw										
East Los Angeles										
Encino										
Exposition										
Hollywood										
Koreatown										
Northridge										
Pacoima										
Pico-Union										
Riverside										
San Bernardino										
Santa Ana										
Vernon-Central										
Watts										
West Hollywood										

14. **Please use the space below to let us know about any other lending programs or services that your bank offers that have had an important impact on the geographic areas that are the subject of this self-examination.**

TESTIMONY OF JAMES FLETCHER
PRESIDENT OF THE SOUTH SHORE BANK OF CHICAGO

SEPTEMBER 15, 1992

Honorable Chairman and Members of the Subcommittee:

I am Jim Fletcher, President and CEO of South Shore Bank in Chicago, Illinois. I also serve as one of the four-member Management Committee of Shorebank Corporation, the parent company of South Shore Bank.

It is my understanding that South Shore Bank was the only bank in the country to testify in favor of the Community Reinvestment Act prior to its enactment in 1977. It is, therefore, with great pleasure that I return today to reiterate our bank's support for CRA as well as to provide you with an overview of the impact of CRA on neighborhoods such as those in which we work. I will argue that not only should Congress continue to support vigorously the 1977 Community Reinvestment Act, but it should also consider the public policy benefits of enhancing the capacities of community development banks in our country.

HISTORY & CORPORATE STRUCTURE

South Shore Bank is a community development bank located on the south side of Chicago. With almost $225 million in assets, the bank targets five minority communities on Chicago's south and west sides for its development lending efforts.

Since the current ownership and management bought the Bank 19 years ago in August 1973, we have made over $220 million in loans in those targeted communities. Through our subsidiary and affiliate companies, we have leveraged an additional $100 million in economic development finance.

South Shore Bank is the architect and perhaps best known practitioner of community development banking. Its Shorebank parent holding company is in the business of rebuilding underinvested communities. That is, neighborhood development is our corporate mission. To achieve that central purpose, it owns an insured depository institution and has several proactive community development subsidiaries and/or affiliates. (The Shorebank organization chart is found on page 26 of the 1991 *Annual Report,* attached herein.) South Shore Bank has one branch in the Austin neighborhood on Chicago's west side and, in June of this year, opened a loan production, venture capital and technical assistance office for small business development in the Upper Peninsula of Michigan.

Through our consulting group, Shorebank Advisory Services, we are working on applications of the Chicago model in several midwestern cities and in Portland, Oregon. We regularly receive calls and visits from public and private entities across the U.S. requesting help in designing effective community development initiatives, including development banks. In addition, at the request of the Polish-American Enterprise Fund, we have designed and continue to manage a small business lending program in Poland. Through that contractual arrangement, we operate in a dozen cities around Poland.

With our sister organization in Arkansas, Southern Development Bancorporation organized in 1988, we continue to define the community development bank model and to test its capacity as a vehicle for the renewal of underinvested communities. To our knowledge, the Self Help Credit Union in North Carolina is the other development bank in the country attempting a comprehensive approach to this issue. At this point, we know that a community development bank is a financially self-sustaining institution that is able to have broad community reinvestment impact. The success of South Shore Bank in the past two decades has demonstrated that community reinvestment lending is possible, profitable and effective in revitalizing underinvested communities and in igniting market forces in those same communities ignored or abandoned by more conventional financiers.

COMMUNITY REINVESTMENT & CRA

South Shore Bank initiated its reinvestment lending prior to the passage of the CRA. The Shorebank blueprint dates to 1972 when the holding company was incorporated. It continues to expand its community reinvestment activities, not out of pressure to comply with CRA, but because community reinvestment is our business.

As I review the history of CRA, I am struck by how much time, discussion and effort has gone into the process of defining compliance, monitoring the effectiveness of the regulators in enforcing the law and documenting individual lender efforts. I am also struck by how many banks or savings and loan associations continue to view CRA and community reinvestment as a burden rather than as an opportunity.

"Development" loans at South Shore Bank are market rate, unsubsidized credits make within the Bank's target neighborhoods. Their purpose is to accrue to the long-term economic development of those areas and their residents. As such, development lending falls into the categories of Commercial, Community Organization, Multi-Family, Home Improvement, and Education. Loans made by South Shore Bank to residents and local entrepreneurs to rehabilitate housing, finance businesses, buy or repair homes and support non-profits meet the credit needs of low- and moderate-income people. Further, South Shore Bank's designated lending areas are neighborhoods that other lenders have considered or continue to consider risky. While our borrowers may appear to be unsophisticated, they have proven to be extraordinarily creditworthy. We routinely use the U.S. Small Business Administration guaranteed loan and FHA Title I Home Improvement loan programs to reduce our risk and to help qualify more borrowers. Our success in demonstrating how underinvested communities can, over time, become prudent lending areas and profitable markets has attracted other lenders to our target communities.

Let me illustrate our reinvestment efforts with one loan product, single family home mortgages. When current management bought the Bank in 1973, single family homes in South Shore had been declining in value for the prior decade, and, precipitously so since the mid-1960's. The area had been redlined by banks and savings and loans due to rapid racial change that occurred between 1965 and 1972. New Bank management recognized the value of the solid, gracious homes in the area and established single family home mortgages as one of its lending priorities. Between 1974 and 1980, South Shore Bank made approximately $32.7 million in home mortgages in South Shore. As a result, home values increased faster in South Shore during this decade than any other community in Chicago, and other lenders began to make home mortgages in the area.

By 1980, South Shore Bank had significantly reduced its single family mortgage lending in South Shore because the private market for credit was once again functioning. This decision has proven to be correct. According to Home Mortgage Disclosure Act data, other banks, savings and loan associations and mortgage companies made 231 home mortgages totaling $13.9 million in South Shore in 1990. As early as 1976, we began turning our attention to a different severely underserved market, multifamily mortgage loans. We continue to focus on financing the purchase and rehabilitation of such multi-family properties—perhaps the simple most important category of lending for South Shore Bank in terms of development and profit over the past 14 years.

In 1986, South Shore Bank opened a branch in Austin, a community on the west side of Chicago that had experienced serious deterioration due to disinvestment for well over 20 years. Once again, we led the way with conventional single family mortgages to meet a severely underserved market. As our HMDA statement reports, in 1991, South Shore Bank originated 82 conventional single family home mortgages in Austin totalling almost $5 million. While it is too soon to assess the impact of this lending, we have confirmed over the past five years that there are, indeed, qualified borrowers, a good housing stock and a need for credit.

Despite the perception of many bankers that reinvestment lending is risky and unprofitable, the experience of South Shore Bank demonstrates that these perceptions are inaccurate. With the exception of one year over the last ten, the Bank has consistently achieved a return on assets in excess of .80 percent as well as double digit returns on equity. The Bank's 1991 net losses of .67 percent on a $142 million year-end loan portfolio continue an eight-year trend of outstanding performance. In fact, South Shore Bank has met or outperformed its peer group banks on loan losses for the past several years (see FDIC Uniform Bank Performance Report for banks of comparable size, i.e., $100–$300 million in assets with 3 or more offices, and located in a metropolitan area).

I do not mean to imply that reinvestment lending is either easy or as profitable as other loan markets. South Shore Bank's transaction costs are higher due to the time and effort required to work with less sophisticated borrowers and to book smaller loans. (Our average loan size is approximately $150,000.) The impact of our lending is also significantly enhanced by the development activities of our non-bank subsidiaries; and the Bank upstreams much of its earnings so that the parent company can pursue expanded economic development initiatives.

However, we were pleased that other lenders gradually recognized the market potential of single-family mortgage lending in South Shore. A few also compete with us now in the multi-family market. We believe there are ample opportunities for other lenders to make loans in the neighborhoods we have targeted and in other underinvested neighborhoods in Chicago, as well as in urban and rural areas across the country.

Unfortunately, making loans in underinvested communities is not a priority for most banks. The Community Reinvestment Act and effective enforcement of this law is one of the most critical resources available to low- and moderate-income communities. In Chicago alone this law has produced CRA loan commitments totalling over $300 million. Through discussions with nonprofit organizations, Chicago banks realized the need for first mortgages for larger multi-family buildings in city neighborhoods, and there is now an active lending market for the acquisition and rehab of these buildings. A similar process led to the creation of loans for mixed-use buildings that have both residential and commercial space. Without CRA, these loans would not be available today, and many Chicago banks would not be the active lenders they are in the city of Chicago.

RECOMMENDATIONS

It is important that the Community Reinvestment Act continue to offer low- and moderate-income and minority communities protection from being dismissed or forgotten by banks in their rush to pursue the biggest and fastest profits—profits which, as we have seen to our peril, often prove not only short-lived but in many cases, extraordinarily costly. We must continue to be vigilant so that enforcement of the law does not focus on counting unimportant factors and present an expensive bureaucratic burden that falls heavily on smaller banks. The spirit and the letter of the Community Reinvestment Act is that the public privilege of banking must be accompanied by the responsibility to meet community credit needs. I do not believe that Congress intended this to mean that banks should spend an inordinate amount of time and money studying community credit needs and documenting their efforts to talk with community residents. Congress' intent—in 1977 and now—was clear: it is a bank's responsibility to make loans and to service the credit needs of the community(ies) in which it operates.

Finally, I want to reemphasize that it is not difficult to seek and find credit-worthy borrowers in low- and moderate-income neighborhoods. And it is even less difficult to seek and find credit-worthy minority borrowers of every income level. However, it is difficult to achieve long-term community development in underinvested communities. Most regulated financial institutions have the capacity and may have the desire to engage in the development process in communities that lack the resources to attract sufficient private sector development. At the same time specialized financial intermediaries such as community development banks are uniquely qualified to serve as a model for the broad-scale, long-term development that can make a difference. Congress should, therefore, do two things: 1) continue to support and strengthen the Community Reinvestment Act; and 2) examine ways to provide the capital needed to create and sustain these specialized financial institutions. This could include encouraging banks to invest capital in community development banks as one of the ways they meet their CRA responsibility. Thank you very much.

TESTIMONY OF JULIA F. JOHNSON
VICE PRESIDENT, CRA–BANC ONE CORPORATION
THE COMMUNITY REINVESTMENT ACT

SEPTEMBER 15, 1992

Chairman Cranston and members of the subcommittee, thank you for the opportunity to appear before you today. I am Julia Johnson, Vice President of Community Reinvestment for BANC ONE CORPORATION. BANC ONE is a multi-bank holding company with $48.4 billion in assets as of June 30, 1992. We operate 57 banks with 887 offices in Indiana, Illinois, Kentucky, Michigan, Ohio, Texas, and Wisconsin. I have the benefit of working to encourage and evaluate the Community Reinvestment Act ("CRA") programs in each of these 57 independently chartered banks and I have the good fortune to share my experience with this committee. Our banks range in asset size from $62.9 million to $13.1 billion. Some of our banks serve rural areas and some serve large metropolitan communities. Some BANC ONE communities have a wealth of resources and local community-based development expertise. Others have little or none.

I would like to state at the outset of this hearing that BANC ONE interprets the Community Reinvestment Act ("CRA") as a mandate to make our country's banking system work for everybody—everyday. Making it work means focusing on business. Our success rests on our ability to profitably offer appropriate products which are accessible and affordable. CRA is our business. To the extent that the Federal Government believes community reinvestment is so important as to require the regulation of our business, it is inconceivable to us that any institution could be granted exemption.

The mandate of CRA requires financial institutions to creatively and aggressively pursue business opportunities. Notwithstanding, the history of banking and the anti-competitive restrictions imposed on the industry in the past have created a legacy which is antithetical to the mandate of CRA. For this reason, many institutions will regard CRA as a burden not an opportunity. Institutions which are burdened by CRA seek exemptions and "safe harbour." I believe we have safe harbour today. It is the harbour of continuing effort and tide profitable exploitation of market opportunity in low and moderate income communities.

There has been much talk of discrimination in the past year and there will certainly be more as the new Home Mortgage Disclosure Act ("HMDA") data is released. It would be naive to think that any industry is free of discrimination. I believe that discrimination exists any place where people of diverse origin are gathered together. Certainly, it is not a condition unique to banking. Nevertheless, I am very concerned with how this issue is being debated. Bankers will tell you that they do not discriminate and that HMDA data do not provide evidence of discrimination. Bankers will tell you that there are more than enough equal credit opportunity regulations and consumer compliance examinations to prevent or uncover acts of discrimination. If these industry assertions are true, why do the HMDA data reflect disparities in lending patterns?

In my experience, the greatest barrier to the equitable distribution of credit is perceived profitability. If lenders have a bias, it is against making small loans. To the extent women and minorities represent much of the low and moderate income segment of the population, they seek credit in smaller amounts than middle and upper income customers. More often than not, this business is not considered desirable. The costs of banking have increased and the ABA has put a price tag on regulatory compliance at 59 percent of profits. Ironically, as bank profits continue to be eaten up by compliance costs, financial institutions accelerate their efforts to make larger loans with bigger profit margins. The situation gets worse—not better.

If banks thought small loans made economic sense, they would do whatever necessary to facilitate their extension. Banks would have no minimums on consumer credit; they would market home improvement loans instead of dream vacation loans; they would open more branches in low and moderate income neighborhoods and they would have an incentive to regularly review underwriting criteria to ensure maximum flexibility. Isn't this what CRA is all about? In short, many lenders believe CRA doesn't make sense from a profitability standpoint. That is the prejudice and that is precisely why we need CRA.

Subsequent to the enactment of the Financial Institutions Reform Recovery Enforcement Act (FIRREA) a great deal of information has been made available. Geocoding activities and HMDA reporting have provided a wealth of data. Most banks are overwhelmed and many are struggling to make sense of the data which they have. This is not an exact science and there are as many ways of interpreting the numbers as there are geocoding consultants. Everyone is having difficulty—even the largest institutions. Small banks located outside of Metropolitan Statistical Areas are being asked to undertake an extraordinary amount of effort to create geocoded reports which are, more often than not, a waste of time.

Lost in all of the confusion of geocoding has been the reason for why we do it. Regulators want it so they can hang their hat on something tangible when they issue an examination report. Certain community groups want the data because they believe the standard of equitable distribution of credit means credit allocation. Most lenders don't want it and don't use it because they do not perceive it adds value to doing business. The situation has become terribly politicized such that governors and mayors now want data in customized reports which they, in turn, evaluate to see if their community got its 'fair share.' Regulated financial institutions stand in precarious balance between private enterprise and public utility. I believe that the current CRA environment has upset the balance in favor of the public utility. We must restore some balance. Collecting more data is not the answer.

Why should banks collect data? How much data should be collected? Who should interpret its meaning? Financial institutions are commonly regarded as numbers-oriented institutions. The man on the street might naturally assume that market penetration numbers, application and denial data, or exhaustive loan to deposit ratio reports are routinely generated and manipulated in the banking business. Prior to FIRREA this was not the case. The history of geocoding is a very brief one dating back to 1989. Today all banks are struggling to create statistical reports—many do so manually. Yet very few financial institutions utilize the data for strategic planning. CRA means using information to identify market opportunity; to direct resources for the profitable exploitation of market opportunity and to measure success within the context of the bank's business environment.

Banks should collect data because it has strategic value. Enough data should be collected as provides value and relevance. The bank should interpret the meaning of the data in terms of its business plan. I have observed that some banks have been required to geocode out of market lending activity despite having high loan to deposit ratios with the vast majority of loans having been made inside the delineated market. I have observed that many banks have been asked to track and geocode loan application activity for all products despite the fact that market penetration data may not indicate credit distribution problems.

In desperation or frustration, some banks throw money at lending consortia hoping that, if market penetration in low and moderate income communities is poor, the bank's contributions to some other lending entity may deflect criticism. When HMDA data are released, these organizations are quick to point out that the HMDA report is not a true indicator of their lending activity. As lenders flock to delegate low and moderate income consumer lending to external organizations, the banking system becomes more dysfunctional for this segment of the population.

CRA can and does work. Everyone should give it a chance but it seems no one—not Congress, not the regulators, the advocates or the bankers are willing to do so. It took a little time to come to grips with FIRREA and the revised examination procedures. The HMDA data provide valuable information even though it will take some time before we can all agree on how it should be interpreted. It will take time for banks to utilize HMDA as a strategic planning tool but they are moving in that direction. Now is not the time to impose additional data collection requirements, including the ill-conceived requirements of the Federal Deposit Insurance Improvement Act. Nor is this the time to create safe harbours or grant exemptions.

We have been asked to address the role of CRA in providing access to capital for all members of the community. I have stated BANC ONE's belief that CRA means making our banking system work for everybody each and every day. To the extent that banks have not or cannot safely and profitably grant credit or provide services, other institutions may have taken our place. This is as true in the low and moderate income community as it is in upper income neighborhoods. Unregulated consumer finance companies provide one means of access to capital and credit unions have always been significant competitors. Without the significant costs of regulation, these institutions are able to obtain more profit from small loans. Similarly, upper income consumers are often times better served by borrowing against margin accounts at the brokerage companies.

It is difficult to determine the extent to which segments of the community may lack access to capital. Regulatory reports from banks may provide some information but there is no context within which to consider them. They certainly cannot and should not be used as the only yardstick to measure credit availability for low and moderate income people or minorities. What then is the role of CRA in providing access to capital? CRA requires banks to lend money. CRA should provide the incentive to banks to work aggressively and creatively to ensure that the lending is both safe and profitable. That is different than saying that all banks should be all things to all people. That is different from saying all banks must have branch facilities in low and moderate income neighborhoods or that they must provide venture capital for small business start-ups. CRA means that a bank can't arbitrarily decide to offer some products to some people and delegate the rest of the business to another entity when they perceive profitability to be poor.

CRA is business at BANC ONE. It ought to be viewed that way in the Congress and in the community. Legislative proposals should facilitate business not inhibit it. All the data in the world won't create a venture capital fund for minority and female small business development. Geocoding small business loans won't enable banks to offer long term fixed rate commercial credit. HMDA hysteria shouldn't be a mandate for more data until we come to agreement on the meaning of what we have.

CRA works at BANC ONE because we make it work. Our strategic CRA plan is our business plan. I hope that any and all legislative proposals to modify, expand or limit CRA will be viewed in this context. If you do, you will not needlessly add to our cost of doing business. You will not encourage us to delegate our lending responsibilities. You will not ask Government regulators to allocate credit or micro manage our company. You will not be inclined to grant exemptions.

Thank you for this opportunity to participate in your review. I will be happy to respond to any questions you may have.

STATEMENT OF CALVIN BRADFORD
PRESIDENT, COMMUNITY REINVESTMENT ASSOCIATES
"WE TRUST OUR BANKS"—15 YEARS AFTER THE CRA

SEPTEMBER 15, 1992

My name is Calvin Bradford. I thank you for the invitation to address the Subcommittee on Housing on issues that are critical to the future of lower-income, minority, rural, and inner-city communities in our country. Today we struggle to work our way out of a deep recession and to find the resources to rebuild from the riots in Los Angeles and to avoid the consequences of riots in many other communities teetering on the brink of financial collapse. In this context, we need to take this time here to reflect on the role of the Community Reinvestment Act and the larger policy statement that it makes with regard to or response to the needs of these kinds of communities.

Access to capital and credit is the engine that drives our free and capitalistic economy. Indeed, it is the engine that drives all developing economies. But today, as Congress reviews bill after bill to strip the Community Reinvestment Act of its powers, we have to ask ourselves if we care more about the economies of Poland, the former Soviet Republics, our North and South American neighbors, or almost any developing nation of the world than we do about our own inner-city and rural communities in America. So fundamental is the role of capital and credit to the development of any economy that it is the first resource we put together after emergency relief for food, medical care and temporary shelter. The internationally recognized measure of our commitments to other nations is our willingness to participate in the provision of capital and credit though direct loans and loan guarantees and through efforts to support programs of the Work Bank and the International Monetary Fund. When we seek to help Poland, for example, we encourage programs to provide capital, credit, and investment services from the World Bank to the services of the South Shore Bank in Chicago.

But, if these are the measures of our commitments to rescue and advance troubled foreign economies—and thus to provide a sound economy upon which democracy can grow to its full potential—how do these measures reveal our domestic commitments to the third world economies in our own cities and rural communities? The thrift industry that was created in the 1930s to provide capital and credit to our local communities as a means of building our way out of the Great Depression has now been encouraged by bad policies, poor regulation and deregulation to abandon its community roles and speculate on junk bonds, commercial real estate investments, and high income housing developments. The savings of people in existing communities, older communities, and poorer communities were siphoned off and used for the personal benefit of wheeling and dealing banking tycoons and investors. Commercial banks have too frequently also followed paths of investments in real estate investment trusts, high risk commercial real estate, junk bonds, energy industry speculation, and foreign lending that served the personal greed of the corporate officers more than the fiduciary responsibilities owed to the depositors or the lending needs of our local communities.

While economists at the World Bank pointed out the need to develop special programs to insure the flow of capital and credit to third world economies, economists at the Fed (and even the Chairman of the Fed) lauded the diversion of funds from the savings of families and individuals in lower-income, declining economic areas to areas of high growth and speculation as the efficient operations of a natural market channeling money to the areas of highest demand. When these false markets collapsed of their own weight, the taxpayers whose Government had guaranteed the flow of funds to the banking industry by insuring the deposits of these financial institutions were left to bear the costs of bailing out the fools and felons who ran these institutions into the ground under the watchless eyes of the Federal agencies charged with protecting the public interest.

For all Americans, the hundreds of billions of dollars that have been and will be committed to this effort represent critical resources lost to rebuilding our national economy, our health systems, and our educational systems, and our systems of safety nets. For the people who live in the inner-city, minority, and rural communities which suffered from redlining and disinvestment while their personal savings were poured into these unconscionable get-rich-quick schemes for overpaid banking and investment executives, there is a threefold penalty. They suffered once when their communities were disinvested. They suffer a second time as they have to pay for the bailout. They suffer a third time because the costs of the bailout limit the ability of the Government to respond to the present economic needs—some of which are caused by the original cycle of disinvestment itself.

If there is any real gold to be found in our domestic banking policy, it is found in the energy, creativity, and determination of the very community people who have suffered the most from the cycles of redlining and speculation. The Community Reinvestment Act, the Home Mortgage Disclosure Act, and over $30 billion in reinvestment programs and agreements came from the people in the disinvested communities. I began my own work in disinvestment, reinvestment, and lending discrimination 20 years ago just as the community movement against redlining and disinvestment reached a national scale through the founding of the National People's Action in 1973. With my statement today, I have prepared and made statements on disinvestment, reinvestment, and fair lending 10 times before Senate committees, House committees, and hearings by HUD and the U.S. Commission on Civil Rights. Over that time, whatever the scope of new research and new information or experiences, the analysis I have provided has remained substantially the same:

- The Community Reinvestment Act is the only law that places an obligation on American financial institutions to serve the economic needs of American communities.
- The banking industry has consistently opposed this responsibility in favor of policies and practices that support speculative investments that have consistently resulted in huge losses.
- Where lenders have made thoughtful and sincere commitments to reinvestment, these efforts have provided lending opportunities that typically perform as well, or better, than the remaining portfolio of these lending institutions.
- The Federal agencies charged with the enforcement of the Home Mortgage Disclosure Act, the Community Reinvestment Act and fair lending laws have provided a legacy of neglect and even wholesale abuse of their responsibilities.
- Community-based organizations—that have no statutorily defined roles or obligations to enforce these laws—have been left as the major enforcement agencies. They have even been criticized by regulatory agencies when they fail to perform tasks that are the specific—statutory—obligations of these regulatory agencies.

As I come before you today, there is only one modification I can make to these historical patterns—**things have gotten worse**—and Congress has become involved in the efforts to undermine the implementation of the Community Reinvestment Act. In the past two years, the bogus issue of regulatory burden has been used to advance efforts to gut the CRA—to exempt over 80 percent of all lending institutions based on their asset size—and to shelter the vast majority of all remaining institutions from challenges and other CRA obligations by using the shoddy record of CRA public evaluations as a defense against community efforts to secure reasonable and responsible access to credit from the Nation's larger lenders.

Based on the international measure of our Nation's commitment to economic growth (programs to assure access to capital and credit) only the Community Reinvestment Act stands between the needs of our economically depressed and minority communities and virtual abandonment of these communities by the Nation's banking industry. Whatever significant level of reinvestment exists today exists because of this Act—and in spite of all efforts of the banking industry and the regulatory agencies to undermine its goals and free our banking system from all obligations to serve the American people. The Community Reinvestment Act is the only force that stands between the needs of our communities and the efforts of the regulatory agencies and the major banking institutions to sacrifice these needs to the goal of building a huge, internationally oriented banking system for the personal interests of the officers and stockholders of the institutions. This new banking system will belong to the giants who survive the wars of mergers and consolidations—wars that will eliminate thousands of jobs in the financial service sectors and which (by existing evidence [1]) seem destined to increase both local disinvestment and the costs of lending and banking services to consumers.

It was not just humorous, but a cruel irony, when President Bush blamed the War on Poverty programs for the riots in Los Angeles. Over the past two decades there has been a quiet revolution at the community level. Where community organizers once organized to gain access to everyone's share of Government programs, they now organize to gain access to the resources to build working private economies. Far from seeking to survive on the Government dole, community organizations and thousands of community-based development organizations have advocated solving their long-term economic problems by turning to private sector partnerships for reinvestment—often specifically seeking to ameliorate the consequences of Government programs such as FHA, whose dominance of the market undermines the role of the private economy in their communities. Indeed, it was the reinvestment movement—not the Government or the private sector—that initiated the original "public-private partnerships" for reinvestment with lending institutions long before that phrase became a fashionable mask for Government programs that have reduced Government support for housing and economic development.

The reinvestment philosophy is essentially a conservative philosophy both in the economic and literal sense. It is designed to preserve and rebuild existing communities—and the economic options for the people who live in them. It seeks to use the creativity, inventiveness, individual initiative, and private capital of our free market capitalistic economy. Its only radical aspect is in its commitment to these conservative principles as a means of allowing people to save their own communities and rebuild their own lives. The reinvestment movement recasts the role of Government from one of maintenance programs to one of investment programs. While the movement would like to see more funding of Government investments to leverage private investments, the key resource of the movement is an act that costs the Federal Government not a single penny—the Community Reinvestment Act. The Act requires that in return for the market advantages of depository insurance and regulation against over competition these institutions serve the "convenience and needs" of their local communities. It is, indeed, a cruel irony and a betrayal of the people in our inner-city, minority, and rural communities that have accepted the private sector ideology, that the Bush Administration now adds its own bill to gut the CRA (a bill with the sadly ironic title of "The Credit Availability and Regulatory Relief Act").

While I am prepared to answer questions about any of the 10 issue areas listed in the invitation to appear before this committee, I will limit the remainder of my statement to 5 issues:

- The quality of the public CRA ratings;
- The alleged regulatory burden of the CRA;
- The need for improved and additional disclosure;
- The persistence of race discrimination; and
- The powerful but dangerous drugs of FHA and VA lending.

In responding to these issues, I have attached to my statement a selection of documents that provide detail and background to many of the main points. I have tried to select a few poignant examples in each issue and to suggest in the support papers the larger range of studies, resources, examples, and information that has been collected over the years. Even with these added resources, my statement only skims over the full range of examples and evidence to support the points I will make. The Subcommittee staff has endeavored to assemble a larger body of redlining and disinvestment studies and other works related to the topics you seek to address. In addition, there are many organizations and individuals who have been asked to submit written statements for the record. Hopefully, the personal statements that we make today will convey the range of concerns and issues that are reflected in this larger collection of written statements, research, and policy papers.

1. The Quality of Public Ratings

The effort to secure better CRA compliance by providing that the CRA ratings be made public has been of little value. Statistically, about 97 percent of all covered institutions received passing CRA grades prior to the public ratings. Reviews of the public ratings reveal that the new system has reduced the number of institutions with passing grades to about 90 percent. This seems a marginal improvement in enforcement when compared to the problems created by this public rating system. First, these ratings have revealed the huge levels of inconsistencies and sloppy and ineffective regulatory effort that had always been assumed in the rating process before it was made public. Second, it has been the fear of these ratings by the lending industry that has been the driving force behind the effort to gut the CRA. Thus, the ratings have become a rallying point for industry opposition to the real goals of the CRA. Ironically, because the ratings still pass 90 percent of all lenders with flying colors, the ratings have provided a resource for legislative efforts to reward lenders that leave the best paper trails and plans with safe harbor from challenges and scrutiny for compliance with the full provisions of the CRA. Here, the poor enforcement revealed in the ratings is used to exempt lenders from any real enforcement efforts from the community.

My main focus is on the poor quality and improper focus of the rating process—as this reflects the most fundamental failings of the regulatory agencies to take reinvestment seriously—and thus points out the folly of developing any policy that relies on the soundness of these ratings. The ratings have become a critical issue in the efforts of community groups to enforce the CRA in the absence of serious Government enforcement efforts. The regulatory agencies announced in a 1989 policy statement that they would rely primarily on the existing CRA rating when reviewing any challenges. Experience has shown that it is virtually impossible to prevail in a challenge when a lender has a passing CRA rating.

Generally, lenders have been able to gain the highest CRA rating (outstanding) in spite of serious problems with service to lower-income and minority lending needs. I can give a few examples of the problems of the poor quality of CRA ratings here, with other examples placed throughout the remainder of my statement. New York City has the largest number of multifamily housing units of any city in the Nation. Multifamily housing is the main source of affordable housing to low-income people. Yet, the Federal Reserve gave both Manufacturers Hanover Trust and Chemical Bank outstanding ratings even though they made only one multifamily loan between them in 1990. These two banks had combined assets in excess of $100 billion. The outstanding ratings made it virtually impossible for community groups in New York to fight the merger of these two giant institutions.

In Chicago the Comptroller of the Currency gave an outstanding rating to Columbia National Bank (a detailed review of this rating is submitted with this statement). The bank's service area is defined just short of an Hispanic population to its east and a black population to its south. The bank made few loans in lower-income minority communities. But the single-family loans it did make in these communities were to white borrowers—at an average loan amount of over $200,000. The restriction of the lending community to a white area and to gentrification loans to minority communities were rewarded with an outstanding rating.

Meanwhile, the Federal Reserve gave a failing rating to Harris Bank in Chicago. Harris Bank has been a leader in making multifamily loans in severely depressed minority communities. Harris has often taken on the most severely deteriorated buildings requiring several layers of subsidies and financing to rehabilitate them for lower-income tenants. These loans have made a significant difference in the revitalization of minority communities such as Austin and West Garfield Park. But it was precisely the targeting of these programs to these minority areas that the Fed held against the bank—even though the programs were developed in direct response to needs defined by a broad coalition of community groups.

At meetings last spring between the National People's Action and the regulatory agencies, the agencies, and the Fed in particular, adopted the position that lenders cannot target programs to particular areas, but must provide identical services to all parts of their territory. This places an absurd penalty on programs that are the most likely to meet unmet credit needs in low-income communities—that is, programs that best meet the goals of the CRA. Thus, while some lenders are rewarded for disinvestment, others are punished for their successful reinvestment efforts to serve minority communities.

One of the most criticized aspects of the way regulators have assigned ratings revolves around giving credit for plans and processes as opposed to basing the ratings on actual performance. More and more we find both lenders and community groups complaining that the regulatory agencies are assigning grades based on the paper trail of meetings and community contacts that lenders can document rather than the record of providing loans and banking services. The 1989 CRA policy statement endorsed by all of the regulatory agencies states specifically that "commitments for future action are not viewed as part of the CRA record of performance of the financial institution. . . ."[2] But at the annual meeting of the National Community Reinvestment Coalition, Dennis Diescher, a senior officer of the Office of the Comptroller of the Currency and a member of the ruling body of the FFIEC, showed his disregard for that policy by stating:

> If I had an institution that put together a CRA plan, if you will, that had not had one in the past, and I felt that plan given time is going to result in significant contributions to the community in a way of meeting credit needs, I can, I believe, rate the bank as performing outstanding even though they may not have the volume of loans as the bank across the street that may have had the CRA plan in place a little bit longer.[3]

It is precisely this attitude that encourages lenders to invest in developing elaborate plans rather than investing in lending and banking services in lower-income and minority communities. The idea that the regulatory process should seek out a paper trail and the development of planning documents was developed by the FFIEC in its programs to implement the public rating requirements. Where did the FFIEC get this orientation? It appears to me that it came from J.S. Barefoot & Associates, a private consulting firm headed by a former Deputy Comptroller of the Currency and official of the Federal Home Loan Bank Board. According to the firm's own marketing literature, the firm "created(ed) the FFIEC training the agencies used to teach 750 examiners the 1990 changes to CRA ratings and CRA public disclosure guidelines."[4] This leads us to the claim that the CRA represents some kind of arbitrary and capricious regulatory burden on the lending institution.

2. The Alleged Regulatory Burden

While it surely represents a useful and legitimate business to provide institutions with assistance in responding to regulations, there is something strange and perverse about the regulatory agencies farming out their policy development and training obligations to private firms whose growth in sales are directly related to an increase in regulatory requirements and the paperwork burdens imposed on the banking institutions. Interestingly, no outside organizations involved in the community side of reinvestment or fair housing enforcement were notified of the potential contracts for such training services. Instead, they are offered occasional cameo appearances at seminars and conferences. Clearly, no one who is critical of the CRA regulatory process is sought out to provide balance and diversity to the processes by insuring that these organizations and individuals have access to such contractual services. Public notices of contracts are not placed in the kinds of publications civil rights lawyers, fair housing groups, and community reinvestment experts and researchers generally use. If banks marketed their CRA-related services the same way the FFIEC and the individual regulatory agencies market their contracts for the review and development of their enforcement programs, they would surely receive failing ratings.

The regulators have become enmeshed in a closed system of information and attitudes where regulators move into the private consulting sector and sell their knowledge of the regulatory process. Then, these firms are hired by the regulatory agencies to develop regulatory programs and compliance procedures. Lenders then hire the consulting firms staffed with exregulators to help them deal with the compliance processes developed, at least in part, by the firms whose economic survival depends upon the perpetuation of some kind of regulatory burden. It is not surprising that Dennis Diescher recently left the Comptroller's Office to join the consulting firm that developed the training materials for the CRA examiners—and that now guides lenders in developing the paper trail, plans, and programs that the examiners use to measure compliance.

The burden of regulatory compliance for the CRA is overwhelmingly the creation of the regulatory agencies, compliance consultants, and banking institutions that confuse performance with process. The Act itself requires almost no paperwork. What is required:

- Lenders must develop a Community Reinvestment Act statement that defines a local community with a map representing that community and a list of the types of loans the lender is prepared to make in the community. This statement must include some prescribed language indicating that the institution is subject to the CRA and indicating which regulatory agency regulates the institution with regard to the CRA. These statements are typically only 4 or 5 pages long—and sometimes as short as both sides of one page, including the map and prescribed legal language.
- Lenders must maintain a public file containing the two most recent CRA statements, a copy of the public CRA rating (supplied by the regulatory agency) and all comments relating to the lender's CRA performance in the past two years.
- Lenders must post a single page legal notice (in words prescribed in the CRA regulations) indicating that the lender is subject to the CRA and indicating the public availability of the CRA statement and file.

This is all the paperwork that is required under the law. Lenders are required to review their CRA activities and to assess the credit needs of the local community on a timely basis. How this is done is not defined in the law or regulations. It is no wonder that the Office of Management and Budget indicated that it found the CRA to be at the bottom of regulatory burdens.

While there are surely some efforts required to assess and serve local credit needs, lenders are free to develop the techniques that they deem most appropriate. Lenders are expected (but not required) to review their lending patterns and assess their own records of service—but these are things that any reasonable business ought to do with or without Federal obligations. Some lenders count the time and effort involved in making loans in low-income areas as a regulatory burden and compliance cost. The law was passed to insure that all people have reasonable access to credit and banking services. It is absurd to count the time allocated to serving lower-income needs as a compliance burden while the effort spent on higher-income groups is considered normal business. Such an attitude does not reflect a regulatory burden, but simply reflects the reasons why there is a need for this law in the first place.

The elaborate plans that some lenders develop, or the paper trails indicating the names of every community person anyone in the bank ever talked to during the year are not requirements of the Act and are typically not related to real measures of performance. But, we can see how these false measures and "regulatory burdens" can be created by misguided regulators and lenders trying to substitute process for substance. For small banks, in particular, there is no need for these paper trails and elaborate plans.

In 1980, I engaged in a review of banks in two rural counties in Minnesota as part of a project sponsored by the Comptroller of the Currency and supported by the other regulatory agencies. It took only a discussion with the senior bank officials and a few contacts in these rural communities to establish the service profiles of the lenders. For the most part, you simply had to ask the lender what economic development and credit needs existing in the community and what they had done to meet them—**with examples**. Basically, lenders either knew the needs and had taken steps to meet them, or they had not. In some cases, as aggressive as the lenders had been, they were unable to overcome some local economic problems—but they were able to identify the initial efforts to intervene and subsequent attempts that tried to learn from the failure of the initial efforts. It is important to point out that not all small rural lenders did serve their communities well, contrary to the present proposals to eliminate them from coverage because they can naturally be assumed to serve their markets. (See the attached paper on the misconceptions about exempting small banks from the CRA.)

While large institutions in major urban settings may have to deal with a wider range of problems, neighborhoods, and economic factors, the evaluation process should be guided by the same simple approach. In urban areas where public data, such as the HMDA data, exist that can reveal lending patterns, regulators should rely primarily on measures that reveal performance in making loans and providing banking services. If an institution can demonstrate this performance (urban or rural) there should be much less concern with probing documents that define the activity that led to this performance. It is when the performance is lacking that regulators need to probe the process to seek out reasons for the failure—whether internal or external to the activities of the lending institution. For the most part, these concepts are written into parts of the FFIEC's 1989 policy statement on the CRA—but they are not the concepts that rule the evaluation process.

Rather than seeking to develop such a basic approach, the regulatory agencies have engaged in obtuse thinking and the measurement of the number of pages of contact lists, meeting minutes, and drafts of planning documents. One example from Harris Bank, in Chicago, reveals how a regulator's absurd definitions of CRA requirements actually undermines the established efforts of lenders to meet serious unmet credit needs in lower-income communities.

Harris Bank often develops special programs and services for particular market niches—and seeks ways of marketing these programs to specific customers in these markets. For example, Harris markets its upscale personal banking services through ads in the program book of the Lyric Opera. It markets its special lower-income housing programs through ads on the subways and buses and through ads in local church bulletins in these communities. Surely there are some low-income opera lovers that might need access to housing credit that are not served by the upscale ads in the Lyric Opera program. Just as surely, there are some attorneys, doctors, or accountants in low-income, inner-city and inner-ring suburban communities that might respond to an upscale banking ad in an inner-city church bulletin or on a local bus. But in making reasonable and effective marketing decisions, it would hardly meet a significant underserved market to spend huge amounts of time and money advertising for low-income housing loans at the Opera or to advertise for upscale private banking services in severely distressed inner-city neighborhoods and churches. Indeed, having worked with some of the doctors and lawyers who work in these inner-city communities, I can assure you that they would define the lack of safe and decent shelter as a critical and immediate need that is more fundamental than their own need for yet another bank marketing scheme to serve their personal investment needs.

I tell you about these marketing efforts because the position taken by the Fed (both by Sandra Brownstein of the Office of Consumer and Community Affairs in Washington at a meeting with the National People's Action on April 6, 1992, and the position taken by Lorraine Woos of the Office of Consumer and Community Affairs of the Chicago Fed) is that any program a bank offers in one community it has an obligation and responsibility to market throughout its entire CRA territory. Because Harris failed its CRA rating for concentrating its low-income housing programs—and the marketing of these programs—in the communities of Chicago where they were most needed, the Fed has pressured the bank into wasting huge sums of money running around to wealthy suburban locations marketing its low-income and other housing loan programs. It doesn't seem to matter to the Fed that these communities have abundant access to all kinds of loan programs from the assets of the regional financial institutions that have located the vast majority of all their offices in these white city and high-income suburban locations. So, Harris is taking some of its resources that it had so successfully allocated to providing low-income housing and housing rehabilitation in inner-city communities and it is dashing about in the high-income suburbs touting these programs in order to satisfy the Madd Hatter CRA orders of the Fed. **This is what regulatory burden is really about.**

3. Lending Disclosure

Disclosure has always been at the heart of the reinvestment movement. The first piece of national legislation for reinvestment was the Home Mortgage Disclosure Act. The HMDA data have been used by virtually every organization in any urban area that has negotiated one of the more than 200 reinvestment agreements. These data are supposedly used by the examiners when reviewing CRA performance—which would mean that they are used thousands of times each year by the regulators. The use of these data by the media—especially the expanded HMDA data with information on applications and the race, gender, and income of applicants—has refocused national attention on the problems of race discrimination in lending. Yet, the Fed, the agency that controls the regulation of the HMDA, has continued to obstruct all community efforts to secure reasonable and timely access to these data. These data were created for the public, for use by citizens. As powerful and valuable as the media use of the HMDA data have been, this represents, in part, a vacuum filled by the media with their access to sophisticated computers. This is a vacuum created when the public, lacking these massive technological resources, was cut off from access to the data by the practices and rules of the Fed.

A. The Obstruction of Access to HMDA Data [5]

In 1988, Congress amended the Fair Housing Act to require racial, gender and income recordkeeping as part of the HMDA. Yet, the Fed has failed, after almost three years of negotiations with a host of community-based organizations and researchers, to produce these data in a format that can be easily used by the public and community groups for whom the data were intended. Only those with large computers can review and analyze data on the locations of loans by race, income and gender and the data on the individual loan application registers. Moreover, the Fed used the opportunity of the amendments to rewrite the HMDA regulations to withhold other HMDA that used to be available on March 31 of each year for the previous year's lending. There is no reason why lenders could not be required to disclose the information on their individual loan application registers at the same time in March of each year that they submit these logs to the Federal agencies.

Last year the data were not released until October (8 months later than the normal date). This is an extreme hardship for communities using the data. The regulators claim that this time is needed to insure the accuracy of the data. But we now see from a recent GAO review and from analyses by Fannie Mae and Freddie Mac that there are serious questions about the accuracy of these data. Not only have the agencies failed to reveal serious errors in reporting, but even when lenders such as Citicorp inform the agencies of these errors, they are not corrected.

In 1989, the regulators developed a policy that they will not take community challenges seriously unless the group indicates that it has dealt with the lender about its service record prior to the time of the challenge. The main source of data that groups use to develop a meeting with a lender is the HMDA data. By delaying the release of the HMDA data the regulators have created a Catch-22 where the regulators require community groups to review a lender's record while the regulators take away the public data that the groups need to assess that record. By the time the data are released now, they are too old to have much meaning. Indeed, the data are so old that the statute of limitations for fair housing suits has run out on many of the loans included in the disclosure. In spite of letters to Alan Greenspan from the Chairman and other members of the Senate Banking Committee that this process violates the law, the Fed has refused to restore public disclosure to its proper time.

B. Commercial Loan Disclosure

We have become so used to the Home Mortgage Disclosure Act that very few people remember that it was originally called the Financial Institutions Reporting Act. In its original form, it included commercial loan disclosure and disclosure of deposits. Commercial lending has always been a major reinvestment issue. Businesses create jobs and provide products and services for a community. I have reviewed about 175 of the more than 200 reinvestment agreements that have been negotiated since 1973, when the National People's Action made reinvestment a national movement. From the first oral agreements to the most complex written agreements of today, commercial lending has been a major focus of these reinvestment efforts.

But, commercial lending review has not been a major part of the CRA enforcement process by the regulatory agencies. When we read the CRA evaluation of huge commercial banks, we often see constant references to single-family home lending efforts and patterns, with almost no hint that these commercial banks are essentially commercial lenders. Commercial lenders are the main source of credit for established small- and medium-sized businesses that do not raise capital in the stock and bond markets. The main reason we do not see more analysis of the commercial lending patterns and reinvestment needs is that there is no set of data that provides information about the locations and categories of commercial lending.

The regulatory agencies have consistently opposed commercial loan disclosure for the public. But they clearly recognize the need for geocoded commercial lending data. That is why the FFIEC issued its policy statement last year defining their expectation that lenders would geocode their lending and provide the regulators with the reviews the lenders make of these loan patterns (including commercial lending).

The regulatory agencies were trying to create a set of commercial lending data for their own use, without making these data available to the public. Of course, these agencies could have required the public disclosure of these data, just as they could always have created public disclosure and just as they do create various forms of public disclosure related to insider loans, portfolio lending, foreign investment, profits and losses, and nonperforming loans. The regulators know that they should review lending patterns because this is the best measure of real performance—as opposed to the paper trail of meetings, community contacts, and planning documents that now substitutes for performance in the CRA examinations. The regulators, however much they have denied the need for commercial loan disclosure, recognize its value so much they have tried to coerce lenders into producing it internally for the regulators—but not the public.

Under provisions of the Federal Deposit Insurance Corporation Improvement Act of 1991, lenders are now required to submit some information on small business and small farm lending on their reports of condition (Call Reports). Other provisions of the act require the regulatory agencies to produce reports at a regional level, at least, of lending to small businesses, small farms, and minority-owned small businesses. This could have provided for commercial loan disclosure, but in the proposed regulations for this data collection, the Fed chose the least useful and most conservative definition of disclosure, providing regional data with no identification of the patterns of particular lenders in particular communities. This is consistent with the Fed's long history of opposing disclosure before it has been enacted and minimizing disclosure after it has been enacted. The time has come to recognize the need for public disclosure of commercial lending, small business lending, and lending to minorities and women—just as we recognize its value in home lending.

Business lending is even more critical to reinvestment than home lending. Partly this is because of the dynamic role credit plays in business expansion and job development. Partly this is because there is no other source from which one can identify business lending. As difficult as they may be to use, home lending at least leaves a public record of title transfers, mortgage documents, and property liens. Aside from commercial real estate lending, no such public record exists for business lending. That is why you don't have community groups coming before you with at least some studies of commercial lending. Only in the city of Chicago, where commercial lending and deposits must be disclosed by all lenders seeking deposits of city funds, do you have some commercial loan studies.

Chicago has had this form of deposit, housing and commercial loan disclosure since the year before the Home Mortgage Disclosure Act was passed. Lenders can and do code all loans and deposits by census tract and report them to the city for public use. There have been serious problems with the accuracy of these data, but these problems are related to the lax attitude the city has taken in the past to monitoring these data. In spite of these problems with accuracy, these data have been used to negotiate some of the most complex and comprehensive reinvestment agreements in the Nation. I have analyzed three of these lending agreements from three of the largest banks in Chicago. Commercial loan disclosure data was used to define general patterns of business lending that opened the door to discussions with each lender on its business lending practices. The reinvestment programs included new commercial lending products and identified some markets not being served. For one lender, Northern Trust, the focus on small business lending has opened up an active lending program not only to established businesses, but to many new businesses as well.

It is true that these data are far from perfect in terms of supplying all the data needed to reveal the lending efforts and performance of all aspects of commercial lending. These data are not perfect—and no set of data, no matter how complex, will be perfect. It is also true that great improvements could be made in these data by some simple addition of a few more categories for the types of loans and the size of the businesses seeking loans. For example, the commercial loan disclosure format proposed by the National People's Action for an amendment to the Home Mortgage Disclosure Act provides separate categories for real estate and non-real estate loans, and separate categories for the size of the assets of the business. It also provides a category for Small Business Administration Loans and loans to sole proprietorships—all broken down by location. These categories might be translated into loan application logs, as is the case for the detailed HMDA reports. This selection of categories is not meant to be all inclusive. Rather, it is designed to provide some indications of the focus of business lending and the capacity of the bank to deal with Government or other complex loan processes (measured in SBA activity) and the capacity of the lender to deal with very small and varied businesses (measured in lending to sole proprietors).

C. Deposit Disclosure

A final word should be added for disclosure of data on the location of deposits. The only existing form of disclosure for deposit data is the reporting of deposits by branch location by the FDIC. This does not record the location of the depositors, but simply the location of the banking office where the accounts are located. In addition, as branches are removed from inner-city and rural areas, no data exist to suggest the potential banking markets in these areas. Deposits in the main offices of large banks are all listed as deposits from the ZIP code where the main office is located. This masks the huge diversity of locations of the depositors who use these central facilities. The Chicago ordinance has revealed that deposit disclosure is also feasible. It deserves serious consideration as an addition to the present disclosure requirements.

4. The Persistence of Race Discrimination

From the redlining articles in the *Atlanta Journal/Constitution* in 1988 to the **Frontline** documentary and *The Wall Street Journal* tabulation of rejection rates for every lender in the Nation receiving significant numbers of minority applications, the past several years have refocused national attention on the problem of the persistence of discrimination in lending. Other hearings have collected information about HMDA data and the responses of the lending community and the regulatory agencies. What remains a mystery is how the patterns can seem so clear and how fair housing groups can find and successfully litigate cases of lending discrimination across all segments of the lending industry while the regulators have found only one case of suspected discrimination to refer to the Department of Justice over the past 18 years. If it can be said in relation to sexual harassment that "they just don't get it," then it should be said of lending discrimination that "they just can't find it." I believe the answers lie in the low priority, negative incentives, poor training, and general disregard for existing investigation and evaluation procedures that are given to fair housing issues by both the regulatory agencies and HUD.

A. The Performance of HUD

HUD is designated as the lead agency in fair housing enforcement by the language of the Fair Housing Act itself. Personally, Secretary Kemp is the only member of the Cabinet who understands the value of the CRA. Certainly he has been the lone voice speaking up in support of the CRA in Cabinet meetings. No one doubts his personal concern about the injustice of race discrimination. Secretary Kemp even sent a letter to Alan Greenspan complaining about the Fed's efforts to delay public access to the HMDA data. But, personal enthusiasm is not enough. While Jack Kemp has been a visible spokesperson for fair housing, HUD's performance record of antidiscrimination efforts in lending under Secretary Kemp has been no better than the record under his invisible predecessor. Some examples will illustrate the point.

When Congress amended the Fair Housing Act in 1988, it imposed a 100 day target on HUD for completing the investigation of fair housing complaints, "unless it is impracticable to do so." HUD has turned this effort to insure timely justice into a perverse penalty on employees who fail to meet the deadline. Employees receive a black mark on their personnel records if they fail to complete enough cases within the 100 day limit. Naturally, this encourages HUD employees to discourage people from pursuing complaints that appear to be complex or difficult to investigate—which is typically the situation in lending cases. It also encourages employees to give up on cases that have reached the 100 day limit—regardless of the merits of the case. Finally, it encourages employees to do incomplete investigations in order to meet the deadline. It is also held against an employee if they make a determination at a field office that a complaint has sufficient cause to prosecute and this determination is overruled at the central office in Washington. This encourages employees to find no cause to avoid being overruled. Finally, while a finding of no cause is never reviewed, a finding of cause is reviewed at least two times after the initial finding in the field, thus creating a bias in the review process that allocates additional resources only to efforts to reverse a finding of cause.

The new amendments have been a major success in generating complaints about discrimination. But for HUD, this is a burden for the staff. Many fair housing organizations and their attorneys now find that HUD offices try to talk their clients out of cases—or try to talk them into settling for minor amounts of damages in order to get the number of cases reduced.

The National Fair Housing Alliance received a contract from HUD to mount a national advertising campaign to inform people of their rights under the Fair Housing Act. After the campaign was initiated, the number of complaints to HUD's hotline increased from about 12,000 calls in the year before the campaign to over 110,000 calls in the 6 months of the campaign. When the National Fair Housing Alliance applied for a renewal of the funding—this time to add marketing on lending discrimination, HUD did not reward them for a job well done, but placed them at the bottom of the funding list and cut their allocation from $400,000 to $25,000.

HUD has claimed that it has reformed its contracting process to insure that funds are not granted for political reasons. HUD should have been following the funding guidelines and the performance points that are assigned to each grant application. In this case, the National Fair Housing Alliance proposal earned more points than any other application. HUD violated its rules in dropping the highest rated proposal to the lowest position in order to spread the money around to other groups. The success of the advertising campaign increased HUD's work load dramatically. One can only wonder if the Fair Housing Alliance was being punished for its success. Of course, this punishes the citizens who were benefiting from the advertising campaign as well.

When given the opportunity to increase the scope of fair housing in its program and regulatory roles, HUD has actually scaled back existing fair housing language. In its existing regulations for Fannie Mae, HUD required the agency to clear all changes in its underwriting with HUD for their impacts on fair lending. In these regulations, HUD defined redlining and prohibited practices. When Congress expanded HUD's powers to include both Fannie Mae and Freddie Mac, HUD drafted regulations that gutted the existing fair housing language and replaced it with a simple statement that the agencies should comply with the fair housing acts. Only continued community pressure, especially from Gale Cincotta of the National People's Action, and the exposure of HUD's retrenchment at a Senate hearing on the secondary market forced HUD to replace the fair lending language in its regulations.

HUD's regulations for applying for Community Development Block Grants included provisions recommending that recipients engage in a study of the barriers to fair housing. When these application regulations were replaced by the new Comprehensive Housing Affordability Strategy (CHAS), HUD had the opportunity to require this analysis of the barriers to fair housing as part of the CHAS. Fair housing groups, the National People's Action, and other organizations pointed out this opportunity to HUD—on one occasion dealing directly with the Assistant Secretary for Fair Housing and Equal Opportunity. But when the draft regulations were released, they contained only the simple statement that recipients were required to comply with fair housing laws.

Finally, in the area of testing HUD finally announced a proposal to fund a national lender testing project. Yet, HUD actually disclosed the names of two of the three cities where testing would be done when it announced the request for proposals in May ("the Department has made a preliminary determination on St. Louis, Missouri and Philadelphia, Pennsylvania as sites"). By announcing the sites and imposing some restrictive rules on the testing process, HUD has developed a plan that all but requires the testers to wear big signs announcing that they are Government funded testers. In addition, the proposal required applicants to have their proposals screened by all four of the financial regulatory agencies "so as to ensure the validity of the findings and the viability of the proposed methodology." One has to wonder at the logic of requiring the applicants to screen their testing proposals with three regulatory agencies that have not developed any testing programs of their own and with the Fed whose Board of Governors unanimously rejected testing in part because they believed it to be unethical. In July, HUD had to publish amendments to the application process eliminating the naming of the cities and changing the requirement to clear the applications with the regulatory agencies to a strong recommendation. Such confusion reveals a less than serious attitude toward enforcement by the Nation's lead fair housing agency.

B. The Financial Regulatory Agencies

Generally, experience reveals that the regulatory agencies take fair housing issues rather lightly. Partly this seems to stem from poor training or limited training and from generally ignoring the regulations and guidelines that are already in place. As in the case of HUD, some examples make the point.

First, regulators will give outstanding ratings to lenders cited for fair housing and HMDA violations. One often reads a public CRA evaluation similar to the one given to Northwest Bank of Rockford (Illinois) by the FDIC which noted under the assessment factor for evidence of discrimination "technical (violations) are noted with respect to the bank's compliance with the provisions of Fair Housing, Home Mortgage Disclosure and other consumer regulations." When I discussed such technical violations with an examiner in the Chicago office of the FDIC, the examiner told me that one of the most common violations was the failure of the lender to send out an adverse action notice to applicants whose loans were denied. Thus, these applicants were not provided with a written reason for the denial, were not told their rights under the Equal Credit Opportunity Act or Fair Housing Act, and were not told which agencies the applicant might turn to if they felt that there had been discrimination. I would consider this a serious violation of the law, but the examiner said that it was just considered a technical violation which was not serious.

Where strong and clear guidelines for fair lending enforcement exist, they are not implemented. The compliance manual of the Office of Thrift Supervision states that in reviewing lending data, the examiner is to compare actual file data with the loan application registers to insure that the data are accurate and complete. (These registers were not created voluntarily by the regulatory agencies but resulted from a lawsuit against the agencies by a coalition of civil rights groups in the late 1970s.) Yet, last year I was asked to review the loan logs of a branch of the largest savings and loan in the United States (the former Toledo branch of Home Savings of America) as part of litigation against this lender for race discrimination. The review indicated that many of the loan files did not correspond to the data in the loan logs. Some cases were inaccurate and others were missing. In one reporting period almost ⅔ of the cases reported on the loan log summary disappeared altogether by the next reporting period. Litigation of this case is seriously obstructed by the tremendous gaps in these data that are at the core of fair lending examinations.

The branch manager of the institution responded in her deposition that she was not trained in the purpose and use of these data by her institution. While she stated that she used these records to review the institution's lending record, she was unable to explain what some of the categories and data entries meant. How could the largest home lender in the United States have such poor—and potentially discriminatory—practices? Moreover, how could a regulatory agency that claimed to check the accuracy of these data have allowed such massive recordkeeping failures to occur? **Amazingly, a week after leaving this institution, this previous branch manager went to work for J.S. Barefoot & Associates as a senior consultant. What is even more ironic is that after she joined the firm, the firm was hired to train the examiners of the Office of Thrift Supervision—the agency that regulates Home Savings of America.** Interestingly, when I asked examiners of the Chicago Office of the Comptroller of the Currency about the quality of their fair housing regulation, they responded that there could be no question about the aggressiveness of their examinations because they were monitored by Karen Godfrey, this very same senior consultant from Barefoot & Associates.

One of the low points of regulatory neglect came in the 1987 challenge of an application by SunTrust, in Atlanta, by a coalition of community groups. In responding to the challenge, SunTrust admitted that it only offered one type of mortgage loan. It conceded that the bank understood that the result of its decision to offer only this one type of loan product meant that it did not serve minority communities in its service area. Yet, the bank asked the Fed not to apply the effects test in reviewing the bank's service record. The Fed complied and rejected the community challenge. It has not been unusual to find a lender with an "outstanding" rating while the public CRA rating report indicates that the lender has numerous or even systematic violations of some requirements of the Equal Credit Opportunity Act or the Fair Housing Act.

In my experience, I have found other instances where the regulators do not have even a basic understanding of the fair housing laws. In a conversation with an examiner in the Chicago office of the FDIC, an examiner told me that if a property has 1–4 units, it is covered under the Fair Housing Act, but if it has more than 4 units it is not covered under the Act (when, of course, multifamily properties are covered). On May 12, 1992, Lorraine Woos of the Federal Reserve Bank of Chicago made a presentation before the Regional Housing Study and Action group there. In the presentation she described an alleged (but inaccurate) difference between two fair housing laws by indicating that the Equal Credit Opportunity Act protected people against individual discrimination and that the Fair Housing Act protected people against redlining.

In my experience, however, no case represents the failure of the regulatory agencies more than the case of Peter and Dolores Green, highlighted in the **Frontline** documentary on lending discrimination last May. I have attached to my statement a detailed profile of the Green case, which I shall summarize here.

The Greens are an African-American couple from the African-American community of West Garfield Park in Chicago. They were turned down for a loan from Avenue Bank of Oak Park. This community has suffered deterioration and blight, some from past riots (not unlike the problems in Los Angeles) and some from FHA abuses. But, community development groups like Bethel New Life, The Neighborhood Institute and PRIDE have been rehabilitating the housing in this community and the neighboring community of Austin. In December of 1989, HUD Secretary Jack Kemp took a tour of this area to see what a difference these efforts of community groups and lenders was making. The tour passed close to the home the Greens were applying to purchase. Here is a case that shows what happens when someone takes the initiative to complain about discrimination to a regulatory agency charged with enforcing the law.

When the Greens were rejected, they asked for a reason in writing (which the Equal Credit Opportunity Act requires). They got no reply. Dolores Green recalls that she was told that the bank did not make commercial loans—such as a mortgage loan on the multi-family building they wanted to buy. But the HMDA data show that the bank made multi-family loans both before and after the Green's application. On the **Frontline** show, the loan officer claims that the loan was rejected, after consultation with the president of the bank, because of the neighborhood where it was located. This would be racial redlining.

The Greens complained to the Fed, which sent the complaint on to the Chicago office of the FDIC. The agency never contacted the Greens to ask them about their complaint. The FDIC did write to the bank. The bank sent the FDIC a copy of an appraisal that the Greens had brought with them when they applied for the loan. The loan officer had told them that this appraisal was too old to be used in the loan application—yet the bank used this appraisal to claim that the loan was rejected because the value of the property was less than the loan amount requested. The bank never made its own appraisal. When another lender made an appraisal, the loan amount turned out to be well below the appraised value. The lending institution gave three different reasons for the loan denial. If the loan was actually rejected because of the neighborhood, then the bank falsely represented the case to the FDIC. But, the FDIC never made any investigation—even though the FDIC has clear guidelines that define in great detail exactly how an investigation is supposed to be made. The FDIC did not question the bank's use of an appraisal that was not done by the bank and that was almost two years old when the loan application was made. The FDIC did not question the bank's clear violation of the Equal Credit Opportunity Act in failing to provide the Greens with a written reason for the loan rejection. The FDIC simply accepted what the bank said and wrote the Greens that the reasons for the rejection were reasonable and that the case was closed.

No indication was ever given to the Greens of their rights under the Equal Credit Opportunity Act or the Fair Housing Act. The communications submitted to the FDIC by the Greens clearly indicated that the bank failed to comply with the Equal Credit Opportunity in this respect. The FDIC guidelines for investigations include a sample letter to the complainants that clearly informs them of their rights under the Equal Credit Opportunity Act and the Fair Housing Act—but no such letter was ever sent to the Greens by the FDIC. Fortunately, the Greens saw an article in the local paper about Gale Cincotta and the National Training and Information Center—the Nation's leading organization in enforcement of the Community Reinvestment Act. They sent information about their case to her and she asked me to review it. I reported on my findings to the Leadership Council for Metropolitan Open Communities, and the Greens are now in court with claims of discrimination against the bank.

When I called the FDIC office and spoke to Marybeth Apolzan, a compliance examiner, I asked if there were any formal guidelines for investigating such complaints. I was told that there were no actual guidelines. Yet, the examination manual for the FDIC contains over 15 pages of instructions and guidelines on the investigation of fair housing complaints. Obviously, the first instruction is to contact the complainant—something the FDIC never did. The guidelines encourage an on-site investigation, which the FDIC did not do. The guidelines indicate that the investigator should obtain information on when an appraisal was done. Had the FDIC done this, they would know that the bank never made an appraisal that could have been used to deny the loan. The guidelines instruct the investigator to check to see that the proper Equal Credit Opportunity adverse action letter is sent to the applicant—as the Greens had requested and the bank had ignored. Had the FDIC office used the guidelines, it would have sent the Greens a letter explaining their rights under Federal law, something the agency failed to do. Indeed, there were many specific actions defined in the guidelines that the FDIC should have taken—but did not.

When I asked the examiner how the FDIC knew if a bank's explanation for a denial was correct, she said that "we trust our banks." This sums up the attitude of the regulators. They see the lenders as "their banks" and are simply not concerned about protecting the rights of minorities—even when the minorities go to the trouble and effort of filing a complaint. It may or may not be a coincidence that this office of the FDIC was found guilty of racial discrimination against an African-American examiner and later convicted of taking retaliatory action against this examiner for suing the agency over its discrimination.

Outraged over the lack of concern by the regulatory agencies for enforcement of the fair housing and equal credit opportunity laws, Senator Alan Dixon introduced an amendment to the Equal Credit Opportunity Act that now requires regulatory agencies to report instances of suspected discrimination to HUD and the Department of Justice. One wonders what effect this requirement could have when the agencies simply "trust their banks" and fail to follow even the most basic guidelines for investigating complaints. Indeed, I have brought up the Green case at two meetings with FDIC regulators in Washington. In neither case was any effort made to contact me or the Greens to review the behavior of the agency. At this point, the Greens are waiting for a response from the Department of Justice about whether the Government will investigate possible criminal action by the bank if it lied to the FDIC about the reason for the denial of the Green's loan. Finally, the Greens are seeking advice on filing a suit directly against the FDIC for its total failure to meet its obligations to enforce the fair housing laws. Surely we have hit the bottom of fair lending enforcement when those who file cases as victims must also sue the agencies that were supposed to protect them.

5. The Powerful but Dangerous Drug of FHA and VA Lending

Last April 6, when this Subcommittee held roundtable hearings on FHA, Warren Lasko the Mortgage Bankers Association of America held up a report by the Woodstock Institute, of Chicago, that reported that in its study of lending in the Chicago area, mortgage bankers showed no differences in their levels of lending to minority and white communities and lower-income and higher-income communities. In the context of those hearings, this was to support the expansion of FHA and the endorsement of FHA as a means of rescuing people from the present crisis in affordable housing. Because this is the Housing Subcommittee, it is most important here to revisit the FHA/VA lending issues as a critical part of community reinvestment. In the past, when banks and the regulatory agencies have been questioned about the numerous studies that show that minority and lower-income communities do not receive reasonable levels of conventional loans, these institutions and agencies have consistently responded that these markets are served by FHA and VA lending. About 75 percent of all FHA and VA loans are originated by mortgage companies—so FHA/VA lending and lending by mortgage companies are parallel patterns. Before any more efforts are made to infuse minority and lower-income communities with FHA/VA lending in some misguided belief that this will save these neighborhoods, we need to recall that the reinvestment movement began as an opposition to the tremendous harm done to minority and racially changing communities as a result of the FHA/VA lending by mortgage companies.

HUD and the banking regulatory agencies have a long history of neglect and abuse in relation to the use of FHA and VA programs. Both HUD and the regulatory agencies have seemed to accept a dual lending market that provides all forms of lending to white communities while restricting minority communities to FHA and VA lending. In this context, it is revealing to note that **the community reinvestment movement emerged out of opposition to HUD's FHA program that was being used to exploit racial change and destroy minority and racially changing communities with massive waves of abandoned properties.** The failure of the Government to understand the separate and unequal nature of this dual housing market still haunts minority communities.

After the riots in the 1960s, the response of the Government to inner-city credit needs was to ignore conventional lending by banks and savings institutions and simply infuse minority and racially changing neighborhoods with FHA (and later VA) lending. But, by their very nature, FHA and VA loans are high risk loans. With their very low down payments and liberal credit underwriting policies, FHA and VA leave many homebuyers with few financial resources. In newer homes this is not a critical problem. In the initial years, all the systems of the home are new and do not need major repairs. Over time, the rapidly increasing property values provide new equity against which one can borrow for major expenses. One could always sell the home for enough to pay off the loan, if necessary.

But in older areas where the homes often need major repairs soon after they are purchased, the liberal financing leaves homeowners without the resources to meet their needs. Property values do not rise rapidly in these areas and there is no new equity to borrow against. Without pre-purchase or default counseling after people get in trouble, thousands of people find themselves in foreclosure. This is compounded by the practices of mortgage companies that file for foreclosure as soon as possible to avoid servicing costs and to get the insurance proceeds. HUD's policy of requiring foreclosed properties to be conveyed to HUD vacant transforms each foreclosure into an abandoned building.

The result of these policies and practices has been massive exploitation of racial change. With the Government taking all the losses and the communities suffering all the devastation, real estate agents team up with mortgage companies to reap huge profits from accelerating racial change through the FHA/VA policies.

The process of rapid racial resegregation through the dual housing finance market was first identified by the anti-redlining movement of the 1970s, led by the National People's Action. To this day, the financial regulatory agencies systematically respond to the lack of lending by banks and thrifts in minority communities by asserting that these communities are served by FHA lending. This is strangely reminiscent of the old segregationist's argument that there was nothing wrong with segregated lunch counters as long as blacks had a place to eat. These dual lending markets are not simply separate, they are unequal. The blight caused by FHA lending in the past continues. FHA lending may initially create opportunities for minority individuals—but this is done at a terrible cost to the communities where these loans are concentrated. Whole sections of Detroit, Cleveland and Chicago are still blighted with the abandoned homes from this infusion of FHA "fair lending."

The National People's Action is responsible for a provision of the Affordable Housing Act that requires HUD to release FHA foreclosure data by census tract and lender. These data are now being analyzed in several communities across the Nation under the FHA Foreclosure Abatement Project of the National Training and Information Center. They reveal precisely the patterns that community groups have tried to explain to public officials for years. Preliminary results reveal that in several minority and racially changing communities in the Chicago area, for example, the levels of defaults and foreclosures themselves are at epidemic levels. The study combines all FHA lending over the period from January of 1986 through September of 1991. Recent studies of FHA loan losses by Price Waterhouse reveal that these loans are still young, with their highest levels of loss still ahead.

In Chicago's African-American community of East Garfield Park, defaults represent 26 percent of all loans made and foreclosures represent over 12 percent of all loans made. In the African-American community of North Lawdale, the level of defaults is at 22 percent but the level of foreclosures is already at 15 percent. In the African-American communities of Washington Park, Englewood and West Englewood, default rates range from just over 21 percent to over 29 percent while foreclosure rates range from just under 10 percent to over 21 percent. For the Chicago suburb of Harvey, which has undergone a massive racial change, the level of defaults is 26 percent and the level of foreclosures is over 9 percent. Some of the largest FHA lenders in Harvey have foreclosure rates as high as 31 percent. Typically, the defaults will lead to foreclosures and foreclosures indicate an empty, boarded up, and abandoned property. These properties become drug houses, fire hazards, and havens for crime. Just two weeks ago, Lindsey Murdock—a six year old child—was abducted, beaten, raped, and stabbed to death in the garage of an abandoned FHA home just two blocks from where he lived in the African-American Roseland community in Chicago.

FHA is a powerful drug that can be beneficial when administered carefully and in limited dosage. But, HUD has become a drug pusher in the use of FHA. While HUD pushes its dangerous FHA drugs, the financial regulatory agencies and the secondary market agencies (Fannie Mae and Freddie Mac) fail to open access to the health giving blood of conventional lending. **Many communities struggle to rebuild from the blight caused by the very Federal agencies that were supposed to protect minority communities from discrimination and exploitation.** It is ironic that millions of dollars of HUD funds are used by community groups to rehabilitate communities that were destroyed by HUD's FHA lending.

I have submitted several articles with my statement that provide details on many aspects of this pervasive and lethal process of discrimination and the abdication of their roles by HUD and the regulatory agencies. The report traces the previous studies of the dual market, which universally describe the infusion of FHA and VA lending into communities with the resulting destructive effects of abandonment and blight when conventional lending could serve existing needs. HUD's National Housing Discrimination Study released in August of 1991 documented that when minority and white couples were sent to real estate agents with the same economic and employment profiles, minority home seekers were more frequently referred to FHA and VA for home financing. The only study that claims the mortgage companies and their use of FHA/VA lending represents a pattern of fair lending is the Woodstock study. Therefore, it deserves some special attention.

Much of the work done over the years by the Woodstock Institute has been sound and has provided a valuable contribution to the field of reinvestment. The Community Lending Fact Book that Woodstock produces annually for Chicago from the HMDA data and data from the state's disclosure that covers mortgage companies is the only such publication of its kind in the Nation. It has been a valued resource over the years, and the recent edition that tabulated data from the newly expanded HMDA data for 1990 provides some critical figures on community lending by race that cannot be secured from the public disclosure tables produced by the Fed. Woodstock produced a report advancing a method for commercial loan disclosure that represents a thoughtful proposal for a more detailed form of disclosure than has been recommended thus far by the National People's Action.[6]

Other work, such as the Institute analysis of the Chicago commercial loan disclosure data, has been plagued by inaccuracies and errors—and even an unwillingness to correct significant errors when they are identified.[7] In the analysis of the commercial loan data for Chicago, for example, the Institute lending data for one bank (American National Bank) had been inflated by a factor of 10 due to an error in placing the decimal point. This was clearly evident in the Institute's own reporting of the asset size of the banks included in the analysis, where the level of loans for a 2 year period were greater than the total assets listed for the bank. While this lender accounted for only a small fraction of all lending in reality, this error resulted in 37 percent of all Chicago lending and 43 percent of all suburban lending being assigned improperly to this one institution. This contaminated the entire analysis—yet after the Institute had been informed of this major error it revised its report without correcting the lending level for this institution.

The Institute's report on mortgage bankers (and FHA and conventional lending patterns) presents a more egregious problem. The data analysis clearly reveals one pattern (in line with all the previous literature on the dual lending markets) while the executive summary and all the press release materials emphasize a distinctly different—and unfounded—conclusion that "there were no racial disparities in the mortgage banks' lending patterns." In large measure this comes from the fact that the Institute contracted the study to a person with no background in FHA/VA lending or the operations of mortgage bankers and mortgage brokers. The report is called **The Unknown Lenders: The Role of Mortgage Banks in the Chicago Metropolitan Area.**[8] In fact, the role of mortgage banking companies is far from unknown, especially in Chicago where the anti-redlining movement began and where major studies of the dual FHA/VA and conventional markets have been conducted since 1975. Earlier studies of the dual market are easy to find, since two of the best early studies (from Baltimore and Philadelphia) are contained in the original hearings on the Home Mortgage Disclosure Act in 1975. It would appear that mortgage banks were unknown mostly to the consultant doing the research and to those who provided support from the Woodstock Institute.

The consultant hired for the report contacted me after securing the contract, asking if I would assist her in learning the basics of mortgage banking industry. While I provided some materials and some extensive references, the report indicates that the consultant never developed an understanding of the existing literature. Ironically, the first comprehensive analysis of the dual housing finance market was one that I wrote for HUD with Dennis Marino—who later became President of the Woodstock Institute for several years.[9] Other major studies of the dual housing finance market have been produced by Anne Shlay, who was a staff member of the Woodstock Institute when she did one of the studies.[10] The most recent study of the dual FHA/VA and conventional housing markets was completed in Chicago the year before the Woodstock report on mortgage banks. This report used data obtained from the Woodstock Institute.[11] Having failed to explore and understand the substantial literature in the field, the author of the Woodstock report erroneously claims that her report is "the first in-depth examination of mortgage bank residential lending in a major metropolitan area."

The conclusions in the executive summary and introduction of the report and in the press release materials are based on data an that combined all the loans (both FHA/VA and conventional) for all mortgage companies for each census tract used in the analysis for 1989 HMDA and state mortgage banker disclosure data. While it is true that the data show no significant effect due to the race variables when **both** FHA and conventional loans are lumped together, the equations in Section Four of the report clearly indicate that the variables for racial change and race are **the most important** predictors of the levels of FHA loans in a community. In other words, the traditional patterns we have become used to—**high levels of FHA loans in minority communities and high levels of conventional loans in white communities—are clearly documented by the report—but ignored in the final analysis.** It is only when one ignores the type of loan and combines the loans of all mortgage bankers together into one pool that the lending patterns of mortgage bankers appear to be equal in minority and white areas and lower-income and higher-income areas. Even when the differences in FHA/VA and conventional patterns are discussed, only a slight passing reference is made to how this pattern might fit models of the dual housing market. The report prefers to cast these differences as "in many ways complementary" and reflecting the need for FHA/VA loans due to the lower-income levels of the minority communities.

My own review of lending data reveals both that mortgage banking companies do allocate FHA/VA loans disproportionately to minority communities and also that the patterns of other lenders reveals that this does not conform to the high level of demand for conventional lending that exists in these communities. Second, my analysis reveals that the home lending market in Chicago is so dominated by a small groups of very large lenders (as was clear in the Woodstock report) that an analysis that combined all lenders into a single total for each census tract was inappropriate. An analysis that looks at the patterns of individual lenders is far more representative of the variations and patterns in the market, since the volume of lending by any one lender can radically alter the profile of any given community.

I have attached a table made from the same 1989 lending data that was used in the Woodstock study—as reported in the 1989 Community Lending Fact Book. The table calculates levels of lending (total, FHA/VA and conventional) for the 10 largest depository lenders and the 10 largest mortgage bankers in 1989. These lenders dominate the single-family mortgage markets for both the depository institutions and mortgage banking companies. All of these lenders have the capacity, and general range of lending, to define them as lenders serving the entire metropolitan area. Yet within this common market, levels of service to the predominantly black communities in Chicago with large single-family markets vary considerably. These variations raise questions about the equal lending of mortgage bankers, as well as the justification of serving minority communities with a preponderance of FHA/VA products.

The table compares lending for the entire metropolitan area with lending in 10 of Chicago's black communities (Austin, East Garfield Park, West Garfield Park, South Shore, Chatham, Roseland, Pullman, West Pullman, Englewood, and West Englewood). The first 10 lenders in the table are depositors institutions. All but 2 of these lenders have at least 1.0 percent of their loans in these black communities. But for the 10 largest mortgage bankers, only 6 have more than 1.0 percent of their loans in these black communities. So, for the dominant lenders, the depository institutions have higher levels of service than the mortgage bankers. This is particularly significant since 8 of the 10 depository institutions make only conventional loans while 7 of the mortgage bankers also originated FHA/VA loans—which mortgage companies argue are better for serving these types of communities.

One of the largest mortgage bankers, Rand Investment, made no loans in any of these black communities—Sears made only 2 loans, and Draper and Kramer made only 6 loans. This is a sum of 8 loans out of a combined total of 4,474 originations (or 0.2 percent). This combined pattern is worse than the record of all but 1 of the depository institutions.

Among the mortgage bankers historically defined as a problem in minority communities because of concerns about their rates of default and foreclosure (Fleet, Margaretten, and Midwest Funding in this sample), the traditional patterns of low conventional lending and high FHA lending are as one would expect. About 80 percent of Fleet's metropolitan lending is in conventional loans, but in these black communities, only 27 percent of the lending is conventional. In fact, over 20 percent of all the FHA lending Fleet did in the entire metropolitan area was in these black communities that generally represent less than 3–4 percent of even the markets of the lenders most noted for reinvestment. For Midwest Funding, about 23 percent of its entire area market is in conventional loans. But, this drops to about 6.5 percent in these black communities. Margaretten is the largest mortgage banking lender by far. While it does make a significant number of conventional loans in some black communities, when compared to the entire area, its percentage of conventional lending drops from 43 percent in general to 16 percent in the black communities.

Where conventional lending by mortgage bankers rivals FHA/VA lending it is not because of balance by individual lenders, but because a few mortgage bankers have become aggressive conventional lenders in these black areas. In most cases, it is the conventional lending of a single company—Old Stone—that tends to offset the FHA concentrations of Fleet, Margaretten, Midwest Funding and other FHA/VA mortgage bankers in black communities. In many cases this is aided by the conventional lending of Travelers. Both of these mortgage bankers are relatively new to minority communities. They represent a positive profile in mortgage banking practices—but by no means a dominant force.

Finally, data from the 1990 HMDA on some selected Chicago lenders shows that lower-income and minority markets represent considerable markets for conventional lending. Graph #1 is taken from some guidebook materials I have developed to assist people in analyzing lending patterns. In this case the 6 lenders are Chicago lenders. The lender with the highest level of service to lower-income tracts is FSB (which is Citicorp Savings Bank). Citicorp is a conventional lender (self-insuring its loans). Its level of service with only conventional lending is much greater than the levels of service of MB #1 and MB #2 (which are Margaretten and Fleet)—which use both conventional and FHA/VA lending. Indeed, other HMDA data show that while about half of Margaretten's loans are FHA/VA only, 20 percent of its total loans are to low-income people (those with less than 80 percent of the area median income). Citicorp made 17 percent of its loans to this income group—without using FHA/VA loans at all.

It is unfortunate that the Woodstock Institute did not contract with more experienced researchers in this area. Hopefully the Institute will probe the dual housing loan markets more deeply in its future work on mortgage companies. The Institute now has a new president who is a most accomplished and capable researcher.

CONCLUSIONS AND RECOMMENDATIONS

There needs to be a new commitment, and new effort to involve those with the skills and commitment to make reinvestment and fair housing work. This committee has the opportunity to raise its voice to initiate that new commitment. The time has come to support the thousands of existing and developing community-based efforts, to overcome discrimination and rebuild inner-city communities. The missing partner is not the community—and not even the lender—but the Government that has failed utterly in its enforcement roles. There are many legislative proposals that could be made. What is most important is to intervene in ways that make reinvestment and fair housing serious issues—for all of the participants in the lending industry and for the Federal agencies charged with enforcement of fair housing laws. I have included a range of proposals for the CRA, disclosure, HUD, and the fair housing laws:

THE CRA—

1. Reject all efforts to gut the CRA or revoke any CRA provisions already enacted.

2. Prohibit any efforts to gut the CRA by the back door through the reductions of effective regulation based on an alleged finding of "regulatory burden."

3. Change the language in Section 804 (1) of the Act from "including low- and moderate-income neighborhoods" to "especially minority and low- and moderate-income communities and individuals" to block efforts by regulatory agencies to claim that the CRA has no special purpose to serve these people and these communities.

4. Add to the Act a community service requirement (perhaps similar to the one required by the Federal Home Loan Bank Board for access to lending) for mortgage companies that are rapidly becoming the major source of home financing in the country. It would be absurd after two decades of community efforts to develop home lending programs through depository institutions to have them become meaningless because mortgage companies had taken over this lending market.

5. Mandate that agency reviews of CRA records (or community service obligations by mortgage companies or other lenders covered by the community service obligations of the Federal Home Loan Bank Board) be based on the existing measures of the provision of lending and banking services to the communities and individuals defined in the CRA legislation.

DISCLOSURE—

1. Amend the HMDA to insure timely release of all disclosure data and provide funding for resources that can be used by the community to analyze the data. This might include requiring an analysis of the barriers to fair housing (including a fair lending analysis) as part of the CHAS requirements. This might include providing a fee for CRA covered applications that would be placed in a fund that would be used to provide funding for community-based analyses of lending records.

2. Provide for disclosure of commercial lending so that access to commercial lending can be traced within older, minority, and inner-city communities—and to minority and women business owners.

3. Provide for the disclosure of deposit data so that underserved markets can be identified.

FAIR HOUSING—

1. Amend the Equal Credit Opportunity Act and the Fair Housing Act to provide standing for suits against HUD and the financial institutions regulatory agencies from all parties that have standing to sue members of the lending industries under these acts. HUD and the financial regulatory agencies will never take fair housing seriously until they are also at risk of being sued for their failure to enforce the law. To place enforcement in the hands of these agencies without providing a means of relief for protected classes to address the harm done by these agencies abdicating their obligations is to make a mockery of the laws.

2. Amend the Equal Credit Opportunity Act and the Fair Housing Act to provide mandatory regulatory penalties (up to and including the withdrawal of deposit insurance) for depositories whose behavior has demonstrated a disregard for the law or an effort to cover up their violations of the law. Only by imposing real penalties will lenders take the laws seriously. If lenders fail to serve citizens because of their race—or the racial composition of the community where people live—then such lenders should not be given the advantages and benefits of Federal deposit insurance.

3. Amend the Equal Credit Opportunity Act and the Fair Housing Act to specifically include disparate impacts—the effects test—and provide for a test of disparate impacts that is no more difficult to establish than is now required in employment discrimination cases.

4. Amend the Fair Housing Act to specifically include insurance companies for all forms of insurance related to the purchase of residential property (homeowners, mortgage insurance, etc.).

5. Investigate HUD's investigation and management of Title VIII complaints and cases.

6. Investigate the policies and practices of the review of fair housing and equal credit opportunity complaints by the financial institutions regulatory agencies.

7. Support programs, such as the HUD Fair Housing Initiatives Program (FHIP), that provide resources for enforcement of fair housing and fair lending laws by citizens and organizations with an interest in fair housing. For example, FHIP should be made a permanent program and funded at a level of $25 million.

HUD AND OTHER AGENCIES—

1. Investigate HUD's operation of the FHA program (and the VA's operation of the VA housing program) for adverse effects on minority communities.

2. Review and investigate the means by which HUD, and other agencies, engage in contracting for research and policy analysis to insure that individuals and organizations are not excluded simply because they do not have the advantage of belonging to the elite "Club Fed" of ex-Government employees and their consulting ruins that systematically dominate these contracting efforts. A full review should be made of HUD's contracting procedures and activities to insure that no guidelines or regulations are imposed that discourage minorities, the most experienced applicants, or small businesses or not-for-profit public interest and community groups from applying and securing funding and contracts in the area of fair housing and lending policy, research, and technical assistance. A similar review should be made of the means by which the financial regulatory agencies contract for services for training, monitoring, investigations, and general compliance consulting in relation to their obligations under the CRA, HMDA, ECOA, and the Fair Housing Act.

LIST OF ATTACHED REPORTS

1. Never Call Retreat: The Fight Against Lending Discrimination

2. The 20-Year Effort to Secure Data on Race and Home Lending

3. Columbia National Bank Evaluation

4. The Federal Reserve CRA Evaluation of Harris Trust and Savings Bank

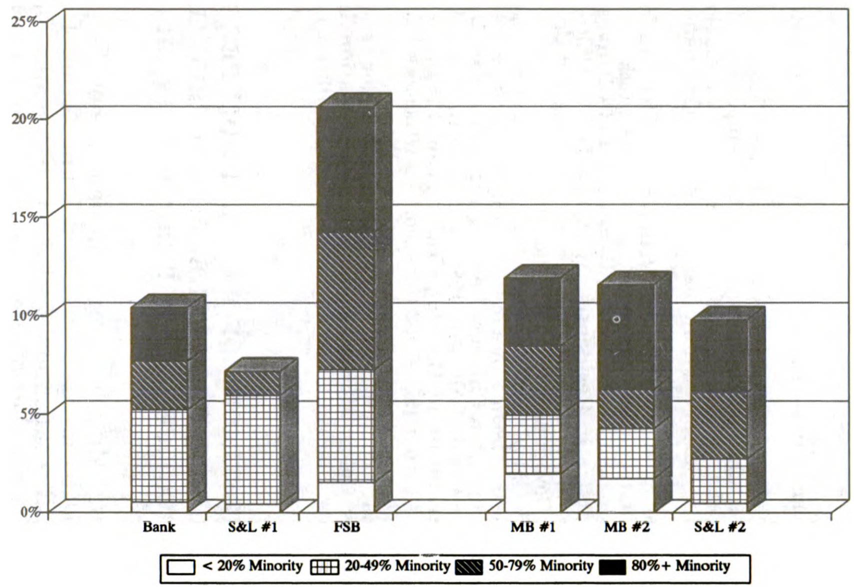
5. Misconceptions on the Exemption of Small Banks from the CRA

6. Case Story: Peter and Dolores Green v. Avenue Bank of Oak Park

Lending by 20 Major Lenders in 10 Black Communities for 1989 HMDA Data

Lender Name	# Conv. Mortgages	# FHA/VA Mortgages	Total # Mortgages	Percent Conventional	Total All Black Communities					
					Conv.	FHA/VA	% Conv.	% All Conv.	% All FHA/VA	% All Loans
Avondale FSB	1540	0	1,540	100.00%	40	0	100.00%	2.60%	0.00%	2.60%
Citicorp FSB	5811	0	5,811	100.00%	194	0	100.00%	3.34%	0.00%	3.34%
Cragin FSB	1177	0	1,177	100.00%	12	0	100.00%	1.02%	0.00%	1.02%
Household FSB	2671	0	2,671	100.00%	10	0	100.00%	0.37%	0.00%	0.37%
Home Savings of America	3793	0	3,793	100.00%	65	0	100.00%	1.71%	0.00%	1.71%
Mid America Federal S&L	1604	169	1,773	90.47%	1	0	100.00%	0.06%	0.00%	0.06%
St. Paul Federal S&L	1667	0	1,667	100.00%	38	0	100.00%	2.28%	0.00%	2.28%
Talman Federal S&L	3961	264	4,225	93.75%	83	36	69.75%	2.10%	13.64%	2.82%
United Savings of America	1085	131	1,216	89.23%	9	4	69.23%	0.83%	3.05%	1.07%
First National of Chicago	895	0	895	100.00%	22	0	100.00%	2.46%	0.00%	2.46%
Crown Mortgage	627	1,609	2,236	28.04%	2	12	14.29%	0.32%	0.75%	0.63%
Draper and Kramer	650	702	1,352	48.08%	2	4	33.33%	0.31%	0.57%	0.44%
Fireman's Fund	515	760	1,275	40.39%	5	37	11.90%	0.97%	4.87%	3.29%
Fleet	810	205	1,015	79.80%	16	43	27.12%	1.98%	20.98%	5.81%
Margaretten	2232	2,995	5,227	42.70%	23	122	15.86%	1.03%	4.07%	2.77%
Midwest Funding	476	1,579	2,055	23.16%	3	43	6.52%	0.63%	2.72%	2.24%
Rand Investment	1045	0	1,045	100.00%	0	0	100.00%	0.00%	0.00%	0.00%
Sears Mortgage	1637	440	2,077	78.82%	1	1	50.00%	0.06%	0.23%	0.10%
Travelers	1044	0	1,044	100.00%	55	0	100.00%	5.27%	0.00%	5.27%
Old Stone	730	0	730	100.00%	145	0	100.00%	19.86%	0.00%	19.86%

Graph 1: Loans To Low Income Areas
In Low Income Tracts By % Minority



NOTES

1. See "Analysis of Banking Industry Consolidation Issues," staff report to the Committee on Banking, Finance and Urban Affairs of the House of Representatives, March 2, 1992 and the Statement of Jonathan Brown before the Committee on Banking, Finance and Urban Affairs of the U.S. House of Representatives, September 26, 1991.
2. See "Statement of the Federal Financial Supervisory Agencies Regarding the Community Reinvestment Act," **Federal Register** (Volume 54, Number 64—Wednesday, April 5, 1989), page 13746.
3. Transcript of a panel presentation at the Annual Meeting of the National Community Reinvestment Coalition (February 28, 1992), page 13.
4. Promotional materials titled "Who We Are" circulated by J.S. Barefoot & Associates, Inc. (1991).
5. See the attached paper—**The 20-Year Effort to Secure Data on Race and Home Lending.**
6. Josh Hoyt, **Commercial Lending Disclosure and Economic Development: A Plan for Action.** Chicago: The Woodstock Institute (updated April, 1988).
7. David Flax-Hatch, **Tracking Chicago's Business Bucks: Commercial Lending and the Chicago Municipal Depository Ordinance.** Chicago: The Woodstock Institute (revised December 1987).
8. Constance Dunham, **The Unknown Lenders: The Role of Mortgage Banks in the Chicago Metropolitan Area.** Chicago: The Woodstock Institute (1991).
9. Calvin Bradford and Dennis Marino, **Redlining and Disinvestment as a Discriminatory Practice in Residential Mortgage Loans,** Office of Fair Housing and Equal Opportunity of the U.S. Department of Housing and Urban Development. Washington: U.S. Government Printing Office (1977).
10. See Anne B. Shlay, "Credit on Color: The Impact of Segregation and Racial Transition on Housing Credit Flows in the Chicago SMSA from 1980–1983," in **Fair Housing in Metropolitan Chicago: Perspectives After Two Decades** (Chicago: Chicago Area Fair Housing Alliance, 1987) and Anne B. Shlay, **A Tale of Three Cities: The Distribution of Housing Credit From Financial Institutions in the Chicago SMSA from 1980–1983** (Chicago: The Woodstock Institute, 1986).
11. William Peterman and Qi Sanshi, "Lending Discrimination in Metropolitan Chicago: Continuing Connections Between Race, Racial Change and Mortgage Credit," in **Credit by Color: Mortgage Market Discrimination in Chicagoland,** Cathy Cloud, editor. Chicago: Chicago Area Fair Housing Alliance (1991).

TESTIMONY OF DEBORAH GOLDBERG ACTING DIRECTOR, NEIGHBORHOOD REVITALIZATION PROJECT CENTER FOR COMMUNITY CHANGE

Good morning, Mr. Chairman and members of the subcommittee. My name is Deborah Goldberg, and I am Acting Director of the Neighborhood Revitalization Project of the Center for Community Change. I am a member of the Federal Reserve Board's Consumer Advisory Council and I chair the Council's CRA Committee. The Center is a national, non-profit organization that provides technical assistance to low income, predominantly minority community groups around the country on housing and community development matters. CCC's Neighborhood Revitalization Project advises groups on community reinvestment and fair lending matters. In addition, we are a founding member and serve on the Board of the National Community Reinvestment Coalition.

I want to thank you for the opportunity to testify here this morning, and even more importantly, I want to thank you for holding this oversight hearing. Experience has shown over the years that the amount of attention devoted to CRA enforcement by the banking regulatory agencies is directly correlated to the amount of oversight provided by the Congress through hearings like this one. We are at a critical juncture with respect to CRA right now. The banking industry is mounting a major revolt against the law, and is supporting a series of legislative proposals that would effectively gut the Act. At the same time, community groups are gathering their forces in support of the law, which has been a lifeline to their neighborhoods in the face of massive cutbacks in resources for poor communities at all levels of government. How these cross currents will ultimately play out is unclear. But the evidence compiled by your subcommittee through this hearing will be extremely useful in guiding us all.

THE ROLE OF CRA IN PROVIDING ACCESS TO CREDIT

In places where community groups have made active use of the law, CRA has proven to be a remarkably effective tool in providing access to credit for those previously shut out of the banking system. We estimate that, in the fourteen years since CRA went into effect, community groups have negotiated more than $7.5 billion in commitments from lenders that are targeted to low income and minority communities across the country. In recent years, banks have made an additional $23 billion worth of unilateral commitments to community development lending. Thus, CRA has resulted in the commitment of over $30 billion to poor communities around the country.

Key to Successful Programs

More important than the dollar amounts committed have been the terms upon which banks have agreed to lend this money. These terms represent an important breakthrough in lending to poor people. For many years, if banks tried to make such loans at all, they used the same underwriting standards they applied to everyone else—underwriting standards that were developed for middle income, middle class people. Those standards simply do not work for people of modest income. Not only do they automatically exclude such borrowers from qualifying for credit, they are not very good predictors of the likelihood that a person of modest income will repay a loan. Another set of standards was needed, and community groups have shown banks what these standards should be. These new underwriting standards address such issues as:

1. *Size of Downpayment.* Lenders have been reluctant to make loans with low downpayments, fearing that a borrower with a small amount of equity in a property will simply walk away if times get tough. But for poor people, a relatively small downpayment (5 percent or less) is still a large investment. In addition, housing is such a priority that people will go without heat, electricity, and telephone, if necessary, rather than miss a mortgage payment.

2. *Source of Downpayment.* This is addressed in two different ways. One way allows people to use money for part of a downpayment that has not necessarily been kept in a bank account, that is, money whose source is undocumented. This is often called "mattress money," or cash on hand. Since so many poor people do not have bank accounts, it is difficult for them to prove that such

money is not a loan that needs to be repaid. But under the new underwriting standards that banks are using, they are allowing some amount of cash on hand to be used toward a downpayment.

In addition, many cities have developed programs to provide "soft second" mortgages to help with the downpayment and closing costs for lower income homebuyers. These are loans that generally only have to be repaid if the borrower moves within a certain period of time. Many lower income people can carry the cost of monthly mortgage payments, but have a hard time getting over the hurdle of putting together enough money to cover these costs. Such programs help meet the needs of both borrowers and banks, but not all banks have been willing to work with them.

3. *Length of Time on the Job.* Bankers are used to looking at white collar workers. They assume that, if a person changes jobs frequently, it means they have trouble holding a job, and therefore may be a poor credit risk. As a result, they tend to require that loan applicants have a certain number of years on the same job. For lower income people, however, changing jobs may be a fact of life. They may work in seasonal industries, or in marginal businesses that come and go. Or they may change jobs in the hopes of finding one that will allow them the opportunity for advancement. Given this reality, what matters about a low income person is not how many years they've been on the same job, but their ability to generate a steady stream of income. If they've been able to do this despite job changes, the chances are good that they will maintain the income necessary to pay back their loan.

4. *Poor Credit Record.* There has been a lot of discussion lately about problems in the accuracy of reports generated by the major credit reporting companies. In fact, several states have sued these companies in an effort to force them to improve the accuracy of the reports they provide to creditors. Knowing the kinds of problems credit records have created for sophisticated borrowers, imagine how much worse they may be for people who aren't even aware that there is such a thing as a credit bureau. Many poor people are not only unaware of the credit reporting system, they don't know their rights and have no idea how to correct problems that may exist in their own records.

It's no big surprise then, that when banks get credit reports for lower income borrowers, credit problems sometimes appear. Under the new underwriting standards, banks allow borrowers to provide an explanation for any credit problems, and may even refer borrowers to a non-profit agency that can help them clean up their records. In addition, if a borrower can show that his or her recent record has been good, then the bank will agree that the past problems will not be grounds for rejecting the loan application.

5. *No Credit Record.* Many poor people pride themselves on the fact that they've never used credit. If they need a new car or a new refrigerator, they save their money until they can afford it. This doesn't work so well when it comes to buying a house, which is a much bigger-ticket item. And a side-effect of this frugality is that the credit bureaus have no records on such people. Lack of credit history makes banks very nervous. As risk-averse people, bankers don't like to be the first one to lend a person money. They want someone else to have taken that chance and created a track record.

A track record does exist for most low income people, but it's not at the credit bureau. Rather, it's with the landlord, the utility companies, the phone company, etc. Poor people do have financial obligations to manage, and if a banker looks at their record of doing so, even though the record is kept in a non-traditional place, he or she can predict the likelihood that the person will pay back the loan they're requesting.

These are just a few of the most important underwriting changes that community groups have helped banks make. The full list is much longer. And similar standards have been developed for small businesses and for non-profit, community-based development organizations.

In addition to the underwriting changes, many CRA agreements negotiated between lenders and community groups contain a number of other important features. These are designed to make sure that the credit gets out on the street. They include:

1. *Special Marketing Efforts*. These are written specifically to appeal to the targeted groups, which in some cases means they are in a language other than English. Ads may include pictures of minorities, and they are placed in media that are directed to specific neighborhoods or minority groups. They send the message that the bank is interested in doing business with low income and/or minority customers, in a way that general ads in the mainstream media do not. Affirmative marketing measures are extremely important in overcoming the effects of years of past discrimination and discouragement that many low income people have experienced from their local banks.

2. *Pre-Purchase Home Ownership Counseling*. This type of counseling helps prepare prospective homeowners for the process of applying for a mortgage and the responsibilities of home ownership. It includes a review of the applicant's credit record and help clearing up any problems. It may also include helping the applicant develop a budget that allows him or her to save money for a downpayment and closing costs and to pay off any excess outstanding debts. The applicant learns how much house he or she can afford, how to shop for a house, the role of the real estate agent, and what to be prepared for in the long term maintenance of a house.

By the time someone completes comprehensive pre-purchase counseling, they are ready to walk in and apply for a loan. All their documents are in order, and they can put absolutely their best foot forward. This reduces the time and risk for the lender. At its most effective, the counseling is done by a non-profit, community-based organization that can refer the borrower to the most appropriate lender for his or her circumstances, and can help them avail themselves of any appropriate assistance programs. The counselor can monitor the application process to insure that the borrower is treated fairly, and if need be, intervene on the borrower's behalf.

3. *Affordable Bank Accounts*. These are often known as "basic banking" or "lifeline" bank accounts. They are structured for people with low incomes, who cannot provide a large opening balance or maintain a large minimum balance. They generally allow a set number of checks a month for no fee or a low fee. Such accounts make it possible for low income people to establish a banking relationship. They also protect them from the very high cost of using

money orders and the predatory practices of many check cashing outfits.

4. *Charitable Contributions.* Most banks have a tradition of making charitable contributions in the communities in which they're located. They see this as part of good corporate citizenship. But many banks have never considered how they can use these contributions to further their goals under the Community Reinvestment Act. On the other hand, for many community groups, the most difficult task they face is raising the general support they need to carry their staff and put together community development projects, offer counseling services to community residents, and engage in any number of other efforts designed to strengthen and improve their neighborhoods. Yet their presence not only means investment opportunities for lenders, it also protects the investments that lenders have already made by strengthening the fabric of the community. Through their partnerships with community groups, banks have come to recognize the strategic value of directing some of their charitable dollars to community-based organizations that serve poor neighborhoods.

5. *Monitoring.* A critical part of most reinvestment programs is some mechanism for monitoring the success of the program. A committee, made up of bank and community representatives, is the most common format. The monitoring committee serves as a forum for maintaining accountability for all parties to the agreement. It allows for problems to be identified and course corrections to be made in a timely manner. This is especially important since it is difficult to work out all of the fine details of the operation of a loan program in advance. The monitoring committee also provides the flexibility needed to make changes in a program in response to changes in the economy or other local conditions.

6. *Commitment from the Top.* None of these components can guarantee success if there is not commitment, from all parties, to make the agreement work. This has to start at the top of the organizations involved, and be carried through to the people directly involved in the implementation.

Agreements with these ingredients have had a significant impact on the communities in which they have been implemented, as a few examples will illustrate.

Impact of CRA Agreements

In Chicago, community groups negotiated agreements for the establishment of Neighborhood Lending Programs with three major banks in 1984. In 1989, Calvin Bradford conducted an evaluation of these programs. He found that the three banks had made 572 loans, totalling $117.5 million, and producing or maintaining nearly 5,000 affordable housing units. The performance of these loans was remarkable, with only one small loan being written off. The success of the programs is indicated by the fact that all three banks unilaterally decided to extend the programs, at an increased level of funding, for another 5 years.

In Philadelphia in 1986, two separate community organizations reached agreements with Fidelity Bank. One of these was the Eastern North Philadelphia Initiative Coalition (ENPIC). The other was ACORN. The agreements were similar in terms, and between them covered virtually all of the low income areas within Philadelphia. Fidelity's goals for the first year of its agreement with ENPIC were 115 mortgages, 200 home improvement loans, and an unspecified number of small business loans. The bank made 197 mortgages, 181 home improvement loans, and 76 small business loans.

The experience with the ACORN agreement was similar. In the first year of that agreement, the bank made a total of $18.3 million in loans, including 290 mortgages for a total of $5.5 million. This represented a 10-fold increase over Fidelity's lending in those same neighborhoods the previous year. Since that time, ACORN has reached similar agreements with three other banks in Philadelphia: Continental, Mellon, and Provident. The Provident agreement was reached too recently to show results yet, but the other two illustrate the level of demand in poor communities in Philadelphia. In 1991, Continental made 123 loans worth $3.4 million. Mellon made 267 loans worth $6.8 million. These programs have begun to have a significant impact on the communities in which the loans are concentrated, where in many cases there has been at least one loan—representing one new homeowner—per block.

A third example is provided by Pittsburgh, where the Pittsburgh Community Reinvestment Group (PCRG) reached an agreement in 1988 with Union Bank (now Integra). As of March of 1990, that agreement had resulted in the bank making 372 home mortgages, commercial real estate and small business loans, for a total of $27.2 million. As of June 30, 1992, that figure had reached $248,721,827. All of these loans were targeted to low and moderate income people and communities, and to minority- and women-owned businesses.

CRA and Rural Communities

CRA has also been used effectively in rural communities, although to a lesser extent. The lower level of activity can be attributed to a number of factors, including fewer community-based organizations, a lack of good information on bank lending patterns, and the social and, political dynamics of life in small towns and rural areas.

However, in the rural areas where CRA has been employed, the results are impressive. A good example is Iowa, where lending to small farms has been the focus. A group called Iowa Citizens for Community Improvement, in conjunction with several rural and agricultural advocacy organizations, has negotiated agreements with three bank holding companies in that state, Norwest, Banks of Iowa (now Firstar) and Brenton Bank. The first of these agreements was reached in 1989, the most recent in 1991. As of March of this year, these agreements had resulted in 322 loans, worth $11.2 million, being made to small- and medium-sized farmers in Iowa. These loans, which average just under $35,000, are reaching a segment of the market traditionally ignored by agricultural lenders. In addition, Iowa CCI also promotes use of a State Beginning Farmer loan program, which encourages small farmers to enter the business by helping them buy their first piece of land. A second program that the group supports is the Farmer's Home Administration Interest Assistance Program, which guarantees farm loans and allows the lender to lower the interest rate by as much as 4 percent.

These examples show the potential that CRA can have to create positive change in poor and minority communities in this country. Unfortunately, this potential seems to be realized only in places where community groups take it upon themselves to make the law work. This positive impact is not the natural outgrowth of the CRA enforcement process.

THE NEED FOR BETTER INFORMATION ON BANK LENDING PATTERNS

In order to persuade lenders to undertake new programs designed to serve low income areas, community groups have to become *de facto* bank examiners. They have to do their own research on the banks' lending records, and often have to show a bank how bad its performance is in order to convince that bank to make changes. To do this, groups must have access to information.

The Home Mortgage Disclosure Act

One of the basic tools that community groups have used over the years to document bank lending patterns is the information made public under the Home Mortgage Disclosure Act (HMDA). Enacted in 1975, HMDA has historically required insured depository institutions to make public, on an annual basis, information about the geographic distribution of their home mortgage lending. In 1989, as part of the Financial Institutions Reform, Recovery and Enforcement Act (FIRREA), Congress made some very significant changes in the law. These changes bring additional lenders under coverage by the law, and also require lenders to disclose information about the race, gender and income level of applicants for mortgage loans, whether those loans were approved or denied. While only one year's data (1990) has become available under the new provisions, that has been enough to illustrate the power of the additional disclosure to highlight problems of access to credit by minorities and low and moderate income persons.

Accuracy of the Data

There are some problems with the data, however. One is simply the quality of the data provided by lenders. This problem has plagued HMDA since the very beginning, and is very much evident in the 1990 data as well. While some of the problems with the recent data are attributable to the new reporting system, they cannot all be so easily dismissed. Never in the history of HMDA have the agencies done an adequate job of insuring that the data lenders report is as accurate as possible. They have relied on community groups and other HMDA users to spot problems, and even then they haven't always taken action.

The pattern appears to be continuing. In the 1990 HMDA data, according to the Federal Reserve's analysis of the data nationwide, no race data was provided for 11 percent of the applications for government-backed mortgage loans (FHA, VA, and FmHA), and for 8 percent of the applications for conventional mortgages. This is a total of 280,100 applications for which no information on the race of the borrower was reported. Income data is missing for 30 percent of the government-backed mortgages, and 28 percent of the conventional loans, a total of 883,400 applications. The missing income figures are particularly shocking, since the only exemption allowed for reporting this information is if the lender did not rely on income to make a loan decision. It is difficult to believe that this was the case 30 percent of the time.

The quality of the data will only improve if the agencies take a more aggressive approach to enforcement of the law. In the past, repeated violations have not led to the imposition of any sanctions on the offenders, and there is no evidence that this practice has changed.

Problems With Access to the Data

A second problem with the way the agencies are handling the new HMDA data is the difficulty of access to the raw data, that is the loan application registers that lenders submit to their regulatory agencies. It is only in the registers that one can get complete race, gender, income and census tract information for individual loan applications. Initially, the agencies declined to make the raw data available. After pressure from community groups and others, they agreed to make it available in an edited form. However, to date, the only way to get this information is to buy the tape for the entire country. Using this tape requires access to a mainframe computer or similar technology that is beyond the reach of most community groups. The only alternative is to pay to have the data for a particular lender or metropolitan area downloaded off the tape and onto floppy disks, but this is a very expensive proposition.

Regulators Drag Their Feet

Two years ago, my agency helped to organize a meeting with representatives of the banking agencies and major users of HMDA data, including community groups, civil rights organizations, and researchers. One of our top priority agenda items was the request that the agencies to develop a system to make the new data available on floppy disks by metropolitan area. In fact, one of the participants in the meeting prepared an extensive, detailed memo suggesting exactly how this might be done most effectively. The agencies expressed a willingness to address this issue, but to date no action has been taken. The Federal Reserve now says that it hopes, but does not promise, to make the raw data available on floppy disk with the 1993 HMDA data, which will be made public in late 1994. Like CRA, the most effective use of HMDA data has been by those outside of the banking agencies. Yet the agencies have not taken the basic steps to make the raw data available to the public in a usable form.

Disclosure of Application Processing Time

As part of the Loan Application Registers, the agencies collect information on how long it takes lenders to process applications. This information can be very useful in pinpointing one potential form of discrimination. One relatively easy way for a bank to avoid making a loan to a particular borrower is simply to drag out the time it takes to process that borrower's application until he or she has no choice but to go to another blending institution or risk losing the home under contract.

In order to be able to investigate this problem, community groups and fair housing organizations have asked the regulators to disclose the dates on which applications were received by banks reporting under HMDA and the dates on which action was taken on those applications. Failing this, groups have asked the agencies to disclose the amount of time elapsed between the two dates. The agencies have refused. They have given two reasons.

In a letter to me dated November 1, 1990, Griffith Garwood, Director of the Division of Consumer and Community Affairs at the Federal Reserve Board, stated, "we believe that a disclosure of the elapsed time could be misleading . . . even within an institution, the elapsed time may vary widely for reasons unrelated to unlawful discrimination. For example, extra information requests (such as multiple employment verifications) may have been necessary, or it may have taken longer to receive a needed insurance approval." This, of course, is true. However, evidence of discrimination would be found, not in isolated cases where a single application from a minority borrower would be found to have taken longer to process, but rather where an institution exhibits a pattern of taking significantly longer to process applications from persons protected under the fair lending laws.

When pressed to take up this issue with the principals of the four regulatory agencies, Mr. Garwood ultimately reported their decision back to me in a letter dated December 18, 1990, in which he said, "The Examination Council . . . decided against adding the elapsed time field that you requested. [This decision was] primarily based on the agencies' reluctance to support any changes that could interfere with the timely implementation of the new reporting system brought about by the FIRREA amendments." Nearly 2 years has gone by since that letter was written, and the new reporting system should be in place by now. Still, the agencies have not made any move to release this information. I suspect that it will take a specific mandate from Congress to force them to take what should be a simple step to further fair lending enforcement.

While there have been problems with HMDA data over the years, nonetheless the data have been extremely valuable in documenting the mortgage lending patterns of financial institutions. Through HMDA data analysis, groups have been able to show the problems that exist in the mortgage market. This, in turn, has provided them with an opening for discussions with lenders about ways to improve the situation. Out of these discussions have grown the kinds of programs described above.

Need for Data on Small Business Lending

Money for mortgages is only one of many types of credit needed by low and moderate income and minority communities. Credit needs assessments have also turned up the need for consumer credit, student loans, and, most importantly, small business credit. Small businesses play an extremely significant role in the health of a community, be it urban or rural. They create jobs—and thereby income—for community residents, and they bring the kinds of goods and services into a community that make it a desirable place to live. Without credit, the neighborhood business sector will stagnate and wither.

Talk to the members of any neighborhood business association and you are likely to hear horror stories about problems with access to credit. They will tell you how hard it is to get a loan, especially a small loan, to start a business, expand a business, or just to weather the off-season or a temporary economic downturn. They will also tell you that it is particularly hard for minority and women business owners to get a loan. However, it is impossible to document the form and extent of this problem, because lenders have historically not been required to make public information about their small business lending.

Information Also Needed on Small Farm Loans

In rural areas, this problem takes on another dimension, that of the family farm. In some ways, this is the agricultural equivalent to the neighborhood-based small business. Family farms certainly have tremendous problems with access to credit, and have a difficult time competing with large corporate farms for access to financial resources. While lenders do report on agricultural loans, these have not historically been broken down by size, so that it has been impossible to distinguish between lending to agribusinesses and lending to small farms.

Congress took an important step toward remedying this problem last year in the FDIC Improvement Act when it required lenders to provide information on the number and dollar amount of their small business and small farm loans as part of their call reports. This information will give us, for the first time, some insight into the general workings of the small business credit market. FDICIA also required the Federal Reserve to report annually on the availability of credit to small- and minority-owned businesses, including start-ups, and small farms. While it is not yet clear how the Federal Reserve will implement this provision, it too should yield useful information.

More Detail Needed

Despite this good beginning, there is a need for more detailed information, specifically, information on the geographic location of the loans made. The information required by FDICIA will not shed any light on the geographic distribution of small business and small farm credit beyond the general lending territory of the bank. For a large, statewide bank, it will be impossible to tell whether credit is equally available throughout the entire state, in urban, suburban and rural markets.

The report that the Federal Reserve issues annually will not provide information about the lending record of any individual institution or about the availability of credit at the local level. As a result, it is unlikely to provide the kind of tool that community groups need to stimulate discussions with local lenders about ways to improve access to credit for small businesses and small farms. To do this, the information must be broken down by census tract or comparable geographic unit.

Data Also Useful For Examiners

I want to stress that this type of geographic analysis of business and farm credit would be of value not only to community groups and state and local governments, but to examiners as well. As things stand now, it is difficult for examiners to measure a lender's performance in meeting small business and small farm credit needs. While technically they have access to all of a bank's files, in reality it is generally not practical for them to undertake a comprehensive analysis of any type of loan that is not geocoded in advance. Limitations on time and personnel simply do not make this possible. Therefore, geographic reporting of small business and small farm credit would prove to be a tremendously powerful tool for the examiners.

Bankers have sometimes complained that the emphasis in CRA enforcement is on housing credit, despite the fact that the regulations refer to small business and small farm credit, and despite the fact that the agencies have stated clearly their belief that CRA does not require a lender to offer a particular type of credit. These bankers say that, even though they are not in the mortgage business, they don't get adequate credit for the small business loans they make. It is my belief that the reason for this apparent emphasis on housing loans is the availability of information on that type of lending and the near total absence of systematic, geographic information on any other type of lending. As a result of this gap, it is nearly impossible for anyone, either inside or outside the regulatory agencies, to adequately measure a bank's performance in any area other than housing loans.

DEFICIENCIES IN THE CRA ENFORCEMENT PROCESS

Responsibility for enforcing the CRA falls to the four federal banking regulatory agencies. Since the enactment of the law, community groups have complained that enforcement was lax, at best. That view has also been expressed by members of Congress. In 1988, in opening up the first Senate oversight hearings on CRA enforcement, Senator William Proxmire, author of CRA, stated:

> "Let's face it. Redlining hasn't disappeared. Neighborhoods are still starving for credit. Too many bankers still think the grass is greener elsewhere. . . .
>
> Regulators seem to think that we're all living in Lake Wobegone. Like the children of the fictional village, U.S. lenders are all above average. Almost all get high ratings year after year and almost none is ever held back.
>
> The committee surveyed CRA rating procedures and found that more than 97 percent of all lenders passed with flying colors. What's more, in the last 10 years, only 8—that's 8 of 40,000 applications reviewed by the agencies were denied. I wish we had graders like that when I was in school.
>
> And I ask myself, how is it that so many neighborhoods are continuing to fail while so many lending institutions are continuing to pass. This record, needless to say, raises questions about whether the examination process has succeeded."

Recent Significant Changes in CRA

Partly as the result of the record developed in those hearings, in 1989, Congress enacted two extremely significant changes in the Community Reinvestment Act. Those changes, which were part of FIRREA, required the regulatory agencies to disclose the CRA ratings that they assign to the institutions they regulate, and to make public an evaluation report that essentially provides an explanation of the rating assigned. Congress hoped that by shedding a little light on a rating process that had previously been conducted in secret behind closed doors, it would create a higher level of CRA accountability for both lenders and regulators.

Now, 2 years later, it is appropriate to ask how well those changes are working. In my view, the answer is that the record is mixed.

More Attention Paid to CRA

There is absolutely no question that both the industry and the agencies are devoting significantly greater attention to CRA than in the past. Practically as soon as the new legislation was enacted, community groups across the country began hearing from bankers who had never given them the time of day before. For those groups that hadn't followed the legislation, a light bulb often went off when they learned about the new CRA provisions. All of a sudden they could understand why their local bankers, who had been so indifferent in the past, were so eager to take them out to lunch. The level of outreach by bankers to community groups took a major leap upward. But the question remains, has this increased outreach led to an increase in loans on the street?

Is More Enough?

It is obviously difficult to provide a quantitative answer to that question, but I believe that the answer is generally no. The Federal Reserve's analysis of the 1990 HMDA data, for example, showed that nationally minority applicants were 2.4 times more likely to. be rejected for mortgage loans than white applicants. And an affluent African-American applicant was more likely to be rejected than a low income white. Subsequent HMDA studies in cities across the country have continued to show the same patterns. Minority applicants have less access to mortgage credit than white applicants at the same income levels, and low income and minority neighborhoods continue to receive far fewer mortgage loans. The exceptions to these rules are places where community groups have taken it upon themselves to actively monitor compliance with the law.

What does this say about the regulators, then, and the amount of attention they devote to CRA enforcement? The numbers indicate that they are devoting more resources to CRA than in the past. At the FDIC, the average time spent on a CRA exam went from 7 hours in 1989 to 30 hours in 1991. While this is a sizable increase, it is still modest in comparison to the average of 597 hours spent on a safety and soundness exam. At the Office of the Comptroller of the Currency (OCC), the total hours spent on CRA exams increased from 12,064 in 1989 to 84,840 in 1991. Again, this is modest in comparison to the 1,707,024 hours devoted to safety and soundness examinations last year. The Federal Reserve and the Office of Thrift Supervision also showed similar increase's, in all but the largest institutions. The number of hours devoted to CRA exams in institutions over $1 billion actually dropped at those agencies, a phenomenon that I am at a loss to explain.

What about CRA ratings? Testimony presented in the 1988 hearings indicated that 97 percent of all banks received a passing grade on their CRA exams. That number has dropped somewhat. Current figures show that 10 percent of the banks rated have received an outstanding rating, 79 percent have received a satisfactory, 10 percent have been rated needs to improve, and 1 percent are judged to be in substantial non-compliance. So, while 97 percent or more used to get a passing grade, now that number is 89 percent. This is movement in the right direction, but the movement hasn't gone far enough. I would hazard a guess that if you took a poll of community groups in this country and asked them to rate their local banks, you would find they would use the same four numbers as the regulators, but in a different order. They would probably find 1 percent of the banks to be outstanding, 10 percent to be satisfactory, 79 percent that need to improve, and 10 percent in substantial non-compliance. Their judgment would be based on their experience in their hometowns, where they see banks and regulators paying more attention to marketing and outreach, but not necessarily to actual lending. The bottom line is that when it comes to giving grades on CRA performance, the regulators are still far too lenient.

What Are The Standards?

One of the reasons for the discontent over the ratings is the lack of articulated standards for evaluating banks. The CRA regulations spell out which elements of bank performance the examiners should investigate, but not what level of performance will rate an "outstanding" versus a "satisfactory," etc. Even bankers complain about this lack of explicit standards. In fairness to the agencies, it would be very difficult to devise a pre-set scheme that would adequately address the very different sizes, locations and types of institutions that exist in this country. What's needed, then, is a clear explanation of why a particular examiner decided to give a particular bank a particular rating.

It was Congress' hope that this is exactly what would happen when it required the agencies to disclose the CRA evaluation reports and specified that the reports should address the bank's performance with respect to each of the 12 CRA assessment factors, and provide facts to support the examiner's conclusions. Unfortunately, what we got instead was a lot of conclusions and very few facts.

I have attached to my testimony copies of two CRA evaluation reports prepared by the Southwestern District Office of the OCC. One of these reports is for Texas Commerce Bank–Dallas, N.A., which was rated satisfactory. The other is for Texas Commerce Bank–Rio Grande Valley, N.A., which got an outstanding rating. These two evaluations illustrate a number of common problems with the reports.

Which Bank Is It?

First, it appears that, in an attempt to insure consistency in evaluations, the examiner has instead achieved near anonymity. By this I mean that, despite the fact that these two banks serve extremely different markets—one, a major urban area and the other, a rural and heavily agricultural area—the evaluations do not reflect this difference in any way. In fact, it appears that the examiner worked from a single text for both reports, and simply filled-in different adjectives.

For example, under Assessment Factor A (activities conducted to ascertain credit needs), the report says the following about the Rio Grande Valley Bank:

"The bank has effectively determined the credit needs of its entire community, including low- and moderate-income neighborhoods. This determination is based upon direct customer contact by bank personnel, the officer call program, and input from board members. The bank's officers, directors and employees are very involved in the community and frequently meet with various organizations to solicit opinions on the best ways to service the community's credit needs."

This is what the report about the Dallas Bank says about that same assessment factor:

"The bank has adequately determined the credit needs of its entire community, including low- and moderate-income neighborhoods. This determination is based upon direct customer contact by bank personnel, the officer call program and input from board members. Frequently, officers and directors meet with various organizations to solicit opinions about the best ways to service the community's credit needs."

It is left to the reader to determine what makes the difference between "effectively" determining credit needs and "adequately" determining credit needs. The same is true of virtually every assessment factor.

Process vs. Performance

A second problem illustrated by these two evaluations is the overemphasis on the banks' outreach, marketing, and internal management systems, and the underemphasis on actual lending. Although there are three CRA assessment factors that address the institution's lending performance, nowhere in either of these evaluations is there a reference to how many loans of any type either bank made. This is not going to help anyone understand what standards the examiner used to evaluate the banks' performance.

In cases where some numbers are included in CRA evaluations, they tend to be inconsistent. For example, the report might say how many mortgage loans were made in low and moderate income census tracts, but not how many mortgages were made across the board, or what percentage of housing units are in the low and moderate income census tracts, so that it is difficult to interpret the meaning of the first number. Then the report might go on to say what the bank's market share of small business loans is, making it impossible to compare the banks' mortgage lending activity to its small business lending activity. Hopefully, with the provision in the FDIC Improvement Act that requires examiners to provide not just facts, but facts "and data" to support their conclusions, this will change. I fear, however, that Congress may ultimately need to specify exactly what types of data should be included before we will get information that will enable us to compare the performance of lenders in a meaningful way.

Inadequate Enforcement of Fair Lending Laws

A third concern that these reports highlights is the adequacy of the agencies' fair lending reviews. In describing the geographic distribution of the Dallas Bank's loans, the report notes that there is a "disproportionate pattern with respect to activity in north Dallas compared to south Dallas." Those familiar with Dallas will tell you that south Dallas is where the minority community is located. This kind of pattern ought to be an indication to the examiner of discriminatory practices or possible effects test problems. Yet, under Assessment Factor F (evidence of prohibited discriminatory or other illegal credit practices), the report states, "The bank is in substantial compliance with all provisions of anti-discrimination laws and regulations. . . . This review disclosed no instance of discriminatory practices in the bank's delivery of its products and services."

There are numerous other examples of reports that cite policies or practices that civil rights experts would call discriminatory, but where the examiner seems to find no evidence of discrimination. Equally disturbing are cases where repeated violations of fair lending laws are cited, but no evidence is provided that action was ever taken by the regulator to rectify the situation. This and other evidence raises serious questions about the banking agencies' ability to effectively enforce these laws. CCC has suggested in the past that the nation has waited long enough for the agencies to take these enforcement responsibilities seriously, and that the time has come to give those responsibilities to an agency that will do the job. That recommendation still stands.

Rural Areas Ignored

A fourth problem in the CRA evaluations arises with respect to the assessments of large banks that cover both urban and rural markets. The reports for these institutions tend to focus on the bank's activities in urban areas, where there are more programs and organizations to work with. In contrast, rural areas barely rate a mention.

An example of this is the evaluation for the Bank of America, which received an outstanding rating. This is the lead banking subsidiary of the third largest bank holding company in the country. BofA claims the entire State of California as its CRA territory, and it has approximately 850 branches across the state. BofA's CRA evaluation is 11 pages long. In the entire document, there are only *two* references to the bank's activities in rural areas. I quote them in their entirety. Under Assessment Factor I (the bank's purchase and origination of housing, small business and small farm loans in its community) we are told that it has a very good volume of mortgage and consumer loans, and that "(t)he bank also extends a sufficient volume of agricultural loans including credit to small farms." Under Assessment Factor J (the bank's participation in governmentally insured, guaranteed or subsidized loan programs), we are given a list of seven programs, including "Farmer's Home Administration." Not another single mention is made of anything the bank does in the rural areas in California.

Even more disturbing is the case in which a large, statewide bank has a mediocre performance in urban areas and its inadequate performance in rural areas still doesn't earn it a less than satisfactory rating. A case in point is NCNB National Bank of North Carolina (now NationsBank), the lead bank in what is now the NationsBank system, the fourth largest holding company in the country.

It is clear from reading the evaluation that the examiner was not overly impressed with the bank's performance in the cities of North Carolina. We read that the bank has not fully implemented its methods for determining community credit needs, that the Board of Directors has not played an active role in monitoring CRA performance, that the bank has not evaluated the effectiveness of its marketing efforts, and perhaps not surprisingly, that the bank's special home improvement loan product for low and moderate income people has not generated many applications.

When it comes to NCNB's record in rural North Carolina, we are told that "the bank does not actively participate in government lending programs specifically for small businesses and small farms." Also, "the bank lacks an operative system to analyze the geographic distribution [of its credit extensions, applications and denials) in rural areas." We learn that NCNB addresses rural credit needs primarily through its community development programs, but in the description of the bank's community development corporation, we are told that while it has been active in Charlotte and Raleigh, "in the rural and small markets, the bank has not consistently participated in such programs and projects."

If this were a small bank whose only branches were in a rural area, one would expect these comments to earn it, at best, a "needs to improve." Yet, even though NCNB's performance in the urban parts of the state was much less than stellar, the fact that it was not doing an adequate job of serving the rural areas in a state like North Carolina was not considered sufficient to bring its rating down even a notch. If this is the case, how can an underserved rural area ever expect to compete with an urban area where a bank was doing a halfway decent job? It appears that, in the case of a large bank serving both urban and rural areas, as long as the bank is doing a few things in the cities, it can virtually ignore the rural areas with impunity. This does not bode well for the credit needs of rural America.

Special Problems for Indian Reservations

Within rural areas, it is beginning to appear that a special area of neglect in CRA enforcement is lending on Indian Reservations. One example of this is provided by the evidence about First Interstate Bank of Montana, in Colstrip, Montana uncovered two years ago by Native Action, a group representing residents on the Northern Cheyenne Indian Reservation. Native Action looked at the CRA statement of the bank in Colstrip, which is very close to the reservation, add discovered that the bank had delineated its community in such a way as to exclude the reservation. Apparently the bank's examiners had never noticed this violation of CRA, or had never taken any action against the bank as a result. When Native Action brought this problem to the bank's attention, it redefined its community delineation to include the reservation, but labeled it as a "secondary lending area," a term that does not exist in CRA terminology, but that smacks of a "separate but equal" approach to the residents of the reservation. As the result of a subsequent protest brought by the Native American group, the FDIC has increased its regulatory scrutiny of the First Interstate Bank in Colstrip. But why didn't the FDIC ever find or address this problem on its own?

A second example of this type of problem can be found in the Navajo Nation. Representatives of the tribe recently took a look at the CRA evaluation of Sunwest Bank of Gallup, New Mexico, which does include part of the reservation within its delineated community. In fact, the area on the reservation that falls within the bank's lending territory has about 78,000 people, according to the estimates of the Navajo Nation. This compares to some 19,000 people in Gallup.

Sunwest received an outstanding CRA rating from its regulator, the FDIC. In its evaluation, the bank is praised for its outreach and ascertainment activities, "The bank actively seeks out meaningful contacts with a wide range of groups representing most facets of its local community. It has established productive relationships with governmental and private developers. . . ."

None of this contact has been with representatives of the Navajo Nation, and the tribal government had never, at the time of the evaluation, been contacted by anyone from the bank. How is it that the FDIC examiners can overlook such a significant gap in a bank's CRA performance? I cannot provide an explanation, but to me this represents more than just a problem with the way CRA evaluation reports are written. It is one more example of the agencies' lack of rigor in undertaking their CRA enforcement responsibilities.

Credit for a Good Attitude

A fifth problem with the evaluations is the common occurrence of regulators apparently giving banks credit for efforts that they intend to undertake or their willingness to explore or consider certain types of loans or activities. This appears to be the case even when no evidence is provided that the bank has ever taken any exploratory steps, or that such exploration has ever resulted in any loans actually being extended. This flies in the face of the agencies' 1989 Joint Policy Statement on CRA, which states on page 18, "Commitments for future action are not viewed as part of the CRA record of performance of the financial institution." There are numerous examples of evaluation reports that appear to ignore this policy.

Agencies Take Limited View of Audience for Reports

A sixth problem illustrated by the CRA evaluations is indicative of a larger issue, namely, the agencies' extremely limited view of the use for which CRA evaluations were intended. The committee report accompanying these provisions in FIRREA clearly states that the purpose of requiring public disclosure of the evaluations was, "to promote enforcement of CRA by allowing the public to know both what regulatory agencies are telling depository institutions and what the community reinvestment records of particular depository institutions are." That is, the purpose was not just to let an individual learn how his or her local bank was rated, but also to help the public understand how the agencies were going about the business of CRA enforcement.

The way these reports are written generally assumes that the reader is familiar with the institution and the community in which it is located. In most cases, no background information about either is provided. However, even from the beginning, the public's interest was much broader. People wanted to know how all of the banks in their city or their state stacked up against each other. As interstate banking activities have expanded, this interest has broadened.

For example, in the case of the recent merger between NCNB and C&S/Sovran that resulted in the creation of NationsBank, people in Washington, DC, where Sovran had a presence, wanted to know how NCNB's banking subsidiaries had performed in places ranging from Baltimore to Houston. Getting the reports was no small task. Yet when they read them, the groups found those reports were not very helpful, because they assumed the reader was familiar with the city where the bank was based. There are some exceptions to this rule, reports that provide a thumbnail description of the bank and the community in which it is located. Even for the reader familiar with the locale, this background provides useful insight into which aspects of the local market the examiner believed to be significant. Among other benefits, this may prompt some readers to bring to the attention of the examiner significant factors that he or she may have overlooked. We recommend that the agencies make this standard practice.

Reports Hard to Obtain

The agencies' narrow interpretation of the use of CRA evaluations is also reflected in the system they set up to disseminate the reports. Since it is their expectation that these reports will largely be used by individuals who want to know how their particular bank was rated, their dissemination system assumes that the public will obtain the reports directly from the banks.

It is extremely important to have an alternative system for obtaining the reports other than directly from the banks. In a major metropolitan area, the task of tracking down reports from tens of institutions is daunting, at best. It is still the case that many bank employees are not familiar with the rudiments of CRA. They do not distinguish between CRA statements and CRA evaluations, and do not make it easy to obtain either. In addition, since institutions only have to make the report available at a single branch in a metropolitan area, the distances one must travel to obtain reports can be considerable.

Special Problems in Rural Areas

In small towns and rural areas, the problem can be much different. There, asking for a CRA statement, let alone an evaluation, may be viewed by the bank as a hostile or suspicious act. Unless there is another way for people in such locations to get the reports, they might as well not be available at all.

When community groups pointed out to the regulators that there was no way to tell when a particular bank had been rated, and therefore no way even to know when to ask for a copy of its evaluation, the agencies begrudgingly agreed to issue periodic lists of banks whose ratings had been made public. However, they refused to include on the list either the actual rating, or an address for the bank. After further urging from community groups, these changes were made.

Nonetheless, the process still falls far short of the mark. Each of the agencies has a different system for making the lists and the reports available. Some have a centralized system, others require interested parties to contact each of their regional offices. Some issue lists weekly, others monthly or quarterly. The OCC and the FDIC, in my experience, are more helpful than the other agencies. However, this is hardly the system one would expect from agencies eager to get CRA evaluations out to the public. All of this is in stark contrast to the system for disseminating call reports. For these, there is a single 800 number that one can call to order the reports for a nominal fee. We recommend that a similar system be set up for CRA evaluations.

The problems with the CRA evaluations have serious implications for other aspects of CRA enforcement. In their 1989 Joint Policy Statement on the Community Reinvestment Act, the agencies stated that, in considering applications from insured depository institutions, "the CRA record of the institution, as reflected in its examination reports, will be given great weight. . . . A favorable CRA examination . . . is an important, and often controlling, factor in the consideration of an institution's record."

Although the statement goes on to say that the evaluation is not conclusive, and that the agencies will consider significant and supported allegations from commenters, this no longer appears to be the practice. The decisions rendered by the Federal Reserve in last year's "mega-mergers" indicate otherwise. In at least two of those cases, commenters did raise serious questions about the banks' performance, and offered concrete evidence of their concerns. The Federal Reserve did not refute, or even explore those allegations in its orders. Rather, it simply offered examples of good things the banks did. These applications involved some of the largest bank holding companies in the country. It is no surprise that they could point to a few good programs or projects among some of their subsidiaries. However, the commenters in these cases were arguing that these few programs were not sufficient to discharge that banks' CRA obligations and that the Board should take further action in the context of these applications. The Board never even responded to the allegations made, it simply approved the applications. If this is the trend, that as long as a bank can point to something it has done under CRA, it doesn't matter how serious the allegations made by the community, then the Community Reinvestment Act will soon be obsolete. This trend must be reversed.

RECOMMENDATIONS FOR IMPROVEMENT

To summarize, we believe that the following steps would lead to a much improved CRA enforcement process:

1. The agencies should be much more aggressive in monitoring banks' compliance with the Home Mortgage Disclosure Act, and should impose sanctions on lenders who repeatedly submit inaccurate data.
2. The agencies should take immediate steps to make the raw HMDA data available to the public on floppy disks, broken down by metropolitan area, and by individual lender. They should also provide information on the time elapsed in processing applications.
3. Lenders should be required to make available to the public more detailed information on the geographic location of their small business and small farm lending, and on their loans to minority-owned businesses.
4. The agencies should use much tougher standards in evaluating banks' performance under CRA. The reports should not emphasize process over performance, but should evaluate both.

5. CRA evaluation reports should contain information that provides the reader with hard data about the bank's lending activities. This information should be consistent across loan categories and types of lenders, so as to allow for meaningful comparisons.

6. When a bank's lending territory includes both urban and rural areas, the CRA evaluation should provide a separate discussion of the bank's performance in both types of areas.

7. Evaluation reports should contain some basic information about the bank and its community, since not all readers will be familiar with this information.

8. The system for disseminating CRA evaluations should be improved. The process should be standardized and centralized, and the public should be able to call a single 800 number to request copies of the reports.

9. The agencies should use all of the tools at their command, from supervisory agreements to cease and desist orders, to enforce CRA. They should not rely only on the applications process to provide an opportunity to impose sanctions on an institution that fails to perform.

10. The agencies must give more than lip service to their stated policy of considering serious allegations made by those who file comment about a bank's CRA performance. Given the severe flaws in the examination process, it is a serious mistake to overemphasize a bank's rating, as now appears to be the case.

IMPACT OF LEGISLATIVE PROPOSALS TO EXEMPT CERTAIN BANKS FROM CRA

There are a number of legislative proposals currently pending that would drastically change the way that CRA works. These proposals generally fall into two categories. One would exempt from CRA "protests" or "challenges" any institution that received either a satisfactory or an outstanding rating. This is generally referred to as a "safe harbor." The second would either set up a self-certification process or exempt small banks from the law altogether. The self-certification proposal is a bad idea on its face. It is inconceivable that any institution would ever say it qualified for less than a satisfactory rating.

The rationale behind the safe harbor proposal is that a positive CRA rating ought to mean something. If a bank gets a satisfactory or better rating, it ought to get something in return, namely, protection from any objection to its expansion plans based on its CRA performance.

This proposal, if enacted, would have an extremely detrimental impact on CRA. To begin with, it would effectively exempt 89 percent of the industry from coverage under the law.

Most importantly, such a move would simply be bad public policy. CRA protests are nothing more than comments about a bank's CRA performance that are submitted to its regulatory agency in connection with an application for expansion. CRA is one of several factors that the regulators must considers when evaluating an application. They routinely receive comments on many of these factors, although one never hears about "managerial protests" or "competitiveness challenges." Even CRA challenges are relatively rare. In the last four and a half years, the agencies, which process thousands of applications annually, received a total of 207 CRA protests. In the overwhelming majority of cases, no CRA issues are raised by commentors, regardless of the bank's CRA rating.

Imperfect Evaluation Process

The agencies admit that the CRA evaluation process is less than perfect. When they conduct a CRA exam, they rely heavily on information provided by the bank itself, and do not routinely check all, or even much of, that information with outside sources. In the case of a large institution with branches in many markets, they examine only a sample of those branches. The OCC, FDIC and OTS don't even have any specific procedures to direct examiners in determining how many branches or which ones to visit. They have historically relied on the public comment process to bring to their attention matters that the examination missed, or concerns that have arisen since the last examination was conducted. The latter is important, since in the case of the OCC, it can be as long as 7 years between CRA exams. It is incumbent upon the regulators, under our standards for administrative procedures, to develop as complete a record as possible on each application they process.

Knowing that exams can miss important evidence about a bank's performance, and that it can be a long time between examinations, it makes no sense to prohibit the agencies from considering public comments that would provide them with a more complete assessment of an institution's performance to consider in the context of an evaluation. This is especially true since the only sanctions available to the regulators under CRA are to deny or impose conditions on the approval of an application. A safe harbor provision would totally cripple a law that already carries very few enforcement options.

Small Bank Exemption

Recently, there have been a lot of complaints about CRA from some segments of the banking industry, particularly small and rural banks. It is important to look at these complaints closely, and to separate out fact from feeling. For there is no question that feelings are running high about CRA these days among small bankers.

The "I Am, Therefore I Comply" Theory of CRA

First, some facts. There are a number of pending legislative proposals that would exempt small banks from CRA. They use various asset sizes, and some speak to the size of the towns in which the bank's branches are located and to the bank's loan to deposit ratio. Depending on the precise formula used, estimates are that these exemptions would apply to anywhere between 87 percent of the industry and 24 percent. But they are all based on the same rationale, the assertion that small banks automatically, by their very existence, comply with CRA and should therefore be exempt. The argument is that in small communities, if the bank doesn't serve its local community, then it can't stay in business. You might call this the "I am, therefore I comply" theory of CRA.

There is simply no evidence to support this theory, certainly not for all small banks, either in rural or urban areas. First of all, not all small banks are active lenders. Some have very high levels of investments in government securities and Fed funds. They may be flourishing, but it's not because they're serving their local communities. The staff of the House Banking Committee recently looked at the ratio of domestic loans to total assets of various sized banks. They found that the smaller the bank, the lower it's loan to asset ratio. For banks over $10 billion in assets, this ratio was 63 percent. For banks under $100 million in assets, the ratio was only 55 percent. (See *Analysis of Banking Industry Consolidation Issues,* Staff Report to the Committee on Banking, Finance and Urban Affairs of the House of Representatives, March 12, 1992.)

Second, even those who are in the lending business may not be fulfilling their obligations under CRA. It is perfectly possible for such banks to make loans in their local communities and never make a single loan to a poor person or a minority. If the "I am, therefore I comply" theory were true, one would expect to see small banks getting superior CRA ratings. Yet, just the opposite is true. Based on figures reported to this Committee, banks under $25 million in assets represented 34 percent of all banks examined for CRA compliance since July 1, 1990. These banks received 34 percent of all of the outstanding ratings given out, and 44 percent of the substantial non-compliance ratings. (These figures do not include banks regulated by the OCC, which doesn't break out ratings using this size category.) Banks under $100 million in assets constituted 74 percent of all banks examined. They got 75 percent of the substantial non-compliance ratings awarded, and only 56 percent of the outstanding ratings.

The Myth of Regulatory Burden

A second rationale that small banks offer to justify their exemption from CRA is that it requires them to spend a lot of time documenting things they do anyway in the normal course of business. They claim that it imposes undue and unnecessary regulatory burden. We have already seen that there is no evidence that their normal business brings them into compliance with CRA. Nonetheless, they are joined in their complaints about regulatory burden by banks of all sizes. The fact of the matter is that there are very few regulatory requirements for banks under CRA. Banks must adopt a CRA statement, post a CRA public notice in their lobbies, and maintain a CRA public file. The agencies' estimates of the amount of time it takes to fulfill these requirements run from one hour a year to eight hours. Hardly a burden.

It's also a fact that, compared to other regulatory requirements, both on the safety and soundness side and on the consumer compliance side, the resources required to comply with CRA are minor. This is borne out by a study of consumer compliance costs done last year by the Office of Management and Budget. OMB looked at the time involved in complying with a variety of consumer regulations for 1,014 state chartered banks regulated by the Federal Reserve. CRA was at the very bottom of the list. According to OMB, it took the banks an average of six hours to comply with CRA.

Despite the fact that CRA is not a big ticket item, 7 out of 10 respondents to a recent American Bankers Association survey cited CRA as their greatest regulatory concern. This isn't such a surprise when one looks at the question asked by the survey. It listed 12 laws and regulations, with CRA at the top of the list, and then asked, "Which of these gives you, as CEO, the most headaches?" One doesn't have to be a PhD to realize that this is not exactly unbiased research. More important, the question didn't elicit any meaningful information about any purported burden associated with CRA compliance, merely the respondents' emotional reactions.

Nonetheless, it is obvious that the banking industry has taken a serious dislike to CRA. Why is this?

Change Creates Anxiety

I would suggest two primary bases for these complaints. The first is that we are going through a period of change with respect to CRA. We are just two years into the new CRA system, under which CRA evaluation reports are made public. Just under two thirds of the banks and thrifts in the country have been examined since July 1, 1990. For these banks, as well as for those yet to be examined, there has been a certain amount of anxiety about what the public rating process would be like, and more importantly, what their own institution's evaluation would say. It's not surprising that the uncertainty surrounding the change in the process would give rise to a lot of complaints.

Messages from the Regulators

A second source of frustration for banks may be the messages they're getting from their regulators. First, they're hearing that there is no right answer on the CRA exam—no guaranteed way to get an A. Second, they're hearing, "if it isn't documented, it didn't happen." Neither of these make banks happy.

Much of the beauty and strength of CRA over the years has been the way it allows banks to tailor their activities to their local market conditions and the type of business they are in. But this flexibility also means that when banks ask their regulators for specific instructions about CRA compliance, what they get back is general guidance and suggestions about the process to go through, but not what the outcome should be. While this is proper, it's not surprising that bankers also find it frustrating, and that they complain about the lack of certainty.

Documentation vs. Verification

What about the message the regulators are sending about documenting CRA activities? The community groups that we work with want examiners to verify what the bank claims to be doing under CRA, not just to take the bank's word about it. That's because they've all had the experience of banks making false or misleading claims.

If documentation enables the examiner to get the true picture, and to focus on the bottom line of lending performance, then groups are all for it. If not, then maybe it needs to be revisited, and replaced by some other form of verification. But there is no question in my mind that groups agree with the principle behind documentation: that the examiner shouldn't just take the bank's word about its CRA activities—just like the examiner doesn't take the bank's word about compliance with any other regulation. But if a bank is spending a lot of time and money documenting activities that have no relevance under CRA, its no surprise that they would feel pretty frustrated, and verbalize that frustration.

What the Agencies Have to Say About Documentation

If bankers are spending a lot of time on unnecessary documentation, they must not be paying attention to what the regulators have to say on the question. The agencies have made it abundantly clear that the documentation they require is what the bank would prepare for its own internal use in the normal course of business. For example, to quote from a June, 1992 statement issued by the agencies, "The documentation expected by the agencies is primarily that which is useful to the institution's own management needs." The statement goes on to recognize explicitly the difference in resources available to small and large banks by saying, "The agencies are mindful that CRA-related documentation will generally be less formal and less extensive in small and rural institutions than in larger, urban institutions." Any bank should want to know how many loans it is making, who its borrowers are, and where they are located. I'm not sure I'd want to do business with an institution that considers this information to be a burden.

Bad Advice From the ABA

Indeed, the source of the problem may be the industry itself. The American Bankers Association offers its members a guidebook on how to comply with CRA. The guidebook, itself 475 pages long, suggests that banks should maintain 15 separate files on CRA compliance, with a variety of subfiles. To help banks fill up all these file folders, it offers more than 80 pages of sample forms to use. No wonder the industry is complaining. If they'd only listen to their regulators, their lives would be a lot simpler. Maybe it would help if the regulators, in the CRA evaluations, would criticize banks that spend too much time on the wrong kind of documentation.

EXPANSION OF CRA TO COVER OTHER FINANCIAL SERVICES PROVIDERS

The subcommittee has asked for feedback on the idea of extending CRA to other financial services providers. This is an intriguing idea, but it is also a highly complex question, worthy of an entire hearing of its own. At this point, I would just say that community groups I have talked to are very supportive of this idea, although no one I'm aware of has yet come up with a concrete proposal for how this might be done. My organization would be happy to work with the subcommittee if you decide to explore this idea further.

Mr. Chairman, that concludes my formal written testimony. I will be happy to answer any questions that you or other committee members may have.

PUBLIC DISCLOSURE
COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

JULY 18, 1990

TEXAS COMMERCE BANK–DALLAS, N.A.

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does

not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.

GENERAL INFORMATION

This document is an evaluation of the Community Reinvestment Act (CRA) performance of Texas Commerce Bank–Dallas, N.A. prepared by the Office of the Comptroller of the Currency (OCC), the institution's supervisory agency.

The evaluation represents the OCC's current assessment and rating of the institution's CRA performance based on an examination conducted as of July 18, 1990. It does not reflect any CRA-related activities that may have been initiated or discontinued by the institution after the completion of the examination.

The purpose of the Community Reinvestment Act of 1977 (12 U.S.C. 2901), as amended, is to encourage each financial institution to help meet the credit needs of the communities in which it operates. The Act requires that in connection with its examination of a financial institution, each federal financial supervisory agency shall (1) assess the institution's record of helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operations of the institution, and (2) take that record of performance into account when deciding whether to approve an application of the institution for a deposit facility.

The Financial Institutions Reform, Recovery and Enforcement Act of 1989, Pub. L. No. 101–73, amended the CRA to require the Agencies to make public certain portions of their CRA performance assessments of financial institutions.

Basis for the Rating

The assessment of the institution's record takes into account its financial capacity and size, legal impediments and local economic conditions and demographics, including the competitive environment in which it operates. Assessing the CRA performance is a process that does not rely on absolute standards. Institutions are not required to adopt specific activities, nor to offer specific types or amounts of credit. Each institution has considerable flexibility in determining how it can best help to meet the credit needs of its entire community. In that light, evaluations are based on a review of 12 assessment factors, which are grouped together under 5 performance categories, as detailed in the following section of this evaluation.

ASSIGNMENT OF RATING

Identification of Ratings

In connection with the assessment of each insured depository institution's CRA performance, a rating is assigned from the following groups:

—Outstanding record of meeting community credit needs.

An institution in this group has an outstanding record of, and is a leader in, ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

—Satisfactory record of meeting community credit needs.

An institution in this group has a satisfactory record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

—Needs to improve record of meeting community credit needs.

An institution in this group needs to improve its overall record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

—Substantial noncompliance in meeting community credit needs.

An institution in this group has a substantially deficient record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

DISCUSSION OF INSTITUTION'S PERFORMANCE

—Institution's Rating:

Based on the findings presented below, this institution is rated: Satisfactory record of meeting community credit needs.

I. ASCERTAINMENT OF COMMUNITY CREDIT NEEDS

Assessment Factor A—Activities conducted by the institution to ascertain the credit needs of its community, including the extent of the institution's efforts to communicate with members of its community regarding the credit services being provided by the institution.

The bank has adequately determined the credit needs of its entire community, including low- and moderate-income neighborhoods. This determination is based upon direct customer contact by bank personnel, the officer call program and input from board members. Frequently, officers and directors meet with various organizations to solicit opinions on the best ways to service the community's credit needs. Management also reviews demographic information published by local and governmental agencies. This data is periodically evaluated as part of the needs assessment process.

The bank offers products designed to meet identified credit needs including: Small Business Administration (SBA) loans; residential mortgage loans; and student loans. Management has indicated a willingness to offer and explore conventional products with special features and offer some flexible lending criteria, consistent with safe and sound banking standards.

Assessment Factor C—The extent of participation by the institution's board of directors in formulating the institution's policies and reviewing its performance with respect to the purposes of the Community Reinvestment Act.

The Board of Directors is involved with CRA from policy oversight to strategic planning and marketing. CRA goals and objectives are communicated throughout the bank. Participation by senior management and board members takes the form of: community credit needs assessment; review of CRA lending opportunities; and review of CRA training.

The CRA Statement is reviewed at least annually and fairly represents the types of credit and services the bank offers. The statement is detailed and meets regulatory guidelines.

II. MARKETING AND TYPES OF CREDIT OFFERED AND EXTENDED

Assessment Factor B—The extent of the institution's marketing and special credit-related programs to make members of the community aware of the credit services offered by the institution.

The bank has implemented adequate marketing and advertising programs to inform the community of the products and services it offers. The marketing strategy fairly ensures that banking products are responsive to identified community needs. Advertisements are designed to stimulate awareness of credit services throughout the community, including low- and moderate-income neighborhoods.

Bank personnel generally provide assistance to individuals and groups in understanding and applying for credit. The bank has given consideration to the Spanish speaking portion of the community through specifically designed marketing efforts. Information about the majority of the bank's products and services is available in the Spanish language.

Assessment Factor I—The institution's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community, or the purchase of such loans originated in its community.

The bank has made efforts to address a portion of the community's credit needs. This was accomplished by providing loans to small and minority owned businesses, residential mortgages, and for home improvements. The locations of these credit extensions were generally located throughout the community. The bank, consistent with its CRA Statement, is involved in construction financing to several low cost housing projects and for health care improvements.

Assessment Factor J—The institution's participation in governmentally-insured, guaranteed or subsidized loan programs for housing, small businesses, or small farms.

The bank is a participant with the Small Business Administration (SBA) in the origination of loans to small and medium businesses. The SBA loan program has generated other lending opportunities located throughout the community, including low- and moderate-income neighborhoods. The bank is also active in the governmentally insured and guaranteed student loan programs.

III. GEOGRAPHIC DISTRIBUTION AND RECORD OF OPENING AND CLOSING OFFICES

Reasonableness of Delineated Community

The bank has designated Dallas County as its delineated community. This delineation is reasonable, does not exclude any low and moderate income areas, and meets the purpose and intent of CRA.

Assessment Factor E—The geographic distribution of the institution's credit extensions, credit applications, and credit denials.

The bank's geographic distribution of credit extensions, applications, and denials demonstrates a disproportionate pattern with respect to activity in north Dallas compared to south Dallas. Senior management and the board are aware of the geographic distribution and are taking positive steps to improve. The most significant action taken by management is in seeking approval to open a branch location in south Dallas.

Assessment Factor G—The institution's record of opening and closing offices and providing services at offices.

The institution's banking facilities are accessible to most segments of the local community. To improve accessibility, the bank is seeking a new branch location for south Dallas. Business hours and services are generally tailored toward the convenience and needs of the community. No banking locations have been closed in the last year.

IV. DISCRIMINATION AND OTHER ILLEGAL CREDIT PRACTICES

Assessment Factor D—Any practices intended to discourage applications for types of credit set forth in the institution's CRA Statement(s).

The bank generally solicits credit applications from within its community. The bank has developed written policies, procedures and training programs supporting nondiscrimination in bank lending and credit activities. The bank periodically assesses the effectiveness of these policies and implements improvements when warranted.

Assessment Factor F—Evidence of prohibited discriminatory or other illegal credit practices.

The bank is in substantial compliance with all provisions of antidiscrimination laws and regulations. However, our review did find the bank to be in technical noncompliance with provisions of the Equal Credit Opportunity Act. Management has taken steps to ensure future compliance. This review disclosed no instances of discriminatory practices in the bank's delivery of its products and services. A formalized audit program is in place to ensure proper compliance in these areas.

V. COMMUNITY DEVELOPMENT

Assessment Factor H—The institution's participation, including investments, in local community development and redevelopment projects or programs.

The bank has maintained, through ongoing efforts, an increased level of participation in development and redevelopment programs. These efforts have ranged from providing funding for low and moderate housing to assisting in the relocation of a small minority university.

Assessment Factor K—The institution's ability to meet various community credit needs based on its financial condition and size, legal impediments, local economic conditions and other factors.

The bank has played a role in developing and/or implementing projects promoting economic revitalization and growth consistent with its size and financial capacity. Its participation in these projects has taken the form of loans, financial services and technical assistance.

Assessment Factor L—Any other factors that, in the regulatory authority's judgment, reasonably bear upon the extent to which an institution is helping to meet the credit needs of its entire community.

The bank has engaged in other activities which make a significant contribution to the quality of life in the community. This participation is often in a leadership role or as a member of various city or county organizations. These activities enable the bank to better assess the community credit needs.

ADDITIONAL INFORMATION

As of this review, the bank had submitted an application to open a branch location in south Dallas. A marketing plan was developed for the branch that is consistent with the identified banking needs of this section of the community.

PUBLIC DISCLOSURE
COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

OCTOBER 22, 1990

TEXAS COMMERCE BANK-RIO GRANDE VALLEY, N.A.

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.

GENERAL INFORMATION

This document is an evaluation of the Community Reinvestment Act (CRA) performance of Texas Commerce Bank–Rio Grande Valley N.A. prepared by the Office of the Comptroller of the Currency (OCC), the institution's supervisory agency.

The evaluation represents the OCC's current assessment and rating of the institution's CRA performance based on an examination conducted as of October 22, 1990. It does not reflect any CRA-related activities that may have been initiated or discontinued by the institution after the completion of the examination.

The purpose of the Community Reinvestment Act of 1977 (12 U.S.C. 2901), as amended, is to encourage each financial institution to help meet the credit needs of the communities in which it operates. The Act requires that in connection with its examination of a financial institution, each federal financial supervisory agency shall (1) assess the institution's record of helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operations of the institution, and (2) take that record of performance into account when deciding whether to approve an application of the institution for a deposit facility.

The Financial Institutions Reform, Recovery and Enforcement Act of 1989, Pub. L. No. 101–73, amended the CRA to require the Agencies to make public certain portions of their CRA performance assessments of financial institutions.

Basis for the Rating

The assessment of the institution's record takes into account its financial capacity and size, legal impediments and local economic conditions and demographics, including the competitive environment in which it operates. Assessing the CRA performance is a process that does not rely on absolute standards. Institutions are not required to adopt specific activities, nor to offer specific types or amounts of credit. Each institution has considerable flexibility in determining how it can best help to meet the credit needs of its entire community. In that light, evaluations are based on a review of 12 assessment factors, which are grouped together under 5 performance categories, as detailed in the following section of this evaluation.

ASSIGNMENT OF RATING

Identification of Ratings

In connection with the assessment of each insured depository institution's CRA performance, a rating is assigned from the following groups:

—Outstanding record of meeting community credit needs.

An institution in this group has an outstanding record of, and is a leader in, ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

—Satisfactory record of meeting community credit needs.

An institution in this group has a satisfactory record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and a moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

—Needs to improve record of meeting community credit needs.

An institution in this group needs to improve its overall record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

—Substantial noncompliance in meeting community credit needs.

An institution in this group has a substantially deficient record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

DISCUSSION OF INSTITUTION'S PERFORMANCE

—Institution's Rating:

Based on the findings presented below, this institution is rated: Satisfactory record of meeting community credit needs.

I. ASCERTAINMENT OF COMMUNITY CREDIT NEEDS

Assessment Factor A—Activities conducted by the institution to ascertain the credit needs of its community, including the extent of the institution's efforts to communicate with members of its community regarding the credit services being provided by the institution.

The bank has effectively determined the credit needs of its entire community, including low- and moderate-income neighborhoods. This determination is based upon direct customer contact by bank personnel, the officer call program and input from board members. The bank's officers, directors and employees are very involved in the community and frequently meet with various organizations to solicit opinions on the best ways to service the community's credit needs.

Management also reviews demographic information published by local and governmental agencies. This data is regularly evaluated to ensure the bank remains informed about the community and knowledgable of the community's credit needs. This is the bank's primary method to evaluate the community's needs and how it measures its success at meeting those needs.

The bank offers products designed to meet identified credit needs including: Small Business Administration (SBA) loans; residential mortgage and home improvement loans; credit cards (through an affiliate) and governmentally insured and guaranteed student loans. Management has demonstrated a willingness to offer and explore conventional products with special features and offer some flexible lending criteria, consistent with safe and sound banking standards.

Assessment Factor C—The extent of participation by the institution's board of directors in formulating the institution's policies and reviewing its performance with respect to the purposes of the Community Reinvestment Act.

The Board of Directors is actively involved with CRA from policy oversight to strategic planning and marketing. Senior management is very active in the community and encourages involvement to all bank officers and employees. The bank's CRA goals and objectives are clearly communicated throughout the bank.

Participation by senior management and board members takes the form of: community credit needs assessment; review of CRA lending opportunities; and evaluation of the bank's advertising efforts. Management has also implemented a computer based CRA training program to further enforce the importance of CRA.

The expanded CRA Statement is reviewed at least annually and effectively represents the types of credit and services the bank offers. The statement is detailed, easy to understand and fully meets all regulatory guidelines.

II. MARKETING AND TYPES OF CREDIT OFFERED AND EXTENDED

Assessment Factor B—The extent of the institution's marketing and special credit-related programs to make members of the community aware of the credit services offered by the institution.

The bank has implemented a comprehensive marketing and advertising program which effectively informs the community of the products and services it offers. The marketing strategy fairly ensures that banking products are responsive to identified community needs. Specific efforts are made to ensure that all segments of the community are reached through the bank's advertising efforts. Advertisements are designed to stimulate awareness of the products and services the bank offers throughout the community, including low- and moderate-income neighborhoods.

Bank personnel provide assistance to individuals and groups in understanding and applying for credit. The bank has given consideration to the Spanish speaking portion of the community through specifically designed marketing efforts. Information about the majority of the bank's products and services is available in the Spanish language.

Assessment Factor I—The institution's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community, or the purchase of such loans originated in its community.

The bank has made efforts to address a major portion of the community's credit needs. This was accomplished by providing secured and unsecured loans to small and minority owned businesses, residential mortgages, home improvement financing, and funds for small farming operations. These credit extensions are generally located throughout the community.

The bank, consistent with its CRA Statement, is involved in construction financing for affordable housing, home rehabilitation, and for education improvements.

Assessment Factor J—The institution's participation in governmentally-insured, guaranteed or subsidized loan programs for housing, small businesses, or small farms.

The bank is a participant with the Small Business Administration (SBA) in the origination of loans to small and medium businesses. Although this activity does not represent a major portion of the bank's loan portfolio, it has generated other lending opportunities located throughout the community, including low- and moderate-income neighborhoods. The bank is also very active in the governmentally insured and guaranteed student loan programs.

III. GEOGRAPHIC DISTRIBUTION AND RECORD OF OPENING AND CLOSING OFFICES

Reasonableness of Delineated Community

The bank has designated the city limits of Mission, McAllen, Edinburg, Pharr, San Juan, Alamo, Harlingen and Brownsville as its delineated community. This delineation is reasonable, does not exclude any low and moderate income areas, and meets the purpose and intent of CRA.

Assessment Factor E—The geographic distribution of the institution's credit extensions, credit applications, and credit denials.

The bank's geographic distribution of credit extensions, applications, and denials demonstrates a reasonable penetration at its banking location. No exclusion of low- and moderate-income neighborhoods was noted. Management has adequately documented its loan distribution through a comprehensive mapping program. The bank has identified and mapped its credit applications, approvals and denials. These efforts are regularly updated and the results are presented to the board of directors for their review.

This kind of information is utilized by senior management in rating the effectiveness of the bank's marketing program and for the formulation of new marketing strategies. Management relies heavily on this information when it develops new products and services. The bank closely reviews the geographic distribution in relation to the lending policy.

Assessment Factor G—The institution's record of opening and closing offices and providing services at offices.

The institution's banking facilities are accessible to most segments of the local community. Business hours and services are generally tailored toward the convenience and needs of the community. As of July 2, 1990, the bank has 4 locations located throughout the community. All of the branches are located within low- and moderate-income census tracts. No banking locations have been closed in the last year.

IV. DISCRIMINATION AND OTHER ILLEGAL CREDIT PRACTICES

Assessment Factor D—Any practices intended to discourage applications for types of credit set forth in the institution's CRA Statement(s).

The bank actively solicits credit applications from within its community. The bank has developed written policies, procedures and training programs supporting nondiscrimination in bank lending and credit activities. The bank periodically assesses the effectiveness of these policies and implements improvements when warranted.

Assessment Factor F—Evidence of prohibited discriminatory or other illegal credit practices.

Anti-discrimination laws and regulations include the Equal Credit Opportunity Act, Fair Housing Act, and the Home Mortgage Disclosure Act. This review disclosed no instances of discriminatory practices in the bank's delivery of its products and services. A formalized audit program is in place to ensure proper compliance in these areas.

V. COMMUNITY DEVELOPMENT

Assessment Factor H—The institution's participation, including investments, in local community development and redevelopment projects or programs.

Through ongoing efforts the bank has become a leader in community development and redevelopment projects and programs. These efforts include but are not limited to active participation in the Community Development Corporation of Brownsville, La Joya Water Supply and Affordable Housing Program Inc.

Assessment Factor K—The institution's ability to meet various community credit needs based on its financial condition and size, legal impediments, local economic conditions and other factors.

The bank has played a major role in developing and or implementing projects promoting economic revitalization and growth consistent with its size and financial capacity. Its participation in these projects has taken the form of loans, financial services and technical assistance.

Assessment Factor L—Any other factors that, in the regulatory authority's judgment, reasonably bear upon the extent to which an institution is helping to meet the credit needs of its entire community.

The bank has engaged in many other activities which make a significant contribution to the quality of life in the community. This participation is most often in a leadership role or as a member of various city or county organizations. These activities enable the bank to better assess the community credit needs.

CENTER FOR INVESTIGATIVE REPORTING, INC.

YOUR LOAN IS DENIED, a report on the persistence of discriminatory lending practices in the 1990's, is a co-production of the Center for Investigative Reporting and Frontline. It aired on PBS stations nationwide, June 23, 1992.

YOUR LOAN IS DENIED

NARRATION: South Central Los Angeles, 1992: 1,044 buildings damaged. Sixty people dead. More than $735 million in losses.

SOT: Obviously you gentlemen know this is the Baldwin Hills/ Crenshaw shopping center . . .

NARRATION: After the fires died out a group of bankers came to look around.

SOT: What was this here?

NARRATION: There is an irony in all this. Community activists have long charged that South Central was underserved by banks.

In fact, only 13 branches serve a population of over 250,000 residents.

In nearby Melrose, 90 percent white, with one tenth the population, there are 15 banks.

The issue is race and credit. Do our financial institutions avoid lending because of color?

SOT: Music: "Sweet Home Chicago."

We went to Chicago where FRONTLINE has investigated race and credit for six months. Chicago—America's third largest city—home to one of the nation's largest black communities.

NEWSPAPER BOY: Paper, paper (unintelligible) . . .

NARRATION: Eighty years ago they began coming here in search of the American dream. Today, blacks live in a Chicago at least as divided as the South they left behind.

BILL SCHECHNER: Who lives over here?

BRELAND: Mostly this side, the German Irish.

SCHECHNER: White?

BRELAND: White, ah, basically, east of California would be black.

SCHECHNER: Ok, on this side of California is what?

ALLEN: This side of California is basically, right now it is more black now. It's still a mixture.

SCHECHNER: But over here, on the other side?

ALLEN: On the other side it is basically white.

NARRATION: On the blackside of one of Chicago's colorlines is Englewood, a neighborhood on the south side of the city. There I met Henry Luellan, a retired homeowner. He's lived here half his life.

LUELLAN SOT: I don't know what's wrong with the banks.

NARRATION: Near his house he showed me how a lack of credit hurts a neighborhood.

LUELLAN: The banks have redlined this area and the banks won't lend money into the area for the peoples to rehab and to take care of their property, so what peoples do, they walk out of the neighborhood and they leave the house abandoned. This is a shell now.

SCHECHNER: Mm-hmm. Can you see it, if we went around the back?

LUELLAN: Go around the back, yeah.

SCHECHNER: Yeah, come on.

LUELLAN: Let's walk around the back and I can show you what I'm talking about.

SCHECHNER: Okay, yeah. You live right across the street right?

LUELLAN: I live right in front of this house and this is a sore eye to me. I'm going to show you what I'm talking about here. This house was perfect. It, all of the back was closed in and it had nice windows up there . . .

SCHECHNER: Well, how do you figure that, Mr. Luellan? I mean here's a house and you are telling me that a year ago it was in good shape and it got wrecked, how come nobody just came along and, and bought it.

SCHECHNER: Couldn't get a mortgage?

LUELLAN: Can't get a mortgage in this neighborhood to buy. There's nobody to lend money and if you can't get a mo—if you can't get money, you can't buy a house.

SCHECHNER: Isn't it all over and done with here, I mean isn't it too late?

LUELLAN: No, it's not too late, because if we get money we will rehab these buildings and put them back, put them backs on the tax role. That's what it takes.

SCHECHNER: Now you've lived here for how many years?

LUELLAN: I lived here for 32 years.

SCHECHNER: What goes through the middle of you when you look around and you see what happened?

LUELLAN: I cry. It tears the inside out of me. This was a beautiful neighborhood.

LUELLAN: I mean we need you to give our community services as you give other communities. This is what we asking you. Our problem is, we need banking in the low and moderate income area, where our community is 100 percent black, and everybody have redlined our community.

NARRATION: Luellan fights for his neighborhood through the local chapter of ACORN, a housing advocacy group. Here, ACORN activists meet with representatives of Affiliated Bank of Chicago whose parent corporation is planning a merger with another bank, Comerica. But, mergers need federal approval and approval can be withheld because of local opposition. That gives ACORN a hammer.

MAN'S VOICE: It's not up to us now, it's up to you. You're going to have to deal with us.

LUELLAN: If you don't deal with us, we're going to hold up your merger.

LUELLAN: We need your commitment that you gonna put some service in our community where we show you we are just as trustworthy as any other peoples on the face of the earth. This is all we asking for. We don't want you to give us anything. We, if you lend us money, we gonna pay you back like any other red-blooded American.

WOMAN'S VOICE: You have all your banks's out in the rich part of the city. You have nothing for us.

SCHNEIDER SOT: Does ACORN, do you have your outreach and your programs that you are operating, are you in certain parts of the city or . . . ?

NARRATION: Brenda Schneider is Director of Community Relations for the bank.

SCHECHNER: Is it real. Is racial discrimination in mortgage lending real?

SCHNEIDER: I would categorically say no. I think there are too many factors that go into making up whether or not an applicant does or does not get a mortgage.

SCHECHNER: Is it possible that the people at the meeting were really angry, at the way they've been treated by the banking system?

SCHNEIDER: I would say that your assessment is absolutely right, angry is an accurate description of what I felt listening to them . . . should that anger be vented at financial institutions? I don't believe so . . . financial institutions in and of themselves have a niche in addressing reinvestment patterns in urban cities. But in and of themselves they are not the single way of addressing or resolving all of the urban problems that are facing America.

LUELLAN: What did you bring tonight that you can show us that you are gonna deal with us in good faith?

SCHNEIDER: I think the fact that we are here, the important—

LUELLAN: The fact—

SCHNEIDER: The important thing is that we are here, we are listening, I am taking diligent notes as is Mr. Hammond—it is our intent to respond to you.

LUELLAN: You see, if you don't lend us money, then we got to move in your community and then you got to start running, cause you don't want to stay where blacks live. So why don't you put a branch in Inglewood, so I don't have to give you trouble? Huh?

SOT: Clapping.

NARRATION: Laws protecting consumers against lending discrimination date back to 1968. It was then that Lyndon Johnson signed into law the Fair Housing Act which courts have ruled prohibits "redlining," the practice of denying loans in a particular neighborhood.

LBJ: I urge every American to join in this effort to bring justice and hope to all our people.

NARRATION: Since then, Congress has made several attempts to strengthen fair lending law. In 1974, they passed the Equal Credit Opportunity Act, which outlaws lending bias against individuals. In 1977, it passed the Community Reinvestment Act. The CRA stated that banks had an obligation to serve low and moderate income neighborhoods.

SOT: Stop redlining, neighborhoods first, stop redlining, neighborhoods first, stop redlining, neighborhoods first . . .

NARRATION: Over the years, community groups have used the law to pressure banks to provide more service.

SOT: Stop redlining, neighborhoods first, stop redlining, neighborhoods first . . .

NARRATION: Austin, on the western edge of Chicago, is the type of neighborhood fair lending laws were intended to help. Income here is close to average for Chicago but mortgage investment last year was 35 percent below the citywide average. Austin's population is ninety-one percent minority.

SOT SALDANA: Want to go to the park? Come on . . .

NARRATION: Maria Saldana and her husband, Donald Davidson, know just how hard it is to get a home loan here.

SALDANA: I really thought that this was the house. I mean, I said this is the house. I want a house where the kids will grow up in and it would have memories of our living in a house, and you know, and all the nooks and crannies of a house that only a kid can, can really appreciate.

NARRATION: It would seem that Maria and Donald are good candidates for a loan. Donald is a real estate developer and mortgage banker. Maria earns $69,000 as a lawyer for the City of Chicago. She holds the couples' assets, which according to her attorney, top $1 million.

But they did have trouble. When Maria Saldana, who had earlier received a smaller loan from Citibank, applied to the bank for a $191,000 mortgage/construction loan, her application was denied.

SALDANA: They sent me a letter saying you got turned down for two reasons; one, bad credit history, and two, too many outstanding loans.

NARRATION: Citibank told FRONTLINE Maria Saldana was turned down "due to her credit performance on her own personal loans." Did the bank have a case?

Maria Saldana's credit report included two late mortgage payments two years ago, some credit cards at their limit, and an unpaid six-dollar fee on an old student loan. The rest of her credit report was clean.

Maria didn't see where there should be a problem.

SALDANA: . . . and when I got the credit report and I looked at it, I really couldn't figure out what it was they were talking about cause you know my credit rating for the last 24 months was great. As far as I was concerned, they already made up their minds the minute we walked in . . . I don't think they ever planned to make that loan.

DAVIDSON: But oddly enough, Citicorp is probably the largest lender in black neighborhoods in the city of Chicago. And their average mortgage, if my memory serves me right, is about $45 or $50,000, and I think they've made a conscious decision that they don't like lending in black neighborhoods but they'll do it and they'll do it well because that's the law. But they have defined in their minds a risk level and I think what must have happened was we went beyond their definition of risk level.

NARRATION: After the Citibank rejection, Maria Saldana did get a loan at another bank, First Chicago. Loan officer, Carol Yanowitz, reviewed the same credit report that Citibank had seen, and agreed to loan Saldana $147,000.

YANOWITZ: It is a very common scenario that we see, and we typically ask for someone to qualify, give us reasons if they have slow payments why they happened and in some particular situations we may actually ask for documentation that explains why that's happened.

SCHECHNER: Are you comfortable with the fact that you gave here a mortgage and she will be able to pay it off?

YANOWITZ: Yes, I am.

NARRATION: Yanowitz's boss is Richard Thomas, president of First Chicago.

THOMAS: We are not in the business of knowingly making bad loans. So we have to satisfy ourselves that the loan has a reasonable, more than a reasonable and very high probability of being repaid as scheduled.

NARRATION: One bank says no, another bank says yes. What turns a decision a particular way is not easy to determine. Citibank said Saldana was a bad risk. But, she is considering suing Citibank to find out if there was another reason why her loan was denied.

SALDANA: I went to Stanford undergrad, I got a Berkeley law degree, I have a job that pays $69,000, but somehow, I'm doing something wrong. I thought I was doing all the right things, but I'm not.

NARRATION: It would seem that Peter and Dolores Green are a couple who wouldn't have trouble getting a mortgage either. He's a state employee and she works for a publishing company. They are professional and well paid.

The Greens live in a neighborhood that's on the edge—with board-ups and fix-ups side by side. Keeping people like the Greens here is important.

They want to stay, and in fact, invest here. The Green's had hoped to buy the six-unit apartment building that has been their only home since they were married.

SCHECHNER: Was it an important step for you to buy the house?

PETER GREEN: Yes, it was. I, for me—I will just speak for myself. I think that it was the fact that we had spoken so many times over, about owning that piece of property, and it is really nothing necessarily so beautiful, or what have you, but it's still special in its own way . . .

SCHECHNER: What do you mean?

GREEN: . . . Well, that's where our roots were. We'd been living there for over 30 years so it had a lot of meaning in that regard.

SCHECHNER: Did you ever think about leaving the neighborhood?

PETER GREEN: God yes.

DOLORES GREEN: Yes.

PETER GREEN: That's the one thing that we could have done at any point of time. But we are not quitters, we are not runners. And I think really that's it. We just didn't feel that we had to run.

NARRATION: The Greens earn approximately $60,000 a year between them. They list assets of over $100,000, and they say they are paying all their bills on time.

SCHECHNER: So when you went to the banks to look for a mortgage, what did you think their reaction was going to be?

PETER GREEN: I thought I was white, and let me just explain what I mean by that. I had all of my documents together, the kinds of documents that I knew would be needed in making an application, such as tax returns, description of the property, record of, of where I was doing my banking, record of where I was employed, copy of operating expenses for the building, all of the kinds of things one would normally need if they are going in to make an application for a loan. I fully expected to be treated fairly and receive a mortgage.

NARRATION: But when Green began to contact banks, he says he couldn't even get an appointment. After several trys, a friend suggested the Avenue Bank of Oak Park. The loan officer at the time was John Hill.

HILL: My job at the bank was a little different than the staunch banker. I mean, I was a business developer and when you are a business developer, you want to bring in loans, you want to bring in deals. So I would a lot of times, go out and look at something that a regular banker wouldn't do.

SCHECHNER: Then you went out and visited the neighborhood? Why did you go to do that?

HILL: Before I make the presentation, I like to take pictures. So I just took some polaroid shots of the six-flat, of the neighborhood around, put them inside . . . this is what it's going to look like.

SCHECHNER: What was your impression of the neighborhood?

HILL: Run down. It's one of those that I think I know why he had bought the place, 'cause it's one of those that it's run down to the point where the only place to go is up . . .

NARRATION: The evening John Hill made his assessment he phoned Peter Green.

PETER GREEN: He made mention of the building next door to me, it seeming to be having some problems, mainly in that the structure had had a fire recently, and he raised the question about Jesus, the same thing could very well happen to your property. And I said: "Why didn't you take a look at what's going on down the street?" And I pointed out to him that there were numerous new townhouses that were going up not only in that corner but throughout the general area. He made no mention whatsoever of the positive, he only wanted to apply his thoughts to the building next door.

HILL: Then I submitted it to my boss, Jerry Collins. Jerry Collins took a look at the thing and said, this one you should show to the president, Michael Speziale, see what he thinks of it. So I did. I went and talked to the president, showed him the thing and this took all of about, this took all of about two minutes. And where was it located, you know, I told him a little bit about the neighborhood. And he says: "Do we really have to do this loan?" I mean, no, we don't have to do this loan.

SCHECHNER: How did you find out what happened?

PETER GREEN: I rang up the bank. And I was advised oh, the committee turned your application down.

SCHECHNER: Who told you that?

PETER GREEN: John Hill.

SCHECHNER: Did he give you a reason?

PETER GREEN: No.

SCHECHNER: What did you say?

PETER GREEN: You will be putting that in writing, OK, and you will be indicating as to why.

SCHECHNER: Why was Green turned down?

HILL: Because of the location of the area. If he were a long time client, or, you know, just a client of the bank for let's say a year or a couple of years, again, he probably would not have been turned down.

SCHECHNER: What's the problem with lending money to someone you don't know if they have what it takes in terms of their assets and qualifications?

HILL: Well, it's like, if he were stronger, you know, it's like, the case of like, a banker who really wants to loan the money to somebody who doesn't really need the money. That's a good client. Well he wasn't that strong. You know, but still he was very good. But, I mean, he wasn't that strong that you would go way out on a limb. And going out on a limb is going into a neighborhood that you don't typically go into.

SCHECHNER: How will the bank ever get to know the neighborhood?

HILL: They don't have to. Why would the bank have to do that? They are setting up a service to help the community that in which they are in. Man, there are branches are everywhere. Those branches are supposed to know. I mean you can't go into, there's probably banks in the neighborhood that Mr. Green is concerned about.

NARRATION: There used to be, but no more. In fact, the bank where the Greens were regular customers—the one bank where they may have stood a better chance of getting a loan—that bank moved out.

PETER GREEN: We were customers with this bank probably pretty close to ten years, more or less.

SCHECHNER: What happened?

PETER GREEN: One day we got an announcement that the bank was going to be moving or closing down.

SCHECHNER: Did you go to another one?

PETER GREEN: Yes, same thing happened. That bank moved away. Bank by bank by bank, if you will, at one time serviced this whole area, they just all disappeared.

NARRATION: When a written explanation from Avenue didn't arrive, Peter phoned the bank's president. Dolores took the return call.

DOLORES GREEN: He immediately says to me, "Well, John Hill should never have accepted the application." And I said, "Why not?" And he said, "Well, we don't give commercial loans."

NARRATION: The bank president says Mrs. Green is wrong. He says he told the Greens only that John Hill wasn't authorized to make commercial loans. But when the bank sent the Greens a letter, it gave them no explanation for being turned down. Federal law requires the bank to give a reason for its rejection.

Peter Green lost patience. He complained to the Federal Reserve Board in Washington. He expected a full investigation.

PETER GREEN: Usually in an investigation of the persons who are making the complaint, usually that person is contacted to get their side of the story.

SCHECHNER: But they didn't do that.

PETER GREEN: No. So, ah, I thought that rather strange, ah, not having been contacted and then, yet they wrote back and said, "Well, we don't see anything wrong."

NARRATION: In a letter to the Greens, the agency that investigated, the Federal Deposit Insurance Corporation, FDIC said the problem was a low appraisal. Now there seem to be three reasons the Greens were turned down.

Wrong kind of loan said the bank president.

Wrong side of town said John Hill.

Low appraisal said the FDIC.

We wanted to ask the FDIC and Avenue Bank about the Greens. The FDIC refused to comment. Avenue Bank, in a letter to FRONTLINE, put the blame on their former loan officer John Hill, for not completing the loan application.

PETER GREEN: I'm not Dr. King, I don't want to be thought of as a Rosa Parks, or anything like that, but it appears that there has been a serious problem in this area in dealing with banks for some time. And the FDIC and those other agencies which have been mandated to oversee these institutions, it seems that they are falling short. I'd like to think that there are persons out there who are going to develop enough courage to stand up and say no, not here.

DOLORES GREEN: If it were a case of say, I spoke too loudly or something I could always soften my voice. If um, I dressed in a particular manner I could always buy different types of clothes and change that, but if it's the color of my skin . . .

PETER GREEN: We can't change that.

DOLORES GREEN: I can't change that.

NARRATION: Time and again, the U.S. Congress returns to the issue of race and credit.

SOT HEARINGS: Good morning ladies and gentlemen.

NARRATION: At hearings last month before a House Committee, community activists complained about lax enforcement of the law.

CINCOTTA: The individual cases like I could bring up of the Peter and Dolores Green on the West Side of the city of Chicago, who were discriminated against by a lender . . . the people had impeccable credit . . .

NARRATION: Gale Cincotta has testified before Congress more than a dozen times in the passed 20 years. She is part of an array of community groups, public interest watchdogs, and lawmakers who know this is an old story.

The Federal Reserve is one of four federal regulatory agencies that oversee financial institutions.

Last October, the Fed released the first comprehensive national study of loan discrimination.

SOT LAWARE AT PRESS CONFERENCE: The new data shows that loan approval rates differ among different ethnic, racial and income groups.

NARRATION: The information was collected under the Home Mortgage Disclosure Act of 1975, known as Hum-Dah. The data base was all mortgage applications filed nationwide in 1990.

The study included the following statistics on conventional mortgage rejection rates:

For black Americans the rejection rate was more than twice as high as for whites.

And even more troublesome: high-income blacks were being rejected more often than whites of much lower-income. The debate over what these numbers mean goes on.

John LaWare is a governor of the Federal Reserve.

LAWARE: The most recent HMDA-data which caused quite a stir when that came out last fall, are like a lot of smoke, ah, you got to believe there's some sort of fire down there creating the smoke, but it's hard at this stage of the game to tell just what that is.

NARRATION: The problem, bankers say, is the study did not include information on credit histories and level of outstanding debt. They say further study is necessary to determine whether the numbers show racism or legitimate credit decisions.

But retired Senator William Proxmire, who sponsored the Community Reinvestment Act, says the data is clear.

PROXMIRE: Well, I make plenty of those numbers. Because what it shows was that people with the same income, rejection rate on blacks was more than twice as high. Furthermore, the really, bombshell here was the fact that the blacks who had the highest income were turned down more often than, whites who had the lowest income. Now that's a, that's just the cruelest, most direct, explicit, kind of discrimination on the basis of, of race.

NARRATION: The Fed's numbers also showed that as the percentage of minorities in a community increases so too does the number of loan denial—regardless of income level of the neighborhood.

As the debate about what these numbers mean has continued, this group, the Federal Reserve Consumer Advisory Council, has studied ways, to detect discrimination.

SOT DEBORAH GOLDBERG AT CAC MEETING: . . . we are at least alerted to a problem in the home mortgage-lending field. And we can then take steps to address it. We can argue about what the nature of that problem is, aid what the appropriate steps are, but at least we all agree that there's some kind of problem out there that we should be looking at.

NARRATION: The council includes bankers, academics, and consumer advocates. Last year it considered using testers, paired black and white examiners posing as loan applicants.

Cathy Cloud, a fair housing expert and new member of the council, supports testing.

CLOUD: If you don't make an application there's no paper trail of your visit there so, there's no way to assess the percentage of people who are being turned away, without even having a chance to apply. So testing shows what happens at that stage.

NARRATION: In 1990, Cloud supervised an experimental testing program in Chicago, which showed clear discriminatory behavior.

CLOUD: At a couple of institutions the black testers were not given any information, were not assisted by the loan officer and were told that they would only be assisted when they had completed an application and brought in their application fee as well, paid their money. That did not happen to the white counterpart of the, the minority tester. They were assisted, provided information and encouraged to apply.

NARRATION: But, when the consumer council recommended testing as a way to detect discrimination, the Fed said no.

LAWARE: Now, we have kind of backed off the testing. If you use it generally, to try to pinpoint the problems, the cost is just going to be phenomenal what we, and we have long had the authority for Federal Reserve examiners to use testing if they sense that there is a problem and they want to find out or they want to confirm their judgement.

SCHECHNER: To what extent do they use it?

LAWARE: So far it has not been used.

SCHECHNER: Why not?

LAWARE: Because we have not found evidence that leads us to believe that there is discrimination going on.

SOT HOUSE DEBATE: Mr. Kennedy of Massachusetts.

NARRATION: Last year, after the HMDA was released, a mandatory testing bill reached the House floor. Its sponsor was Congressman Joseph Kennedy of Massachusetts.

KENNEDY: The problem is not bad laws, it's bad enforcement. Bank regulators are asleep at the switch. They treat banks like golfing partners not banks.

NARRATION: But Kennedy's amendment immediately ran into trouble.

CHALMERS WYLIE: The testing program proposed by the Kennedy amendment is a half baked idea. It is a proposal that was rejected by the Federal Reserve Board because it would not guarantee accurate findings, it would be very costly to administer and is unclear who will pay for the cost of the program.

JIM LEACH: It may be the ultimate intrusion in the American system. The problem is real, it's a secret police solution modeled more after the KGB than it is any part of the American model.

SOT: Will the gentleman yield!

NARRATION: But the amendment's co-sponsor, Republican Robert Walker of Pennsylvania, pointed out, testing is routinely used by other government regulators.

WALKER: That's exactly what we are talking about here. Regulators where they find massive violations being able to turn to device to assure that they are right and getting the job done.

KWEISI MFUME: People talk about not being opposed to redlining, well what are we going to do? This is the Congress of the United

States. Let's do something about it. But don't tell me as I've been told all my life and people of African ancestry and Hispanic ancestry, to wait for the next tomorrow, and the next generation, and the next election. We too were endowed with certain unalienable rights, they were life, liberty, and the pursuit of happiness.

NARRATION: But, the support wasn't there. Even though the HMDA data had been released a month earlier, the amendment lost by 89 votes.

KENNEDY: The only way to get at the truth as to whether or not there is discriminatory lending taking place in this country is to get the facts.

MFUME: And as long as the Congress, or the banking institution doesn't really want to go out and find out what's wrong. We'll simply say as the bankers say, well please don't draw any conclusions from subjective data. Well, give me a break. People are hurting, and they can't understand why they are receiving a different standard of treatment.

NARRATION: To Cathy Cloud, the refusal to test is only a sign regulators aren't trying very hard.

CLOUD: When they have complaints of discrimination from bona fide applicants for mortgages, they do not effectively enough evaluate those complaints. They don't refer them to, for example, to the Department of Justice for investigation and for the pursuit of relief for the persons who are victims.

NARRATION: John Dunne is Assistant Attorney General for Civil Rights. His staff prosecutes discrimination complaints. The paperwork forwarded by the regulators has hardly been backbreaking.

DUNNE: We just have not had the complaints. This has been acknowledged by the various regulatory agencies. Now, we're open for business. We're ready to respond, but we're not going to go around the country looking for problems.

SCHECHNER: Why not?

DUNNE: Because . . .

SCHECHNER: Isn't that you're job?

DUNNE: No, it is not our job. We are not investigators in order to try to dig up cases. We are prosecutors when a citizen claims that his or her rights have been violated then we go to court, but we don't just initiate these on our own.

NARRATION: Only one case has been referred to the Justice Department in the eighteen years since the Equal [Credit and] Opportunity Act was passed.

DUNNE: We don't know really why we haven't had many referrals but we're prepared to make up for any failings that may have been there. I'm not prepared to point a finger at a regulatory agency and say you haven't done your job. We don't know enough about that but we know that the result which was intended by Congress to be achieved has not been achieved.

NARRATION: We asked Governor LaWare of the Federal Reserve if the situation means sloppy work by the regulators or that discrimination has disappeared?

LAWARE: I don't know. If I knew the answer, you know, we wouldn't be trying to prove the answer with the investigation and the research that we're doing. We'd be out there sending in special teams to look at areas where we thought it was going on.

SCHECHNER: What can you tell people then that will reassure them?

LAWARE: Kind of like a blood hound without a scent you know. It just, he mills around he doesn't know what direction to go in.

NARRATION: The Office of the Comptroller of the Currency, or the OCC, is another federal bank regulatory agency. It oversees nationally chartered banks.

A lawsuit forced the OCC to set up a fair lending enforcement office in 1978.

Zina Greene was the first director of that office. She says she came to an agency unwilling to change.

ZINA GREENE: The first inclination came the first week. The first thing we had to do was write testimonies for the Hill. And we had to tell them what wonderful things we were now going to do to find discrimination. So, we were going to test, we were going to look for redlining, we were going to do these wonderful things—and at the end we said nothing. We had 10 pages and we said nothing. We didn't mention the word redlining. We didn't mention the word testing. We didn't say a word about what we were going to do, or how we were going to get there.

NARRATION: That was 14 years ago. To learn if things had changed, we spoke to Susan Krause, a Senior Deputy Comptroller at OCC.

KRAUSE: We as you probably know, don't have very many successful cases of discrimination actually brought to conclusion. Ah, so that can be either good news or bad news. We don't find much overt blatant discrimination and we think, and nobody does, I think that, um, there probably isn't much overt, blatant discrimination, but there probably is subtle discrimination that we have a very difficult time finding, and therefore, we're not very far along on enforcement.

SOT GREENE: These are boxes, files I used . . .

NARRATION: The OCC's lack of action doesn't surprise Zina Green and two other former fair lending specialists. All three quit in frustration. Zina Green left in 1979.

ZINA GREENE: I knew this was an organization that did not want to find discrimination. It was clear, it was eminently clear. I came there as a director of a division. Within a few months, it was rearranged, and I was just off there by myself, with a secretary. And I think that the people who followed me didn't even have a secretary. They were just director of civil rights, but director of nothing.

NARRATION: Michelle White took over the job when Zina Greene resigned. White stayed for 2 years.

WHITE: Under the Bush and Reagan administrations we've seen an erosion of civil rights in general. An there was never a commitment to civil rights from my perspective in the area of either lending or insurance.

NARRATION: Ron Weink was next. He says the lack of interest in fair lending was still the case when he resigned in 1990.

WEINK: I quit as a matter of principle. I though the interest, particularly by senior management in fair lending, had declined over the eight years I was at the comptrollers office.

SCHECHNER: So you had had it?

WEINK: I had had it.

NARRATION: The head of the OCC at the time Weink resigned was Robert Clarke.

SCHECHNER: You think you did a good job?

CLARKE: I believe so.

SCHECHNER: What would you say to people who say: "No, you didn't, sir?"

CLARKE: I think they simply don't understand the facts. . . . I understand why people feel the way they do. I just don't think they have a very good appreciation for what goes on in a bank supervisory agency. And I think they rely too much on statistics without look at the, at what underlies those statistics.

KRAUSE: It makes you wonder if over the years this agency has really been interested in enforcing those laws, in getting at discrimination. Has it been? How could it be that those three people quit?

KRAUSE: Well, I don't know all those people. I wasn't involved in this particular area for as far back as they go. I think this agency has always been interested in fair lending enforcement. Uh, I think it's a very difficult area to try to establish a definitive record in, and we have the same record as the other federal agencies in terms of how successful we've been at finding and proving unlawful discrimination.

SCHECHNER: Who's responsible for this situation taking so long to root out?

LAWARE: I don't know. I refuse to accept responsibility on the behalf of the regulators. Because we conduct what we feel are responsible level of examination procedures to observe compliance. And where we find any indications in the record of discrimination we take whatever steps are necessary to correct it.

PROXMIRE: Regulators are doing a lousy job from any standpoint. A lousy job. Very poor. We have gross, demonstrable discrimination. Racial discrimination, gender discrimination, discrimination against people with low incomes.

MFUME: If you understand this, you got to do something about it, cause it will eat at you. But if you say I don't understand it and maybe we should wait and study the data, and we should not draw subjective conclusions, it puts off the inevitable decision to act.

NARRATION: FRONTLINE requested interviews with the cabinet level officers responsible for bank regulation and fair housing laws. Both Nicholas Brady, Secretary of the Treasury, and Jack Kemp, Secretary of Housing and Urban Development, declined our requests.

SOT AT HEARINGS: These hearings could not be more timely.

NARRATION: One week after Los Angeles exploded, community groups were again on Capitol Hill. The urgency may have been new. The message remains familiar.

GILDA HAAS: The recent Rodney King decision just lit the anger and frustration and despair that was rooted in a long experience of economic injustice.

DONALD MARTIN: There are many laws already on the books to see that these problems don't come about but we seem to come back here year after year, basically report the same numbers and we'll come back again next year and do this same thing again.

CINCOTTA: I hear this debate after twenty years that these banks might be good folks and there isn't any discrimination it's like mind-blowing. I don't know when we're going to get on with the business of getting loans out to these communities. How many more Los Angeles have to blow up?

SOT ACORN PROTEST: ACORN, the peoples voice will rise again . . .

NARRATION: Back in Chicago, ACORN, the neighborhood advocacy group, continues its fight against Affiliated Bank.

SOT WOMAN: We're working people and we deserve a fair share of whatever is going on. We need loans and we don't have to be redlined. We're not going to stand for it. We will be back.

NARRATION: For four months, they've kept up pressure on the regulators and the bank.

Finally, last month the bank and ACORN reached an agreement. Affiliated agreed to grant more mortgages in all of Chicago's low-income neighborhoods and gave ACORN a $25,000 grant. The Fed approved the bank's merger.

SOT WOMAN: Redlining—we're tired of it!

SOT: Rap music.

NARRATION: But ACORN has won a small battle. Chicago's black neighborhoods are still far from receiving their fair share of financial services. We looked at what happens to the neighborhoods when banks are scarce. Without banks, all kinds of opportunists are free to operate here.

It's another side of the redlining story. We looked at one of the most common ripoffs, home improvement contractors offering questionable financing for shoddy work.

LUELLAN: We cannot borrow money from the bank—but then the banks will turn around and let these shyster contractors have it and sell it to us for three times, or four times, or five times the money and they make a fortune of off us.

WANDA GRIGSBY: We were told how much the monthly payments would be and how long it would take to pay the loan off, but we weren't told that the interest rate would be 17.98.

NARRATION: Wanda Grigsby lives with her husband and children on Chicago's Southside. In 1989, she decided to refinish her basement.

GRIGSBY: When there's a heavy rain we get maybe an inch or two of water in the basement, and we were told that that was no problem, they could dig a trench on the side of the house, on the north side of the house and fill in the cracks.

NARRATION: But two years after the work was done, after repeated requests for repairs to be made, the basement still floods after a hard rain.

SOT DOUG ROBINSON: OK, I would like to show you this awning, this awning right here . . .

SCHECHNER: Yeah.

SOT ROBINSON: I had to have this replaced because the awning it fell down. So I had someone come out to put it back up.

SCHECHNER: Uh-huh.

NARRATION: Doug Robinson says he too was cheated. He wanted new awnings and storm windows.

SOT ROBINSON: This particular window here, this was hung upside down. This window here, see that right there? This came apart.

ANNIE TRICE: It was a bad storm and our back porch of this old building where we live in, it blew down.

NARRATION: And, finally, Annie Trice. She co-signed a loan for her mother so that their badly damaged porch could be rebuilt.

TRICE: It was in such bad shape, I had to, we had to try to find someone right away to repair it.

NARRATION: She too received substandard work and says the porch is usable for only half the year.

TRICE: You can sit on the outside and the window get real cold when it rain, it rains on the inside.

NARRATION: Contracts resulting in shoddy work are all too common in these neighborhoods. But, what makes these cases especially troubling is that they all claim they were misled. Grigsby says she wasn't informed about the 18 percent interest rate. Trice and Robinson say they didn't know they were putting their homes on the line.

SCHECHNER: What did you think when you signed it?

ROBINSON: Well, I felt that they would finance the work and I would pay them. I didn't know that they was going to take out a second mortgage.

SCHECHNER: When did you sign the second mortgage?

ROBINSON: I never, the only thing I signed was the contract.

NARRATION: The company behind the contractors was an outfit called the Dartmouth Plan.

It's bankrupt now, but it once operated in 32 States. In Illinois, New York and Connecticut, Dartmouth has been sued for misleading homeowners and fraudulently securing second mortgages.

In 1985, Connecticut was the first to sue. Richard Blumenthal is the State's Attorney General.

BLUMENTHAL: The real deception in the Dartmouth Plan was that second mortgages were placed on peoples homes without their knowing about it. And in some instances documents actually forged, their signatures actually written-in by someone else, notarized in their absence and obviously misrepresented.

NARRATION: In New York State, a similar suit is underway. Elizabeth Bradford, the Assistant Attorney General trying the case, explains how the Dartmouth contractors operated.

BRADFORD: When the contractor comes to the consumer's house, he gets the consumer to agree to a contract. He takes credit information from the customer at the point, and asks him to sign a stack of documents on a clipboard, whole stack of things, including the loan agreement, and the mortgage agreement which is buried under this pile of documents.

PEIREZ: It's not just that we deny the charges, which we do, but the charges really deal, to the extent that there's any validity, to a small, small handful of dishonest contractors.

NARRATION: Dartmouth's attorney is David Peirez.

PEIREZ: We monitored what was going on. We refused to do business with contractors that we thought were dishonest. Whenever a homeowner complained, we sent people out to their homes. Did we make mistakes? Sure, we're human, but very, very few. Nothing that approaches fraudulent conduct.

BRADFORD: I think that the judge, hearing these people get on the stand time and again, essentially telling the same story about how they were not aware of mortgages. They had no idea they were paying that interest rate. They didn't even realize how long they were supposed to pay on the loan, will realize that this is not just a series of isolated problems, but an underlying problem with the way this company did business.

NARRATION: According to the lawsuit filed in Illinois, Dartmouth enticed contractors with expensive vacations to hook homeowners into higher interest rates.

These profitable, high-interest mortgages could then be sold to mainstream banks—the same banks often unwilling to make home improvement loans at conventional rates in minority neighborhoods. One of Dartmouth's biggest customers was Citibank.

PEIREZ: At the time, when Dartmouth purchased the paper, it would turn around and sell to Citibank, or other banks, and they would be the investor, the one that held this paper in order to make money. And Dartmouth would do that over and over again with many thousands of homeowners. To Citibank and other banks.

NARRATION: In New York and Connecticut, Citibank was named along with other banks as a co-defendant with Dartmouth. In Connecticut, Dartmouth settled their case paying $3.5 million to 3,100 homeowners. The case against the banks was dismissed. In New York, the case against Dartmouth is still pending. Citibank has settled with a payment of $250,000 to consumers.

Citibank of Chicago canceled a scheduled interview when we told them we would ask questions about the Dartmouth Plan. In a letter to FRONTLINE the bank wrote that, in addition to their initial background check on Dartmouth in 1978, they did a second check: "After the [Connecticut] Attorney General brought suit" and ". . . found nothing that indicated any impropriety. . . ."

THE LETTER ADDS: "Citibank was not involved in the origination of the consumer paper and did not know what specific practices the contractors used." So, the letter says, Citibank stopped buying Dartmouth's loans in Connecticut. Citibank continued to do business with Dartmouth in Illinois until 1989.

BLUMENTHAL: In our complaint, we alleged that they knew or should have known that Dartmouth was not a licensed mortgage broker and that many of those mortgages were illegally procured because of the extent of complaints that followed.

PEIREZ: Citibank knew about the complaints that were made to Dartmouth. Citibank was regularly informed by Dartmouth. Citibank as I have mentioned, was not only a lending bank, a buying bank and a financial advisor. And as a result we were always giving them information—good information or bad information; financial information or any types of accusations that might affect our business. They were fully informed and, and nothing that was aimed at Dartmouth was withheld from Citibank and they know that.

NARRATION: Meanwhile, homeowners continue to pay off second mortgages on homes, homes still in need of repair.

SCHECHNER: Who are you paying?

ROBINSON: I'm paying Citibank in Hicksville, New York.

SCHECHNER: Why don't you just stop?

ROBINSON: I'd lose my home, I can't. If I stopped paying 'em now, I have a second mortgage, which means if I stop paying they can take my home.

SCHECHNER: Has this been hard on you?

TRICE: It put me far behind. And I was, when I first became a case worker, I was thinking about getting me a car. I couldn't get it. I couldn't get anything.

BLUMENTHAL: There are human beings behind these pieces of paper. When those human beings file complaints with banks, our hope is that banks will be more careful and energetic in trying to follow those complaints and stop doing business with people responsible for them.

JIM FLETCHER: There are still neighborhoods in this city in which the market economy doesn't work properly.

NARRATION: Jim Fletcher is president of Southshore Bank, one of the few pioneers of community development on Chicago's south and west sides.

FLETCHER: And part of the reason it does not work properly is that institutions that are active and can extend credit in those neighborhoods don't do it. They extend it to other places.

SCHECHNER: And why don't they do it in those neighborhoods?

FLETCHER: As I said before, because their perception of that neighborhood is that the risk is too great.

SCHECHNER: And why would they perceive the risk as being too great in that neighborhood? Is it race? Is it economics? What is it?

FLETCHER: It's race, OK. And, and, and that gets tied to economics. And it's a perception that those people that aren't like me won't handle themselves properly.

NARRATION: Other bankers see the issue somewhat differently.

THOMAS: What we need to do is to have people become qualified to borrow money from a bank or from any other lender. But I think access to credit is somewhere down the line. We need to do all we can to stimulate job creation, good education, good credit record, frankly those are the kind of things that are much more important than access to credit. Access to credit comes as a result of other things.

FLETCHER: Bankers manage risk. And they perceive that this is not the way to manage risk and to make maximum return on invested capital. And since they don't believe it, I don't know. And it is hard to convince them so they don't. This is not a business they want to be in.

SOT: Fire-engine siren.

MFUME: We didn't listen in Los Angeles and we are not listening in other urban areas and we are not listening as it relates to the lending practices which I believe in many respects are discriminatory by, by some banks in this country. And I think that the same kind of hostility is growing and it is building up against the nation's financial institutions.

NARRATION: In the wake of the L.A. riots, bankers and regulators nationwide have pledged to do more to ensure fair lending.

The Justice Department has told regulators they want fair lending cases Justice can prosecute. The Department of Housing and Urban Development says it will begin funding the testing of mortgage lenders for discrimination.

NARRATION: In Chicago, Donald Davidson and Maria Saldana continue to rehab their home. It has helped their block, but they are still angry.

DAVIDSON: I know how the game is played and I know how you can hide any reason any way you don't want to make a loan. I'm a real estate developer by trade. I'm a mortgage banker by trade. My wife is a lawyer. You can kid a lot of people, but you can't kid us.

NARRATION: They are now considering a lawsuit against Citibank for discriminatory lending practices.

SALDANA: I feel like I should do it, because who, how are you going to get change if somebody like myself who should know—who knows that something went on that shouldn't have gone on, doesn't get to the bottom of it?

NARRATION: Back in Inglewood, Henry Luellan is determined to see change.

LUELLAN: I'm not gonna to leave this neighborhood until I dies. I'm going to stay in this neighborhood. No matter what happens. I'm going to fight, I'm going to meet, I'm going to talk to peoples. Sooner or later, I will win.

NARRATION: And the Greens? They finally got a mortgage and bought their apartment building. They are suing Avenue Bank.

PETER GREEN: It just should not have happened, I'm sorry. That's all there is to it. Um, it's the law of the land. Born here, educated here, pay my taxes here, I'm entitled to a fair shake. Nothing special, fair shake, under the law.

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October 5, 1992

Senator Alan Cranston
United States Senate
Committee on Banking, Housing, and Urban Affairs
Housing Subcommittee
Dirksen Senate Office Building, Room 535
Washington, DC 20510

Dear Senator Cranston:

We would appreciate the opportunity to clarify for the record certain aspects of a report that was cited by Calvin Bradford in written testimony he submitted recently to your subcommittee. The report in question, "The Unknown Lenders: The Role of Mortgage Banks in the Chicago Metropolitan Area," was written by Dr. Constance R. Dunham of The Urban Institute and was commissioned and published by the Woodstock Institute in 1991.

1. The Testimony states that the Report found no differences in the levels of mortgage bank lending to minority and white communities.

The Report compared predominantly black and white neighborhoods in two ways. First, the Report found that the rate of mortgage bank lending was quite different in black and white neighborhoods, and clearly illustrated this simple comparison (Table 3.9, p. 52).

Second, a major finding of the Report was the absence of significant disparities in mortgage bank lending rates among comparable black and white neighborhoods -- that is, after controlling for housing, demographic, and economic characteristics of census tracts that likely affect mortgage bank lending rates. The distinction between simple comparisons and comparisons that statistically control for other neighborhood characteristics is important and the Report explained the distinction at length (pp. 37, 43, 46,48, 52-4, 65-6, 71, and 89).

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2. The Testimony argues that the Report ignored its own findings that FHA/VA and conventional loans tend to be made in different types of communities.

This allegation is not correct. One of the major findings in the Report, which it discussed in some detail, is that mortgage banks make FHA and VA mortgage loans in neighborhoods that tend to be quite different (e.g., in terms of racial change, income, and racial composition) than those in which they make conventional mortgage loans (pp. 66-70). The Report noted that "FHA/VA and conventional mortgage lending patterns are strikingly different from each other" and that each "has a strong presence in distinctly different segments" of the metropolitan Chicago mortgage lending market (p.66). Furthermore, the Report compared FHA/VA and conventional lending patterns of mortgage banks with those of depository institutions (pp. 81-84). Together, these findings served as the basis for two of the six major recommendations of the Report (pp. 91-2).

The type of statistical analysis used in this Report cannot identify which of several plausible reasons explain the differences in FHA/VA and conventional mortgage lending patterns noted above. The Report pointed out that these distinct lending patterns partly result from differences in the relative appeal each loan type holds for various types of households (pp. 26-9), an important point to consider when grappling with the puzzle of why depository institutions so rarely provide FHA/VA mortgage loans. The Report also cited a recent audit (testing) study of potential homebuyers, as well as interviews with Chicago realtors and statistical studies, all of which support the view that "it is unlikely that borrower preferences alone explain FHA/VA and conventional mortgage usage" (p. 29). The Report noted that the differences could result from realtor or mortgage bank targeting of each of these types of mortgage loans to different parts of the market (p. 70). The Report recommended as a next step specific studies to generate the kind of information that would help resolve the question (pp. 91-2).

3. The Testimony states that the Report found that mortgage banks' use of FHA/VA loans represents a pattern of fair lending.

Nowhere in the Report are mortgage bank lending patterns characterized as "fair." Rather, the Report identified when there are (and are not) significant disparities in mortgage bank lending rates by type of neighborhood, and contrasted these with the mortgage lending patterns of depository institutions (pp. ii, 62-71, 75-84, 87-90).

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The Report found that there were large disparities in depository institutions' mortgage lending rates between comparable black and white neighborhoods, but no significant disparities in mortgage banks' lending rates between comparable black and white neighborhoods. However, the Report did not analyze the reasons for those disparities. Therefore, we cannot conclude from this analysis either that these patterns were caused by mortgage discrimination by depositories or that there was an absence of lender discrimination by mortgage banks. Of relevance to both mortgage banks and depositories is the Report's findings that aggregate mortgage lending rates (of all Chicago-area lenders) were significantly higher in white than in comparable black neighborhoods.

The Report provides policymakers and the public with a great deal of new information on the operation of Chicago-area mortgage banks and their residential mortgage lending patterns. However, it is clear that other studies must be conducted before a clear picture emerges as to the extent to which Chicago-area mortgage lending patterns result from lender discrimination, from other kinds of lender behavior, from borrower behavior, and/or from the actions of other institutions. The Urban Institute, Woodstock Institute, and many other researchers around the country are now engaged in this next round of research.

Thank you for the opportunity to clarify for the record the purpose and findings of this Report.

Sincerely,

Malcolm Bush
President
Woodstock Institute

Constance R. Dunham
Author of the Report
The Urban Institute

TESTIMONY SUBMITTED TO THE SENATE BANKING COMMITTEE, SUBCOMMITTEE ON HOUSING SEPTEMBER 15, 1992

Kathryn Tholin, Acting President
Woodstock Institute

Thank you for inviting Woodstock Institute to submit testimony to the committee on the implementation of the Community Reinvestment Act.

The Woodstock Institute is a nonprofit organization which is based in Chicago and works nationally to bridge the gap between the needs of distressed urban and rural communities and the resources of financial institutions. During the last fifteen years, the Institute has conducted extensive studies of housing credit flows and has documented continuing patterns of disinvestment in poor, working class, and minority communities; it has monitored the community reinvestment performance of financial institutions; it has worked with state and local government and community development financial institutions to develop and implement innovative financing programs; and it has provided technical assistance to community-based organizations in assessing their community credit needs and in designing and implementing financial programs for affordable housing and job creation.

Since passage of the Community Reinvestment Act, the Institute has used the CRA as a tool for encouraging financial institutions to increase their investment in low income and minority communities. The CRA has been and continues to be highly useful to community-based organizations in establishing partnerships with local financial institutions. The CRA has opened up new opportunities to many financial institutions, who have learned through such partnerships that serving underserved markets can make good business sense. Particularly since the public disclosure of examinations, CRA has also provided important information and direction to large and small institutions, as well as individuals, who wish to direct their deposits into institutions which are serious and effective in their reinvestment efforts.

In response to the request of the Senate Banking Committee for testimony addressing the effectiveness and impact of the Community Reinvestment Act, we would like to focus on two primary issues:

1. The continuing need for the Community Reinvestment Act

The Community Reinvestment Act has accomplished a great deal since its inception. That impact goes beyond the $30 billion in targeted lending commitments made in response to community action, and substantial amount of additional lending to low-income and minority communities made unilaterally by banks. The result of these commitments and other compliance efforts is that more and more banks are actively looking for and finding lending opportunities in communities they previously ignored. These efforts have a long term effect on the marketing and lending activities of these institutions. Without the CRA, however, these institutions would not be as likely to seek out such market opportunities.

The presence of the CRA in its current form, applying to all banks and savings and loans, is necessary to ensure that these institutions address the credit needs of low income communities. While these credit needs can be sound lending opportunities, they often require special guidelines and program elements that an institution might not explore and implement without the incentive of CRA.

The Institute strongly opposes any attempt to limit enforcement of the Community Reinvestment Act, through small bank exemptions, safe harbor provisions, or other means.

One of the primary arguments given by opponents of CRA is that many banks should be exempted from its provisions because of the high cost and effort of the paperwork required. We believe that this is a false issue, and certainly does not provide a justification to abandon the overall requirements of the CRA.

We believe that some of the difficulty over documentation of CRA efforts is due to banks' uncertainties about what information regulators are looking for. Much of it is due to the emphasis of bank consultants and vendors on the production of paperwork to document CRA efforts. As a result of these, banks may be defensively compiling more paper than necessary. In addition, some of the problem is due to an overemphasis by some examiners on pieces of paper rather than concrete results.

Resolving these issues does not require changing or limiting the Community Reinvestment Act. The appropriate emphasis of all of those involved in CRA implementation and enforcement should be concrete actions and results. Documentation should be a natural part of all of an institution's marketing and development efforts, and is important to help ensure the success of those efforts. On the other hand, a bank that places primary emphasis on generating an extensive paper trail is utilizing time that could be spend developing new outreach and lending programs. Any bank that is taking CRA seriously should not find it difficult to document their research, initiatives, and results.

Some bankers are contending that rural community banks be exempted from compliance with CRA because those banks by nature must serve the needs of their communities. Our experience is, however, that no bank, urban or rural, inherently serves the credit needs of its community. Many banks, in fact, choose not to lend money at all, focusing instead on purchasing Treasury bills and other government securities. Today, for the first time since 1951, banks have more government paper in their vaults than they do commercial and industrial loans (Martin Mayer, Wall St. Journal, September, 1992).

Small banks, in fact, have received the bulk of the "Needs Improvement" and "Substantial Noncompliance" ratings. According to the Center for Community Change, between July 1, 1990 and December 31, 1991, more than half of the banks receiving these ratings had assets under $250 million, and of those, 83 percent went to banks under $100 million in assets.

Implementation of the Community Reinvestment Act requires a deliberate effort by any bank, urban or rural; any bank should be able to document those efforts and results.

2. Using CRA more effectively to promote community development

Community Development Financial Institutions

The Institute seeks programs and mechanisms to address a wide range of community credit needs. One of the things we have learned is that, despite successful CRA agreements and programs, disinvested communities have credit needs that will not be fully met by a traditional financial institution. Many of these have developed through long-term disinvestment and its impact on a community's resulting inability to function in the market economy.

In many parts of the country, other lending institutions are seeking to address those deeper credit needs. Community development credit unions are making small loans to low income individuals for such purposes as buying a used car to travel to work, education and training, or home improvement. Equally important, they are offering low cost financial services to low income persons and providing the extensive consumer education necessary to bring people from the cash economy into mainstream financial services. Community development loan funds are providing low cost, higher risk loans to needed community development projects which will bring housing, jobs, and increased economic activity to a community. Microcredit programs, through both intensive training and financing, seek to bring individuals from dependency to self-sufficiency through self-employment and very small business initiatives.

It is our view that addressing the credit needs of disadvantaged communities is a long term as well as a short term project. In this context, it is appropriate that financial institutions be encouraged to develop programs and take actions which can increase a community's capacity for credit over the long run. The New York Federal Reserve has taken that approach in determining that investment in and assistance to supportive services such as day care is an appropriate CRA activity.

Support of community development financial institutions should not substitute for efforts of financial institutions to lend directly in lower income communities. We have found, however, that financial institutions can provide valuable assistance--in the form of grants, low interest loans, and technical assistance--to such financial intermediaries. These partnerships can expand the reach of financial institutions in meeting the least bankable credit needs and should be encouraged.

Expanded HMDA reporting

Woodstock Institute has long supported the expansion of HMDA reporting to include small business lending disclosure. Business lending, and the resulting job creation and retention, is clearly critical to a community's financial viability. Many CRA agreements and programs include small business lending as an important component. For many financial institutions, business lending is their primary activity. But today, there is no public information on the business lending patterns of financial institutions.

A local ordinance in Chicago requires all banks requesting city deposits to provide annual information on their commercial lending. A two-year analysis of that data showed that only 10 percent of commercial loan dollars reported were lent in Chicago's neighborhoods, with 90 percent lent downtown or in the suburbs. Expanded HMDA reporting which included the size, location, and type of commercial loans would provide valuable information to assess commercial reinvestment.

Penalties for Noncompliance

Despite the substantial successes of the CRA, large numbers of institutions have not responded in a meaningful way to its requirements, and have made no efforts to address the credit needs of low income communities. In the absence of a pending merger or acquisition, the poor public relations of a failing rating is the only effect on the institution. While public disclosure of ratings has led institutions to pay more attention to their ratings, this is not enough. Additional appropriate penalties for a finding, or a sustained finding, of "Substantial Noncompliance" should be considered. The new practice of the Federal Home Loan Bank of reviewing community records of its member institutions as a factor in approving access to its financial programs for members is an important action in this direction.

Thank you again for the opportunity to submit testimony to the committee. We would be happy to work with you further in the development of policies and programs that can meet the credit needs of low and moderate income communities and households.

Woodstock Institute, 407 S. Dearborn, Chicago, IL 60605, (312) 427-8070

September 25, 1992

To: Ryan Conroy
United States Senate
Committee on Banking, Housing and Urban Affairs
Housing Subcommittee
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From: Charles B. Finn
Director, Banking and Community Economic Development Program
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Re: Comments to be added to hearing testimony

As per our phone conversation, I am sending comments of six issues I view as directly effecting the ability of the regulators, researchers and the public to assess the performance of financial institutions. While the 1990 HMDA data is a great step forward, it only partially addresses the need for comprehensive, reliable and timely information about this critical sector of our economy and its huge potential to contribute towards the failure or success of urban, rural, minority and low income communities in this country.

I will address six areas of concern I have, based upon my research regarding communities, lenders, lending data quality and access. I do want to be clear from the onset of my comments regarding the intent of my testimony: Namely, at this time, we do not have adequate data to assess the performance of the financial sector in rural, urban, minority and low income communities. Frankly it is premature to say the least, for a debate about whether certain institutions of a certain size, or certain communities should be exempted from dissemination of data when we cannot make reliable assessments based on the quality and availability of current data. It is ironic that the same groups that are currently raising the issue of limiting access are the same organizations that have made it so difficult to obtain what data is actually needed.
The larger issue that needs to be addressed is how does the very spirit of economic capitalism regarding equality of opportunity and access survive when the public and government lack the vital information necessary to make informed decisions about markets and regulation.

I. Native American Communities
The 1990 data sets allowed the first access to information

regarding financial institutions activity within these communities. While there are real questions regarding the comprehensiveness of this data in terms of reporting by other federal agencies, it is clear that what data we do have indicates this group has real problems accessing capital.

There were about 19,000 loan applications that identified the primary applicant as native american. This is a very large number when one observes there are a little over 2 million native americans in the whole country. Of those applications, almost 7,600 (40%) have no location variable assigned to them. This means we cannot tell which city, MSA, county or state these applications came from, which makes assessment of any community extremely difficult. Another example of problems of this sort is that the MSA of Minneapolis-St. Paul has only one application listed with native american as primary applicant. This is very curious when the size of the native american community is taken into account and one considers that Minnesota has one of the largest native american populations of any state.
Another problem is the number of application denials, which are not quite as bad as comparable cohorts of black applicants, but far worse than comparable whites. This is especially puzzling when one takes into account the plethora of BIA loan guarantee programs that remove a great deal of the risk and also gives interest rate incentives to this group of applicants.

II. Rural Lending
There is very little information available regarding lending performance in rural communities due the HMDA loophole that does not require reporting of lending in small communities. However, we do know that people in these areas are much more vulnerable to discriminatory lending practices and also lack the ability to do anything about the problem. People are more vulnerable due to the fact there is no reporting of the data for oversight and it is well documented that applicants that are turned down are reluctant to protest or even discuss the problem. In other words, there is no "sunshine" in these communities regarding lenders activities. The other, and even more compelling reason for careful oversight in these areas is that often times, there is only one financial institution available. Consumers who are denied access to the "only bank in town" are simply out of luck, where even in small cities, borrowers at have the opportunity to shop around. Consumers that do travel to another community find bankers in that community uninformed about their area and therefore, not equipped to handle their business.

I had a brief opportunity to use data from FDIC tapes that identified rural bank activity by loan category (ie agricultural, home lending, small business, etc.). When I compared data from this tape to county bossiness data garnered from other sources, I found some large discrepancies regarding portfolio performance of some local lenders and the economies they served. One would posit that an institution's lending performance over time should mirror economic activity to a certain extent within the community it serves. While I can draw no conclusions from this observation due to lack of breadth of the work and comprehensiveness, I will comment that my observations argue for more investigation and better data in this area at the very least.

III. Small business lending- no data
It is well documented that small bossiness lending is critical to the economy of any area. In fact this sector is often called the "engine of vitality and change" as it generates most of the new jobs in the country. Yet there is no HMDA for small business. If small businesses cannot get a loan in a particular community due to discriminatory activity by lenders, how could we expect people within that community to have the ability or need to access financial markets for consumer and home loans? An observation made by several institutions when asked to comment in front of this Committee over the years (I would site my research in Atlanta and Detroit), has been that they do not get any applications from the areas they have been accused of discrimination in. Certainly a large part of this observed result is from attitudes, behaviors and actions of those institutions within their communities. But what part is due to the fact that institutions that not only do not offer home loans in certain communities, also do not offer small business loans that actually generate the incomes that allow citizens to thrive and apply for home loans?

One phenomenon that has been observed over the last few years regarding agglomeration in the financial industry is the new attitude these large institutions take toward financial "lines of credit." These large institutions survive and flourish based upon their ability to balance the additional debt loading incurred for purchasing institutions with increased segmented market opportunity and application of cost savings through "economies of scale" management processes and technologies. These "special lines of credit", which are critical to small business and communities are very difficult for large institutions to handle. They require a much higher level of knowledge about the lender, the market and the community than a business whose profit rationale requires wholesale practice of "economies of scale" can handle. Therefore, many large institutions have been terminating these loan types, which sounds the "death knell" for small business in many communities.

There is no data available regarding small business lending that would allow us to determine the behavior and impacts of this critical lending market in our communities.

IV. Small Bossiness Administration data
[illegible] ata used to be available and I was able to access the data [illegible] 1989 for the country. This no longer appears to be the case.

While this data set does not represent anything other than the activity of landers in this specific category, it is important that we know which institutions are using these public subsidized lending opportunities and who they are lending to.

V. Too big to regulate
With the demise of local communities and states acting as the boundaries of financial institution activity in the country, we now have institutions that are active across whole regions and indeed, the country. One bank in Texas has storefronts in over 100 communities. A recent agglomeration in the Southeast involved activities that not only comprised all of the banking activity in many communities, but actually set up an institution that controlled a large fraction of banking activity in the whole region! When these institutions get into financial trouble, it is well understood by most people who study bank failures, that they cannot be allowed to actually close down because the impact of such an action is so large as to actually destroy whole economies of areas. The same rationale applies to CRA examinations. Institutions of this size, as a matter of policy cannot be evaluated in terms of their performance in communities. One only has to peruse decisions in the Federal Reserve Bulletin regarding Board of Governors decisions regarding CRA challenges to institutions of this type. These challenges are dismissed because while these banks may be operating poorly in one area, they are doing well overall. This successful argument is well founded in that regulation must look at the institution as a whole as any punishment will affect the institution in that manner. Therefore, it is difficult to impossible for regulators to address problems of this scope in the traditional manner as detailed in the act and regulations.
New proscriptions to address institutions of this size must be developed not only in the area of safety and soundness, but in Community Reinvestment as well. It is altogether possible, if the banking lobby is successful in their attempt to exempt small and rural institutions and large banks cannot be approached due the to big to regulate phenomenon, that the spirit and intent of Congress regarding CRA will be not partially, but completely negated.

VI. North American Free Trade Agreement.
Any comments regarding Community Reinvestment must also address the impact of NAFTA on financial institutions and insurance in communities, regions and states. The financial section of this agreement, which legally, is beyond state, federal and even Constitutional law, in essence allow "carte blanc" access to all communities within the United States. These private sector institutions will operate without any guarantees of safety, soundness, security or be required to follow local, state or federal laws and regulations in these areas. It would be hard to overestimate the eventual impact of this treaty as it creates a "superclass" of investors that will not have to compete on the

same level playing field as local institutions. While the immediate impact of these changes is mitigated by the restrictions placed within the treaty in terms of percent of foreign ownership (to protect Mexican business), the abrogation of all local, state and federal regulations in these areas has to lead to the eventual complete de-regulation of these industries. At the very least, this Treaty will eliminate all sub-federal regulation of these industries and in the case of insurance industries, this is all regulation. The old proverb about the "camel's nose in the tent" again demonstratee as how old strategies can still be successful. And this part of NAFTA certainly is a demonstration of this truism.

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TESTIMONY OF

REBECCA ADAMSON,

PRESIDENT

FIRST NATIONS DEVELOPMENT INSTITUTE
FALMOUTH, VIRGINIA

SEPTEMBER 17, 1992

Mr. Chairman and members of the Senate Banking Committee:

I wish to thank you for this opportunity to address the critical need of Indian Communities to have access to responsible financial banking facilities, which are sensitive to the culture of the individual Indians and tribes.

First Nations Development Institute is oldest and largest American Indian reservation based economic development organization in the country. We began our work in 1980, with a strict mandate to work with tribes and individual Indians to help them become less dependent upon the federal government and to become more self-sufficient. This is accomplished through educational efforts and the provision of technical assistance to help Indian communities develop economic programs that are culturally appropriate. Our work over the past 12 years has shown us that there are no easy answers to our economic problems. Development is a lengthy process of both recognizing and building upon leadership skills of individual Indians and tribal organizations. Part of what we do is work with a community or tribal council to learn about that economy- what community members are doing, what their interests are, and how their future goals might fit into the bigger economic and community picture. One of the obvious pieces of our work is to study reservation economies, the spending and investment practices of the reservations, and generally to follow the flow of money in and out of the community. Working with bankers, responsible investors, and foundations, First Nations has constructed several pipelines for injecting capital into the reservations. Through our Oweesta (Mohawk word for money) Program, First Nations places capital on the reservations and builds Indian people's financial capabilities and skills. First Nations' has received loans and seed capital grants of $1.8 million. That capital supplies matching loans to micro-enterprise loans funds, supports deposits in reservation-based credit unions and banks, provides partnership deposits in other financial institutions, and guarantees loans for field projects. Tribes select which commercial banks should receive the partnership deposits in recognition of their innovative lending in Indian Country. In addition, First Nations' has convinced other investors to deposit over three-quarters of a million dollars in Indian-owned institutions, thus helping capitalize Indian economic development while keeping their money safe and earning the fiar market-rate return. Thus, our work and interest in the Community Reinvestment Act, is obvious.

I will start off by sharing with you a few examples of banking experiences of tribes. Not long ago, a lawyer representing the Fort Peck Tribal Housing Authority withdrew the agency's several million-dollar deposit from their local bank and placed it in several banks in Denver, Colorado. This was done because the local bank had been holding the Housing Authority's funds in a noninterest-bearing account for years, a not so uncommon scenario in tribal banking relationships. This action got results. Local banks began treating the tribes in the area as preferred customers.

Another tribe recently received a large judgement award from their local government. In studying their relationship with their local bank, it was found that approximately $400,000 was deposited into the bank, by the tribe monthly to cover administrative salaries and obligations yet with that leverage, that bank made no substantial business or financing loans to members of their tribe. This with the CRA in place. A portion of this award was distributed in the form of per-capita payments to the tribal members. The award money was deposited into the same local banking institution who then distributed the checks to tribal members. Included in this distribution was a notice from the bank notifying members that to enhance services, they had extended their hours.

The chairman of the Salt River-Pima Maricopa Tribe had been turned down for business and personal loans several times by the local bank prior to becoming chairman. When he became chairman and realized that he had a responsibility to negotiate with this bank, he tried to put his personal experiences behind him. Upon entering the bank on tribal business, he could not see the bank president, until it was determined that he had sufficient financial leverage. After several months of negotiations, and educating the bank about his tribe, the bank has now guaranteed several loans and negotiated bonds for infrastructure projects on the reservation, and the tribe is now a preferred customer.

The Northern Cheyenne people have tackled a corporate Goliath. In efforts to prevent mining on the reservation, tribal treasuries were drained and the poverty level of the tribal members did not improve. In 1984, Native Action was formed to study economic alternatives to mining. By surveying the community, Native Action found that there was a tremendous interest to develop small businesses on the reservation, however, no one could find a bank willing to provide financing. A focus group was attended by more than 50 people attending in weather of 40 degrees below zero.

When the First Interstate banking system of Montana announced plans to merge with a Wyoming bank system, Native Action challenged the merger under the CRA. Only one day after receiving notice of the protest in January 1990, the bank board reduced its primary lending area from 30 miles to just 10 miles, thus excluding the entire reservation. The bank stonewalled even more successful reservation businessmen from access to financing, Tribal members found the local bank reluctant to finance young ranchers. But this is common to reservations across the nation, many who are 30 to 50 miles away from the nearest financial institution, to begin with.

Mr. Chairman, all too often banks soak up the savings from a reservation and pump it into the border town economies or out of the regional economy entirely. The effects on the reservation or regional economy are devastating. Without adequate banking relationships in terms of loans, interest and investments, money coming onto the reservation quickly drains away without contributing to the tribal economy. In exchange for tribal and individual Indian monies being deposited into their banks, tribes are only asking for competitive interest-bearing accounts, and loans to tribes and tribal members at competitive interest rates. These practices are readily available to you or I, but not to the Indian people living on reservations.

Without access to reliable, competent banking and financial services, Indians not only fall pray to con artists, loan sharks and hustlers, but get charged exorbitant interest rates in the process. Even the Bureau of Indian Affairs, the trustee of Indian lands and natural resources, has lost Indian Trust fund monies to bank hustlers and embezzlers.
There is the argument that banking regulation has caused the banking crisis because of required burdensome paper work. But current CRA regulations do not require banks to file any lengthly reports. Currently, they are required to file a CRA statement, a CRA notice and the CRA public file. In the statement, the bank needs to simply describe its lending area and the credit it offers. The notice merely requires the bank to display how community members can obtain a copy of their CRA statement and how to comment on the bank's performance. The CRA public file contains all comments received and the bank's responses. In many instances these rural banks produce far more paper work than is required by the law and the regulators. Further, a recent study indicated that smaller "community" banks are the worse offenders of the CRA. Between 1990 and 1992, 71 percent of the banks that received the lowest CRA ratings were smaller banks with assets of less than $100 million.

Mr. Chairman, economic development capital has always been derived on reservations by large infusions of federal money, small-scale financing is virtually non-existent. Reservations need the financial vehicles to form capital for the right purpose, at the right time and in the right amount.

First Nations will be requesting that the Senate Select Committee on Indian Affairs hold a hearing on focusing on Banking Services in Indian Country in the 103rd Congress.

In closing, while much of the banking concerns among Indian reservations are not being resolved, without the protections contained in the CRA, our communities will be left completely to the mercy of con artists, and fly-by-night financing operations, and without access to reliable financing services.

Mr. Chairman, again thank you for this opportunity.

The Community Reinvestment Act in Rural Arizona:

After Five Years, a Light at the End of the Tunnel

Submitted by:
Frank Ballesteros, Executive Director
PHDC/MICRO Program
802 E. 46th St., Tucson, AZ 85713 (602) 622-3553

Prepared by: James Farias, Resource Development Planner III
September, 1992

The Community Reinvestment Act in Rural Arizona:
After Five Years, a Light at the End of the Tunnel

In the spring of 1987, a Planner for Portable Practical Educational Preparation, Inc. (PPEP), a non-profit social service organization serving rural Arizona read an article about a somewhat obscure piece of legislation, the Community Reinvestment Act (CRA -- Title VIII of the Housing and Community Development Act of 1977)[1] which had been passed with little fanfare ten years earlier but which had recently been used by community groups to encourage banks to make credit available to previously red-lined areas.

This intrigued us since it had been our experience that the major banks of Arizona with offices in rural areas had not been making credit equally available throughout their lending territory. Anecdotal information from clients in rural areas suggested that deposits were being funneled from rural areas to invest in large-scale speculative developments in the major metropolitan areas of Phoenix and Tucson. Farmers, home-owners and small businessmen were complaining that they were not able to obtain credit in rural areas. With the national and state economic slump the rural areas had all but been written off.

PPEP contacted a non-profit advocacy organization in Chicago which was funded to provide technical assistance to community groups who wanted to find out more about how to use the Community Reinvestment Act (CRA.) They worked with us and explained what we would have to do to mount a CRA challenge. *(At the time we were unaware that no CRA challenge has thus far been effective against a major bank under CRA.)*

We decided to target Valley National Bank (VNB) because, at the time, it was the largest bank in Arizona with branches in most rural areas. On July 28, 1987, PPEP sent a letter of comment to William N. Wiles, Secretary of the Board of Governors of the Federal Reserve System, regarding the proposed acquisition of California Valley Bank by Valley National Bank Corporation. We challenged VNB's performance in its rural service areas and requested a public hearing to discuss the following issues and concerns:

1. VNB's emphasis on its metropolitan service areas at the expense of rural communities.

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[1] Public Law 95-128 (12 U.S.C. 290)

2. VNB's failure to ascertain the credit needs of low- and moderate-income residents of it rural service areas.

3. VNB's efforts to discourage inquiries about its CRA performance.

4. VNB's attempt to misinform the public about their rights under CRA.

5. VNB's reluctance to engage in meaningful dialogue regarding VNB's lending criteria, policies and procedures in its rural service areas.

PPEP asserted that, first of all, VNB's CRA policies dealt only in vague generalities and with activities in the two metropolitan areas. No CRA plan was in place which addressed the specific and differing needs of rural areas. On more than one occasion VNB had tried to discourage our pursuit of information regarding its CRA performance. Bank representatives, when informed that we intended to pursue a formal challenge and protest, responded with veiled threats, such as: "I really hope this does not backfire on you," and "I hope it doesn't hurt you in the long run."

Also, VNB had tried to mislead us about our rights. Although the official comment period was still open, VNB officials endeavored to convince us that the proposed acquisition was a *fait accompli*; we were told that the acquisition had "already been approved by the board." The "board" referred to, however, was the bank's Board of Directors, not the Federal Reserve Board!

As we developed data for a formal challenge, we found ourselves at a great disadvantage. The Home Mortgage Disclosure Act (HMDA) applied only to urban areas and only two of Arizona's fifteen (15) counties served by VNB -- Maricopa and Pima Counties -- were required to maintain HMDA data. There was no way for us to obtain loan data on the thirteen (13) rural counties and VNB steadfastly refused to provide us with such data for the rural areas. Thus handicapped, and without any cooperation from the bank, we had to make due with what data we could obtain.

We were able to use data from the 1980 U.S. Census and VNB's 1981-1986 HMDA reports for Pima and Maricopa Counties. In Maricopa County we had to compare three rural tracts and three urban tracts around Phoenix; in Pima County we compared a census tract in the rural community of Ajo with an urban tract in Tucson that had a similar housing and economic profile. In all comparisons, we were scrupulous to describe what housing, demographic and economic differences existed between the tracts being compared.

A disturbing pattern emerged. The rural tracts had a higher poverty rate and a higher number of Hispanics than comparable urban tracts, but similar median incomes and housing. Also there was a much greater competition from other banks for loans in the urban areas than in the rural areas (where VNB was often the only bank in town). Yet, the number and dollar amount of home purchase loans and home improvement loans given in urban tracts compared to those in rural tracts ranged from 2 to 1 to almost 100 to 1! The only major differences between the rural areas and urban areas were geography, race and economic status.

Along with the statistical data compiled from VNB's own HMDA reports, we collected a number of letters documenting VNB's redlining practices in rural areas. San Luis, Arizona, Mayor Tony Reyes and a number of members of the Comite de Bienestar, an organization of migrant farmworkers, were prepared to testify to their experiences with VNB, the town's only bank.

In 1981, the Comite de Bienestar purchased 100 acres of land from the State of Arizona for $672,00 with $110,000 of their own money down and the balance carried by the State. The land was to be used to develop low-income housing for farmworkers. It was not until 1984, after extensive negotiations with Valley National Bank, that the Comite was able to obtain a commercial line of credit for $420,000 to finish developing lots on 52 acres as Phase 1 of their housing development.

In order to obtain this commercial credit line at a variable interest rate of 2 points over prime (14.75% at the time), the Comite had to give the bank a First Deed of Trust for the entire 100 acres of land (valued by then at $850,000. In effect, the bank demanded collateral for twice the value of the loan. Individual lots were released one at a time when fully paid off ($6,100 each.) In October, 1985, with a balance of only $187,000 on the first loan, the Comite renegotiated, under similar terms, with the bank for a loan of $1,080,000 to develop the remaining 48 acres.

In June, 1987, with an outstanding balance of $548,947, the Comite renegotiated with the bank to complete the project. At the time the loan was made, the prime rate was 8.25% but Valley National Bank charged them an interest rate of 12.5% (4.25% over prime) for a three-year loan secured by the 216 lots of Phase II.

The Comite was concerned because VNB had made no effort to provide special credit programs to meet the unique needs and circumstances of the migrant farmworkers and other low-income residents of their community, nor had it made any effort to ascertain the true credit needs of the community.

Despite the Comite's admirable and ambitious grassroots housing development activities, for example, VNB, <u>the only bank in town</u>, did not even have a part-time mortgage officer at the branch and limits the branch manager's loan decisions to loans of less than $20,000. In order to obtain mortgage loans on the homes that they are building, resident of San Luis must travel to Yuma.

Further, the credit needs of this farmworker community of 3,000 were hugely impacted by the large number of people who, due to the lack of affordable housing in San Luis, live across the border in the Mexican city of San Luis Rio Colorado, a fast growing city with a population of more than 200,000, but who -- because of Mexico's skyrocketing inflation and usurious interest rates -- come across the border to deposit this money at the VNB in San Luis.

Although we were not able to obtain deposit figures for the San Luis branch, we have reason to believe that they are in the millions of dollars, far exceeding the apparent economic resources of the town. These monies are then funneled out of the community and into VNB's investments in other areas, usually highly speculative developments around Phoenix and Tucson.

Despite dozens of letters testifying to various horror stories of dealing with VNB in San Luis and other rural areas and the loan data which we were able to compile, the Board of Governors of the Federal Reserve Bank refused our request public hearing. That's when PPEP began a media campaign to draw attention to this issue.

In September, 1987, PPEP staged demonstrations at the Tucson downtown branch of Valley National Bank and VNB's headquarters in Phoenix to protest their "redlining" rural areas. Demonstrators, many of them farmworkers and rural residents bussed in from areas as far away as San Luis, carried placards and posters and handed out flyers describing their complaints with VNB's lending practices in rural areas and the bank's reluctance to comply with its mandate under the Community Reinvestment Act. They held a huge red ribbon to symbolize the bank's redlining practices and a number of them, dressed as mourners and carrying a coffin, claimed that VNB was killing rural areas.

The local television stations and newspaper in Phoenix and Tucson picked up the story and carried it. The Arizona Republic (Phoenix) published a story of how the bank was accused of snubbing rural areas and refused to meet with us. The Arizona Daily Star (Tucson) and Tucson Citizen (Tucson) also carried stories about our protest and challenge under the CRA, but in November, 1987, the Federal Reserve Board approved the bank's acquisition.

Through the media blitz we were able to obtain some concessions for the farmworkers in San Luis but little else was accomplished. For the next several years our efforts were mainly focussed at educating the banks through letters and at CRA conference sponsored by the Federal Reserve Bank of San Francisco and the Federal Home Loan Bank of San Francisco. We maintained communication with VNB and with the other major banks in Arizona and their CRA Officers.

PPEP was very active in testimony to the President's Council on Rural America and at the Bank of America/Security Pacific merger hearings. PPEP has also been negotiating with First Interstate Bank of Arizona. Recently we joined the National Community Reinvestment Council (NCRC) and continues to advocate for innovative ways that non-profits can help build partnerships with banks to meet their CRA mandate. At last our efforts have shown the first major progress.

Toward the end of 1991, PPEP presented concept papers to the three largest banks in Arizona -- Bank of America/Arizona, First Interstate Bank of Arizona and Valley National Bank -- setting forth outlines for a model program through which each bank, in partnership with our Micro Industry Credit Rural Organization (MICRO) award-winning microenterprise development program, could improve their performance under CRA and FIRREA[2] by operating a pilot program in a specified target area.

Although we are still negotiating with Bank of America and First Interstate Bank, we are happy to announce that we have just signed an agreement with Valley National Bank of Arizona to initiate an exciting and innovative partnership pilot program in Yuma County. Under the agreement MICRO will deposit $100,000 with VNB to guarantee a revolving loan fund for microenterprises in Yuma County. The program will use the bank's application packet and MICRO's underwriting criteria to provide loans of from $500 to $10,000 to small, family-owned businesses in Yuma County. The bank will process the applications but MICRO, as guarantor, will have final approval of the loan.

MICRO and Valley National Bank are joining hands in a program to provide credit to small, family-owned businesses that, if successful, could be replicated statewide and provide a solid national model. We hope that other banks will look at our pilot program, monitor its success and consider replicating similar bank/non-profit partnerships to provide economic development initiatives through assistance to microenterprises. For further information, contact: Frank Ballesteros, Executive Director/MICRO at (602) 622-3553, FAX: (602) 622-1480 or via HandsNet at HN1952.

[2] Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA)

THE NAVAJO NATION

P. O. DRAWER 308 • WINDOW ROCK, ARIZONA 86515 • (602) 871-6605

PETERSON ZAH
PRESIDENT

MARSHALL PLUMMER
VICE PRESIDENT

October 5, 1992

Honorable Alan Cranston, Chairman
SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
U.S. Senate
Washington, D.C. 20510

Dear Senator Cranston,

We are very honored to have the opportunity to comment on the proposed amendments to the Community Reinvestment Act of 1977 as outlined in Senate Bill 2967.

In view of the fact that the Navajo Nation is actively utilizing the CRA as a tool to improve our banking relationships, we view the proposed changes to the CRA with a great deal of skepticism. The proposed amendments will serve only to compound the present problems of disinvestment, the lack of depository facilities and the absence of other banking services on the Navajo Nation.

We respectfully request that you take into consideration our following comments and attachments.

Sincerely,

THE NAVAJO NATION

Peterson Zah, President

xc: Washington Office

GENERAL COMMENTS OF THE NAVAJO NATION TO THE SENATE SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS ON THE CREDIT AVAILABILITY AND REGULATORY RELIEF ACT

BACKGROUND

The Navajo Nation recently began utilizing the Community Reinvestment Act of 1977 as a tool to encourage the banking industry to become active participants in meeting the credit and depository needs of our communities. Our total population is estimated to be over 151,000 and has a median age of 22.3 years. The Navajo Nation, the largest Indian tribe in the United States, has a land base which extends into three states, they are New Mexico, Arizona, and Utah.

Although 100 per cent of the Navajo Nation is delineated by bankers as being within their service or trade area, only three banks operate branches within the reservation boundaries. Citibank operates two of these branches and the First National Bank of Farmington operates the third. Citibank's branches are both in Arizona, one in Tuba City, the other in Window Rock. First National Bank of Farmington's branch is in Shiprock, New Mexico. The only other financial institution located within the Navajo Nation is the First American Credit Union which is located in Window Rock, Arizona. However, as a credit union, it is not subject to the Community Reinvestment Act.

Surrounding the Navajo Nation are many border towns and cities in which numerous banks exists. In the City of Gallup, New Mexico, there are 4 banks and 2 savings and loan institutions to service a population of 18,000. And although these financial institutions indicate that the Navajo Nation is part of their delineated territory, little attention is paid to the needs of the Navajo Nation. Research indicates that many of these banks which should be servicing the Navajo people have yet to even complete a basic credit needs ascertainment study of our communities as required by the CRA.

This lack of concern by bank officials to service the Navajo Nation not only affects our residents but also the 1 million plus visitors of the Navajo Nation each year. Most of these visitors are tourists and are vital to our economy.

Business entrepreneurs, and the Navajo Nation Government are restrained from reaching their goals by the shortage of credit availability on the Navajo Nation, making it difficult to improve the quality of life throughout the Navajo Nation. Banks have effectively established the practice of redlining the Navajo Nation, which is as large as the state of West Virginia. As a result, inconvenience and frustration emerges frequently due to the denied opportunities of basic bank services. Some Navajo people have to travel at least 4 hours per day to and from the nearest bank. This hardship effects not only the individual but also the over six hundred businesses which exist on the reservation.

Despite the absence of a banking presence on the Navajo Nation and despite the lengthy trip to the banks and back, our communities continue to be the growth area for banks. Savings and checking deposits are on the rise, yet credit opportunities for Navajo communities are decreasing.

Personal income on the Navajo Nation indicate that out of a total of $949 million dollars in personal income, only $160 million is consumed within the reservation, the remaining $789 million dollars flow off into bordering town businesses and eventually into the surrounding banks. Most of this "leakage" is never to be recaptured or invested into the Navajo communities from which it originated. Disinvestment occurs and few loans are provided. Without intervention, this is unlikely to change.

In asking local bankers why credit is so difficult to obtain for those living on the reservation, they respond by indicating that since reservation lands are held in trust by the Federal government, collateral cannot be perfected, therefore, banks cannot provide credit in many instances.

However, most banks have not thoroughly researched Indian trust lands and its usage in extending credit. This is often the case in reservation lands throughout the country and is not limited to the Navajo Nation. In fact, a bank merger was denied in Montana by the Federal Reserve Board of Governors because the bank in question was not lending to the Northern Cheyenne Reservation area. The bank basically argued that they were limited in their ability to loan to the reservation for many reasons, including the status of the trust lands. The Federal Reserve Board researched this case and rendered a decision on October 7, 1991 in which the merger was denied.

The FED noted that:

> Federal law prohibits a lender from obtaining a mortgage on real property held in trust by the United States government for a Native American tribe. 25 U.S.C 464.

They also noted that:

> Real property held in trust by the United States government for individual tribal members may be mortgaged with the approval of the Secretary of the Interior. 25 U.S.C. 483a. According to the Bureau of Indian Affairs ("BIA"), substantially all land on the Reservation is held in trust by the federal government

for either the tribe or individual tribal members.

It was also pointed out by the FED that:

> The BIA has procedures for perfecting and recording liens, employs appraisers, and issues title reports indicating recorded security interests.

The point is that banks have established loan policy based on erroneous information and or non-researched false assumptions which the FED was unwilling to accept.

The local argument from banks, given to the Navajo Nation, regarding the trust status of reservation lands is extremely weak when one realizes that not all lands within the reservation are trust lands. Some lands are "fee" lands which are unrestricted for collateral purposes. In any case, banks, arguing from ignorance, have curtailed much needed financial services and loan opportunities for Indian people, including those services and loan opportunities which are totally unrelated to collateral concerns. They have continued this line of reasoning for decades. Furthermore, banks exhibit a general unwillingness to explore the real facts of credit issues on Indian reservations. This has prevented any possibility of improvement.

Banks also attempt to defend their reservation non-lending practices based on their concerns regarding repossession rights on the Navajo Nation. According to most local banks, repossession is a big problem for them on the Navajo Nation. Yet, there is not one Navajo law which prevents repossession. There is, however, a Navajo law which provides for the process of repossession through court action. This law basically states that the consumer must consent and that the tribal court will order the repossession. Banks view this process as unfair and too slow. However, a financial institution's reluctance to lend due to Navajo repossession laws is born out of fear because most do not know the Navajo laws nor the Navajo regulations which govern commerce. Banks would like to require that any resolution of conflict regarding loans, including repossession, be handled by Federal or state courts and not tribal courts. This position is unreasonable and unnecessary because the Navajo Nation's tribal court system is ready, able and willing to respond to repossession concerns.

In fact, the whole Navajo Nation is quite flexible in its efforts to create an environment conducive to increasing banking activities to its people, short of relinquishing its sovereignty.

SPECIFIC COMMENTS ON SENATE BILL 2967

1. Small bank exemption

The legislation calls for exempting banks with assets of less than $100 million, ratings of satisfactory or better, and for those located in areas with a population of less than 20,000 from a CRA regulatory exam.

This provision would exempt most banks in and around the Navajo Nation and probably most reservation lands throughout the United States.

The amendment calls for using the regulatory ratings of satisfactory or better in providing an exemption from the CRA examinations. This action is unacceptable because of the difficulty in applying the CRA performance ratings consistently and because there is no assurance that those who received satisfactory or better ratings have earned them, or more importantly, that they will do a good job for their respective communities if they are exempted. The benefit of the doubt should go to the community, not to the bank.

2. SAFE HARBOR

This legislation proposes to eliminate the ability of a community group to challenge a bank's application for expansion if that bank receives a rating of outstanding. This provision also calls upon regulators to consider the investments made outside a bank's community for evaluating purposes.

Banks which may have received an "outstanding" CRA performance evaluation may not have complied with the spirit and intent of the CRA. In terms of challenges, the Navajo Nation, assisted with the option to protest a banks application for expansion, has recently been successful in bringing some banks to the Navajo Nation in an effort to initiate discussions.

Banks, however, have not acted upon their own to reach out to the Navajo Nation, and we have no reason to believe that this will change for the better if deregulated. Therefore, we believe that by providing "safe harbor" to many of these banks, they will continue to ignore the needs of the Navajo Nation while developing the surrounding border towns and cities.

3. Elimination of Supporting Data and Geo-coding from Evaluations.

The elimination of supporting data and geo-coding regulations from the CRA process would be devastating for the Navajo Nation because it would be difficult to show when a bank is engaged in redlining activities or other discriminatory practices. Banks would have less of an incentive to service the Navajo Nation. Presently, examiners review the geographic distribution of an institutions credit extension, applications, and denials. It is this geo-coding requirement that tests whether a depository institution is actually meeting the credit needs of it's lower-income communities. Supporting data and geo-coding requirements should instead be strengthened to the extent that data results are analyzed to insure that a certain level of loan origination is made from depressed areas and that barriers to loan origination(s) be identified and addressed by bank officials.

Elimination of supporting data from evaluations is opposed by the Navajo Nation. Such information provides a checks and balance system to the extent that through it, banks are encouraged to be honest in their revelations as to who they list as meaningful community contacts. Banks which document most conversations to their advantage, do so according to how they "think" a meeting took place, must be regulated. Support data is an ethical tool with which banks should have no problem with.

In conclusion, any change in the present CRA law is premature and undesirable. The Federal government itself has not had a full understanding of how it has worked over the past 15 years. In view of the fact that the Federal Reserve Banks of Kansas City and Minneapolis are engaged in researching this topic as it relates to Indian reservations, an action we welcome and applaud, we recommend that the CRA remain as is until further information is brought to light.

Again, we fully appreciate the opportunity to comment on Senate Bill 2967.

City Council
of the
City of Los Angeles
City Hall
90012

Mark Ridley-Thomas
COUNCILMAN, 8TH DISTRICT

Honorable Alan Cranston, Chairman
and Members of the Subcommittee on Housing,
Senate Committee on Banking,
Housing and Urban Affairs
Room 535, Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senator Cranston and Members of the Subcommittee on Housing:

I am writing to strongly urge you to not weaken the Community Reinvestment Act of 1977.

The mandates of this Act are crucial to urban areas such as the City of Los Angeles. Requirements such as the obligations placed on financial institutions to serve the credit needs of the entire community, including low and moderate income neighborhoods, have allowed the City of Los Angeles to forge new important private-public partnerships.

Over the last few years we have successfully worked with financial institutions, banks and thrifts, to assess community credit needs in predominately low and moderate income areas and craft new programs in response. Currently, with financial institution officials in the lead, we are now at the point of implementing a series of programs which will bring new financing products for business expansion, business startups, and affordable housing developments. A Community Financial Resource Center will be opened soon along with a multi-bank Community Development Corporation. These initiatives have broad based support from a number of financial institutions. Initial pilot projects will be established in South Central Los Angeles and then possibly serve as models for expansion to other low and moderate income areas in Los Angeles and other cities in California.

None of these accomplishments would have been achieved without the existence of the Community Reinvestment Act. The Act and its mandates have provided a useful backdrop which initially helped bring everyone to the table to seriously discuss credit needs, and then keep everyone together to continue working on the task at hand. The Act and the follow-up regulations have allowed Los Angeles City officials, community and financial leaders to work positively together and not dwell and bicker on past performance.

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Evidence of the need for the existing and even stronger Federal reinvestment policies are the local policies which the City of Los Angeles had to adopt to further encourage fair lending. The City Council and Mayor approved a Linked Deposit Banking Policy which I proposed that will place City banking business with financial institutions that have the best lending performance. The City's considerable amount of banking business will be used as leverage to foster stronger bank consumer services and lending in low and moderate income communities.

I do have two suggestions on how Federal community reinvestment policy should be improved.

First, a new system of publicly disclosing the number, type, and location of business loans should be implemented similar to the Home Mortgage Disclosure Act system. It is very difficult to accurately assess business loan needs and lending performance without such data. The lack of such information creates a vacuum of knowledge and makes it difficult to engage in serious work on financing economic development.

Second, the publicly disclosed ratings of banks and thrifts should be made more readily available. Financial institutions should perhaps be required to post a notice of their community reinvestment rating in their lobbies for customers to view similar to the current requirement on posting fair lending requirements and the availability of community reinvestment statements. In addition, all current ratings should be sent on a quarterly basis to all depositories of Home Mortgage Disclosure data so that they are more easily accessible to the public.

These improvements would be valuable but the most important matter is to not retreat on the initial spirit and intent of the Community Reinvestment Act. The City of Los Angeles is now engaged in a broad effort to recover from the civil disturbances of this past April. Resources are being drawn from many sectors of the local community towards efforts of rebuilding neighborhoods, and bringing back desperately needed businesses, services and jobs. Weakening the Community Reinvestment Act would only stifle these efforts since financing is one essential ingredient that cannot be missing. The Act as is today and with the improvements I suggest will help us succeed.

Sincerely,

Mark Ridley-Thomas

Mark Ridley-Thomas
Chairman, Community and Economic Development Committee
Chairman, Ad Hoc Committee on Recovery and Revitalization

NTIC National Training and Information Center
810 N. Milwaukee Ave. □ Chicago, Illinois 60622-4103 □ (312) 243-3035

Testimony Submitted to the

Senate Housing Subcommitee

on the Community Reinvestment Act

September 15, 1992

Gale Cincotta
Executive Director

Thank you, Mr. Chairman, for the opportunity to testify before the Senate Housing Subcommittee. My name is Gale Cincotta and I am Executive Director of the National Training and Information Center.

National Training and Information Center (NTIC) was formed in 1972 to address the redlining that plagued minority and low income, inner city neighborhoods. The orientation was strictly grassroots, the role and purpose to assist grassroots organizations across the country in developing the necessary skills to fight redlining. Since its inception, NTIC has worked actively to develop and strengthen the capacity of grassroots organizations by directly providing training and technical assistance.

NTIC was instrumental in the writing and passage of the Home Mortgage Disclosure Act (HMDA) and the Community Reinvestment Act (CRA) in the 1970s. These two pieces of legislation became important tools to ensure reinvestment in our nation's low income communities.

The Community Reinvestment Act

When traditional means of credit were cut off, HMDA and CRA became the vital tools for rebuilding our nation's inner city neighborhoods and rural communities. The Community Reinvestment Act has provided over 10 billion dollars in reinvestment agreements for communities across the country. NTIC, alone, has helped community groups across the nation to negotiate over $5 billion in reinvestment agreements. In addition, lending institutions have created special lending programs which have resulted in an additional $25 billion in lending agreements for our neighborhoods.

The Community Reinvestment Act is a necessary incentive for lending institutions. With the advent of the Community Reinvestment Act, we have witnessed lending institutions forge new partnerships and create unique lending programs in neighborhoods that they had previously ignored. The Community Reinvestment Act has forced lenders to learn that community banking is good, profitable business.

In the city of Chicago, the Community Reinvestment Act is responsible for bringing three of Chicago's largest lending institutions to the table to create a special program where over $353 million in lending agreements were made. In June of 1984, after a year of intense negotiation, the Chicago Reinvestment Alliance (made up of grassroots neighborhood organizations and community development corporations) and First National Bank of Chicago, Harris Trust and Savings Bank, and the Northern Trust Company announced a $153 million reinvestment agreement. In 1988 and 1989, all three banks announced that they would extend the agreements for even larger goals of $125 million, $50 million, and $25 million respectively, for an additional five-year commitment of $200 million.

Along with this testimony, I have submitted a copy of the five year report of the Neighborhood Lending Program.

The Community Reinvestment Act has been the catalyst for lending institutions to become active players in low and moderate income, minority neighborhoods. Without CRA, many special programs would not occur. If the Community Reinvestment Act is taken away, many banks would withdraw from community lending programs, and our neighborhoods would be back to square one. We cannot afford to stop the revitalization process that has turned devastated neighborhoods into successful, thriving communities. If we are serious about saving our neighborhoods, then we must be serious about our commitment to community revitalization. This is no time to turn our backs on the progress made through community reinvestment.

CRA and Small, Rural Lending Institutions

The banking industry has been complaining that the Community Reinvestment Act is not necessary for small lending institutions. They believe that it is a waste of time and money because in order to survive, small institutions must meet the credit needs of its community. The Congressional response has been to attempt to institute a small bank exemption that would exempt institutions with assets under $100 million (or in rural areas under $250 million) from the anti-redlining CRA and HMDA laws. Each of these attempts would have excluded 90% of all banks and S & L's nationwide from their CRA obligations.

Lending institutions discriminate and redline neighborhoods based on race, income and age of neighborhoods. The size of an institution is absolutely unrelated to whether an institution practices redlining or not. It is the location of institutions that matters, not their asset size.

Many bankers claim that small banks should be exempt from the Community Reinvestment Act because small institutions serve their community anyway. They argue that community banks have no choice but to serve their communities fairly, as this is their only market.

In fact, small lending institutions are some of the worst offenders of the Community Reinvestment Act as an analysis of loan deposit ratios show. Institutions with assets under $100 million have loan-to-deposit ratios that fall far below the average state loan to deposit ratio of 55-60%. Small lending institutions located in small cities and rural communities invest very little of their deposits back into the communities they serve. There are hundreds of small institutions with poor CRA ratings who fail to meet the credit needs of their community.

Small bankers in Iowa also maintain that CRA places an undue financial burden on them. And yet, small, rural banks in Iowa made a record profit of $1.6 billion in 1991. In an article that appeared in the Des Moines Register, February 2, 1992, Alan Tubbs, President of The American Bankers Association, stated, "The country banks right now are as strong as they've ever been." We fail to see how the cost of producing a 1-3 page CRA statement could cause an undue financial burden on small, rural banks with record profits.

Excluding any particular set of institutions from the Community Reinvestment Act is unfair and misguided. Excluding smaller lending institutions provides a privileged status to a particular group of lenders.

Effects of a Small Bank Exemption

Chicago, Illinois--Out of the 174 lending institutions in Chicago, 54 institutions have assets under $100 million, with their total assets equalling close to $5 billion. These institutions are located throughout Chicago's communities and they should no be exempt from CRA, when it is a known fact that they continue to redline low and moderate income, minority communities.

Iowa--Of 610 lending institutions in Iowa, this amendment would leave only a handful of institutions covered by CRA. This would be disastrous. Community groups in Iowa have negotiated with 19 financial institutions and have won over $60 million in CRA agreements.

West Virginia--In many states, like West Virginia, a majority of the state's banks assets are held in small institutions. Nationally, while almost 18% of bank assets are held in banks with less than $100 million, just over 50% of banks assets in West Virginia are held in small banks under $100 million. This means that one-half of the total banks assets in West Virginia would be exempt from CRA. These institutions have an obligation to return some of these assets to the communities.

In some states, small banks represent the majority of bank assets. Small banks are sound and profitable, and some of the wealthiest in the country. Again, why should these small institutions be exempt from their CRA obligations?

CRA and Safe Harbor

Enacting a safe harbor amendment would exempt banks that have outstanding or satisfactory CRA ratings from the Community Reinvestment Act. Currently, over 95% of the lending institutions receive outstanding or satisfactory CRA ratings from the regulators.

Banks that fall under a Safe Harbor rule would be exempt from any community challenges for two years after the rating was issued. Community challenges are the teeth behind CRA and to exempt banks from this process is to deny communities the opportunity to challenge a lending institution's actions. A Safe Harbor rule asks concerned community citizens to surrender their judgement and decision-making ability to the federal regulators who are responsible for evaluating all institutions across the country, large and small, for their responsiveness to community needs. It is not practical to imagine that they can perform this task thoroughly in every community.

We have witnessed many cases of CRA oversight from around the country. Regulators have given passing CRA ratings to lenders with serious problems in basic compliance and fair lending. Many of these institutions would be exempt from CRA challenges for two years.

For example, Columbia National Bank of Chicago, is one of largest banks in the country, received a rating of "Outstanding" from the OCC in July of 1990, after a one day examination. The Outstanding rating was based largely on receiving excellent scores on extra efforts to meet minority and low-and moderate-income credit needs, on participation in government programs, and on special lending efforts. Finally, the bank got an excellent rating for non-discrimination.

In fact, the bank was, at the time of evaluation, in substantial non-compliance with some of the basic provisions of the CRA. Dr. Calvin Bradford, of Community Reinvestment Associates, reviewed Columbia's CRA files. When he went to the bank to review its public CRA file, he was not able to find a single person who even knew what this, or the HMDA statement, were. He was denied access for over two days.

The programs for which the Comptroller gave the bank credit for are phantom programs. The one small business lending program from the City of Chicago for which the bank got the most credit is a program which the bank isn't even eligible to participate in. A simple call to the City Treasurer's Office would have provided the Comptroller with this information.

The banks delineated community covers a white area of Chicago and parts of several white suburbs, but draws its boundaries on the south and east along the racial boundaries of black and hispanic communities. In 1988, only 13 of its 118 mortgage loans and 7 of its 129 home improvement loans were in communities with as much as 20% minority concentrations. Only six loans were made in lower income black neighborhoods in 1988 and the average loan amount for those loans was over $200,000 and as high as $400,000. This strongly indicates gentrification. Columbia's 1990 HMDA data shows that of the 5 loans made in minority areas, 4 of them were to whites, including one loan to a white in a community that is over 98% black.

Clearly, Columbia National Bank was in direct violation of the Community Reinvestment Act yet received an Outstanding CRA rating. We have many more examples of poor CRA oversight from around the country.

In contrast, Harris Bank and Trust of Chicago, a member of the Chicago Neighborhood Lending Programs since 1984, has made tremendous contributions to Chicago revitalization through its extensive lending activity and leadership on the Board of Chicago's Neighborhood Services. (The bank's Senior Vice President for Neighborhood Lending also serves as the President of the Chicago NHS). From 1984 to 1989 Harris made $32.8 million in loans to produce 1,527 new units of housing. Both the pace of development and Harris's commitments are increasing; in the period since 1989, 618 more units of housing and 11 small businesses have been financed, and the bank has committed $85 million more in financing. Harris has made loans of every type for single-family and multi-family housing, as well as for mixed-use and commercial/industrial developments in the inner city.

Harris received a CRA rating of "Needs to Improve" from the Federal Reserve. This damages the bank's good name, blocks their ability to so much as open a new ATM machine, and renders their model efforts in the area of CRA meaningless from a regulatory point of view.

Regulators still have not learned how to review the records of lending institutions Clearly then, CRA ratings should not be used as the basis for exemptions from the Act.

CRA and the Paperwork Burden

The Community Reinvestment Act and Home Mortgage Disclosure Act have been under constant fire over the past year from Congress and the banking industry, due to complaints by lenders that they are overburdened with excessive amounts of paperwork.

The paperwork burden and the uncertainty associated with CRA exams are both symptoms of an irrational and inconsistent enforcement policy. The regulators are creating an unnecessary burden for lending institutions by focusing on the institution's "plan" to meet CRA obligations rather than the results of CRA compliance; that is, did any loans go out? By concentrating on a lending institution's plan, bankers busy themselves with phone logs, memos of meetings, and numerous files in an attempt to satisfy regulators in their quest for CRA plans. Creating this unnecessary burden for lending institutions has created a backlash against CRA and HMDA. If we are serious about CRA compliance then we must return to the original intent of the Community Reinvestment Act which is <u>output</u> not process.

During the past year, CRA and HMDA have been attacked by the banking industry for the time spent on compliance with these two laws. However, in an article that appeared in the American Banker in June 1991, CRA and HMDA were ranked at the bottom of time spent in compliance with Consumer Regulations. In an OMB review of 1,014 state banks regulated by The Federal Reserve Board, the Home Mortgage Disclosure Act "brought up the rear" in total number of hours spent on compliance. 1,014 Banks spent a total of only 130,020 hours at a cost of $2.6 million a year. the Community Reinvestment Act was "at the bottom", with a mere 6,137 hours at a cost of $306,850. Yet it is HMDA and CRA that the banking industry has attacked for being too burdensome and yet a substantial portion of the industry fails to meet CRA obligations.

After this article appeared, The Federal Reserve Board was quick to point out that the numbers for compliance with CRA were too low. According to The Federal Reserve Board, hours spent on compliance with CRA have gone from 6,137 hours to 68,952 hours annually, based on 1,000 institutions.

Yet even when aggregate numbers for hours spent on compliance with CRA are given, the Community Reinvestment Act is not a significant burden to banks in comparison with other consumer regulations.

And when broken down by individual institution, the amount of time spent on compliance with the Community Reinvestment Act fails to show that a significant burden is placed on lending institutions. Based on The Federal Reserve's estimate of work hours spent in compliance with the Community Reinvestment Act, a total of 68,952 hours per 1,000 institutions is spent annually. Based on a 2,000 hour work year per individual worker, according to these numbers, the average lending institution spends only 1.4 hours per week on CRA compliance. Clearly, the burden of compliance is not overwhelming for individual lending institutions.

Evidently, there is a huge misconception of CRA Recordkeeping Requirements necessary to fulfill CRA obligations.

What are the CRA recordkeeping requirements?

- A CRA Statement defining a local community, providing a map of the community service area, reproducing the words of the public CRA notice as defined in the regulations, and listing the categories of loan products the lender is willing to make in its community. This is usually a statement that is no longer than 3 pages.

- Keeping a CRA Public File that has the CRA statements for the past two years, a copy of the Public Notice and any CRA related letters of comments sent to the lender.

- Posting a notice in the lobby informing the public of the CRA. This is a notice, (usually less than a single sheet of paper in length) whose words are precisely defined by the regulations for the Act. Once developed it is unlikely that any more then a few words would ever be changed.

Neither by law, nor even by regulation, do CRA recordkeeping requirements include documents beyond those I just described.

Lenders complain of an excessive paperwork burden and of their uncertainty about how to receive good CRA ratings. Regulators must abandon their requests for irrelevant documentation such as phone logs, lists of community meetings attended by bank staff, and analyses of marketing efforts. They must set clear, consistent, common-sense requirements for compliance so that lenders do not feel they have to produce file cabinets full of paper just to cover themselves. What the grassroots community is interested in is fair access to credit. It is the regulators' job to examine HMDA data, and thereby to evaluate whether loans are being made in a fair and impartial manner, without bias due to race, gender, or income. Community groups have never been interested in the size of a lender's CRA cabinet or the weight of its reports, and we continue to be interested only in the bottom line: Are lenders making all the loans they should be making?

What does all this mean for a lending institution?

It means that this burden of paperwork is an invention of the regulators who are more concerned with a lending institution's CRA process than with its CRA performance. It means that the real enemy of the lenders is not the CRA or HMDA law; we still need laws that protect us against redlining. The real enemy is the bureaucratic burden. CRA compliance must return to the simple, bottomline approach we began with.

The Community Reinvestment Act and the Home Mortgage Disclosure Act are simple laws that work to insure that communities have access to the credit for which they are entitled. It seems that the financial institutions and the regulators have forgotten what the intent of these laws is. Instead of concentrating on the intent and the effects of the law, lenders and regulators are more concerned with the lenders' process for meeting CRA obligations.

The purpose of CRA and HMDA is to insure that loans and banking services are available for the community in which a lending institution is located and which it serves. This is what the banking industry must focus on. If lending institutions are operating in a safe and sound manner, providing services, and making loans to all qualified persons in their communities, then they are meeting their CRA obligations. When assessing a lending institution's CRA performance we must return to the Bottom Line: Are loans being made in a fair manner?

Commercial Loan Disclosure

In the same way in which HMDA and CRA have dramatically increased the availability of residential credit for inner-city and minority residents, disclosure of commercial lending in the inner city would increase access to business loans for neighborhood entrepreneurs and catalyze a much broader process of residential and commercial neighborhood reinvestment. Commercial Loan Disclosure is yet another tool communities could use to rebuild low and moderate income neighborhoods across the country.

In 1975 when the Home Mortgage Disclosure Act was being considered, it was called the Financial Institutions Reporting Act. It included not only public disclosure of residential mortgage loans by census tract, but disclosure of commercial loans as well. Included with this testimony, you will find a suggested format for the geographic analysis of commercial loans made by each lending institution by census tract. In order for this collection of data to be most effective, it should also include Small Business Administration loans and Sole Proprietorship Non-Real Estate Loans. These categories get to the heart of the kinds of credit needed to encourage inner-city entrepreneurship and create new jobs. In addition, in all categories, real estate and non-real estate loans are reported separately.

In Chicago, we have had commercial and residential loan disclosure for institutions holding City deposits since 1974. Chicago bankers can attest to the feasibility and usefulness of commercial loan disclosure. Chicago is a perfect example of how this data was used to negotiate business loan agreements to revitalize inner- city neighborhoods. In the Partnerships For Reinvestment: An Evaluation of the Chicago Neighborhood Lending Programs, pages 15, 18 and 20 show how this data was used to build a case for our negotiation with three major Chicago banks: First National Bank of Chicago, Harris Bank, and the Northern Trust Company. Chicago's commercial lending data showed that commercial loans were, without a doubt, being made only in the downtown area and not to low and moderate income neighborhoods. This data helped communities build a strong case for the initial reinvestment commitment of $153 million in 1984 from these three banks.

Public disclosure of commercial lending should no longer be ignored. If we are serious about rebuilding our communities, then we must have public access to commercial lending data. Commercial loan disclosure will have the same effect as the Home Mortgage Disclosure Act. To date, over $10 billion in reinvestment agreements have been secured for our nation's low and moderate income neighborhoods. HMDA has been an effective tool for housing revitalization. True revitalization requires more than housing, it requires economic growth and stimulus provided by access to credit. We must make commercial loan disclosure our next tool for rebuilding our nation's cities and rural communities.

HMDA Data Released By March 31st

The Home Mortgage Disclosure Act was passed in 1975 and made permanent in 1987. Community groups all over the country fought hard for this law.

The federal HMDA legislation was amended and strengthened as part of the Savings and Loan Bailout in 1989. Congress intended to strengthen HMDA and community reinvestment by requiring lenders to report race, income and gender of borrowers. In January 1990, the Federal Reserve Board issued regulations that violate the intent of the law by denying immediate public access to HMDA data. For the past 15 years the public could get HMDA data on March 31, now the public must wait a year longer. Lending institutions no longer must make their HMDA data available to the public on March 31. Now, lending institutions have to submit their loan data to their federal regulators by March 1st of each year. The Federal Reserve Board now compiles HMDA statements for all lending institutions.

Iowa CCI

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(515) 266-5213

IOWA CITIZENS FOR COMMUNITY IMPROVEMENT

September 14, 1992

Ryan Conroy
Senate Banking Staff
534 Dirksen Building
U.S. Senate
Washington D.C. 20510

Dear Ryan:

Enclosed you will find the testimony that Iowa CCI is submitting to the Senate Banking Committee's Subcommittee on Housing. We have had a great deal of practical experience with the Community Reinvestment Act, especially in relation to farmers and the credit issues they struggle with on a day-to-day basis, and we are pleased to offer our thoughts and ideas on this topic as part of the Subcommittee's September 15 oversight hearing.

We are interested in learning about the outcome of the hearing. Please keep us posted on any developments related to CRA.

Sincerely,

Hugh Espey

Hugh Espey

Iowa CCI

1607 East Grand Avenue
Des Moines, Iowa 50316
(515) 266-5213

IOWA CITIZENS FOR COMMUNITY IMPROVEMENT

TESTIMONY SUBMITTED BY IOWA CCI TO THE SENATE BANKING COMMITTEE'S SUBCOMMITTEE ON HOUSING
September 15, 1992

We want to thank Senator Cranston for inviting Iowa Citizens for Community Improvement (Iowa CCI) to submit testimony to the Senate Banking Committee's Subcommittee on Housing. We have had a great deal of practical experience with the Community Reinvestment Act in recent years, especially in relation to farmers and the credit issues they struggle with on a day-to-day basis, and we are pleased to offer our thoughts and ideas on this topic as part of the Subcommittee's September 15 oversight hearing.

In our testimony we will explain the nature and purpose of Iowa CCI. We also will talk about the work we do in urban and rural areas, and then focus on how we have used CRA over the past 4 years to help family farmers. Finally, we will address three of the main arguments put forth by the banking lobby in its attack on CRA. These arguments are cast in a variety of forms, but the essential complaints are: CRA imposes a financial burden on banks; CRA imposes an onerous paperwork burden on banks; and CRA is unnecessary for small banks because they already serve their communities. Our testimony will refute these arguments.

Iowa CCI is a multi-issue, non-profit community organization that works in both urban and rural areas of Iowa. We organize and empower low and moderate income people so that they have a strong voice in the decision-making processes which affect the quality of life in their neighborhoods, communities and on their farms.

Iowa CCI was founded in Waterloo, Iowa in 1976. Since that time we have established a network of three urban chapters (Waterloo, Des Moines and Council Bluffs) and a farm organizing project that operates in all parts of the state. Our urban chapters address issues related to housing, crime and drugs, and other neighborhood-based concerns.

We started working with family farmers in 1981 on rural credit and reinvestment issues. These efforts, for the most part, have focused on the policies and practices of the Farmers Home Administration, Farm Credit Services, commercial banks and bank regulatory agencies. In 1986 Iowa CCI also began working to promote sustainable farming practices (i.e. farming with fewer chemicals) among grassroots farmers. During the past 11 years over 10,000 farmers and other rural residents have participated in our activities and meetings related to credit/reinvestment issues and sustainable agriculture.

We started using CRA in our farm credit work in 1987. We held informational meetings in rural areas to explain the law and answer questions, and to begin developing a list of credit needs that were applicable and relevant to family farmers. Our particular focus was on the needs of smaller farmers, young/beginning farmers and farmers who were rebuilding their operations as a result of the Farm Crisis.

As a result of these meetings, as well as others that we had held since 1984, we developed a list of farm credit needs that included the following:

1.) the need for affordable interest -- this relates to a variety of situations, including the need for banks to participate more actively in various government-sponsored interest reduction programs such as the Farmers Home Administration's interest assistance program and the state of Iowa's Beginning Farmer Loan Program;

2.) the need for reasonable collateral terms -- many banks will require a lien on all unincumbered property even if the loan is already fully secured or over-collateralized;

3.) the need for reasonable downpayment terms -- it is not unusual for banks to require downpayments of 40% to 50% on farm real estate loans;

4.) the need for loan servicing and debt restructuring -- banks are quick to encourage the liquidation of immediate assets, breeding livestock and machinery in cases involving overdue loan payments, rather than working with the borrower to develop revised cash flows and consider deferrals, reamoritzation, rescheduling, reduced interest and other servicing options;

5.) the need for banks to do more than just say "no" on loan requests -- it is not uncommon for banks to review and deny a loan request from a potential farm borrower very quickly, rather than working with the borrower to reach a feasible "middle ground";

6.) the need for banks to make a special effort to serve the needs of smaller farmers, young/beginning farmers and rebuilding farmers -- these farmers are the ones that are most likely to be overlooked by banks on financing requests.

In 1988 we used the Community Reinvestment Act and this list of credit needs to set up a series of negotiation meetings with Norwest Bank, Iowa's largest banking company. The negotiations led to the establishment of our first family farm lending program in January 1989. Between the fall of 1989 and the spring of 1991 we used the CRA to hold negotiations with two other bank holding companies (Firstar Corporation and Brenton Banks, Inc.) that resulted in two more farm lending programs.

At the present time, our three farm loan programs cover 27 banks in 26 communities across Iowa. Based on lending data that we review and discuss with Norwest, Firstar and Brenton officials every six months, we estimate that our three programs have helped over 450 small and mid-sized family farmers obtain nearly $13.5 million in credit for annual operating and crop input expenses, machinery and real estate purchases, and other agricultural needs. Beginning farmer and interest assistance loans are included in these totals. None of this would have been possible without CRA and the accountability that it provides.

Since CRA means so much to us in terms of our work with family farmers, we were very active with other community groups last year and this year in efforts to save the law. We fought against the Kanjorski amendments in the summer of 1991 and the Shelby-Mack amendments in the fall of 1991. Earlier this year we sent a strong message to the American Bankers Association and ABA president Alan Tubbs, telling them to keep their hands off CRA. We will not let the banks take this law away from us!

The remainder of our testimony will explore three of the main arguments put forth by the American Bankers Association in its attack on CRA. These arguments are: CRA imposes a financial burden on banks; CRA imposes an onerous paperwork burden on banks; CRA is unnecessary for small banks because they already serve their communities

<u>Does the CRA impose a financial burden on banks?</u>

There are two major problems with the "financial burden" claims being made by the ABA and its lobbyists. The first relates to cost of compliance. In recent conversations that we have had with regulators, a point that is continually stressed is that some banks spend money unnecessarily on CRA consultants who promise to help the bank receive a satisfactory or outstanding rating. The regulators state that banks produce a great deal of extraneous material that serves no real purpose. Ironically, the regulators provide information and technical assistance to banks at no cost on matters related to CRA compliance. For example, the Federal Reserve Bank of Chicago includes a sheet in its CRA packet stating that its Community Affairs program "...is dedicated to meeting the CRA information needs of the members banks... In its role as an educator, the Community Affairs staff provides, upon request, technical assistance to state member banks and bank holding companies...The Federal Reserve Bank of Chicago encourages inquiries from banks... regarding community reinvestment issues."

The second problem with the ABA's financial burden complaint is the fact that banks throughout the U.S. are making record profits. The picture that ABA officials paint of the financial health of its member banks changes dramatically when they are not attempting to gut the CRA. ABA president Alan Tubbs of Maquoketa, Iowa said in a <u>Des Moines Register</u> article on February 2, 1992 that "the country banks right now, I would say, are as strong as they've ever been." The article goes on to mention that <u>the nation's farm banks in 1991 earned a record $1.6 billion in profits</u>. The same is true of the banking community in general. It was recently reported that the nation's banks made record profits during the first two quarters of 1992.

If CRA is imposing such a financial burden on banks, why are banks (and farm banks in particular) posting record profits?

Does the CRA impose a paperwork burden on banks?

In a related argument, the ABA and its lobbyists have attacked CRA by claiming that it causes "onerous paperwork." They say that CRA forces them to create an extensive paper trail for regulators, and that while they believe in the "idea" of CRA, it is simply too difficult and time-consuming to produce the documents that the regulators require.

This claim does not stand up to close examination, particularly in the case of small banks. Iowa CCI contacted officials at the Federal Reserve Bank, the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation to find out exactly what paperwork is required during a CRA examination. The answers were illuminating. In the first place, there are only **three** paperwork requirements. These are:

1.) A CRA statement, which typically runs no more than 3 pages.

2.) Maintenance of a CRA public file, which contains CRA statements for the past two years, a copy of the CRA Public Notice and any CRA related comments sent to the lender.

3.) A CRA Public Notice, which is typically less than a single sheet of paper in length.

Altogether the paperwork requirement is less than 10 pages, most of which is similar from year to year.

The other paperwork is merely whatever documentation that the banks have to give regulators in support of their activities related to the five CRA performance categories. These five categories are:

1. Ascertainment of Community Credit Needs
2. Marketing and Types of Credit Offered and Extended
3. Geographic Distribution and Record of Openings and Closings of Offices
4. Discrimination and other Illegal Credit Practices
5. Community Development

In each of our conversations, the regulatory agencies stated they tailored their expectations to the bank's situation. Thus, they did not expect a bank in a town of 400 to produce the same computerized analysis of loan distribution that a bank in downtown Chicago would produce. Most interesting of all, however, was the amount of time that the Federal Reserve estimated was necessary for banks of varying sizes to complete the necessary paperwork for the CRA. For banks with under $100 million in assets (approximately 90% of all banks) only 20 hours per year per bank were needed to complete the paperwork for CRA. Estimates from other regulators were even less. **This figure boils down to 24 minutes of staff time a week!** This hardly seems onerous, particularly when one considers the amount of reinvestment that CRA has produced across the country.

Is the CRA unnecessary for small banks?

By far the most commonly voiced complaint from banks, however, is that the CRA is a waste of time and money for small banks, because these institutions must serve community credit needs or go out of business.

The idea that all small banks automatically serve their community's credit needs is ridiculous. In Iowa alone, 53 banks (there are 562 banks in Iowa) with assets under $100 million also have loan-to-deposit ratios ranging from nearly 0% to 35%, well under the state average of 57%. In other words, they loan no more than 35 cents of every dollar that is deposited. Moreover, these banks have made a total of only 14 Beginning Farmer Loans throughout the nine year life of the state loan program. The Des Moines Register also has written stories in recent months about 3 other small Iowa banks that were cited by regulators for major violations, including inside trading, improper loan practices and other problems.

Finally, the CRA process has itself identified other small banks that did not serve the needs of their communities. These banks were cited for items such as a 10% loan-to-deposit ratio, uncompetitive loan terms and down payments, non-participation in relevant governmental programs and apparent violations in the Equal Credit Opportunity Act and Fair Housing Act. Even a number of banks that received "Satisfactory" ratings were clearly not serving their community's credit needs. These banks were cited for low loan-to-deposit ratios, violations of the Equal Credit Opportunity Act and the Fair Housing Act, and lack of participation in Student Loan programs. Clearly, there is a need to regulate small rural banks as well as other banks. The CRA is particulerly valuable in these towns, because there are few external standards to hold the banks accountable otherwise.

Concluding Remarks

We are opposed to any changes in CRA that would allow banks to side-step their responsibility to serve the public and help meet community credit needs. In particular, we oppose small bank exemptions, safe harbor provisions and self-certification. All of these ideas are smoke screens. The ABA and its lobbyists don't like CRA because it give grassroots people power. It enables groups like Iowa CCI to hold banks accountable for their lending policies and practices, and it gives us a voice in decisions that affect the future of our communities.

Every time since the summer of 1991 that we have asked the ABA or its member banks to provide tangible proof that CRA causes burdensome paperwork and unnecessary costs, we've received nothing. All we hear is unsubstantiated stories with no hard evidence. It's time that the ABA and its lobbyists stop complaining about CRA and start recognizing it for the contributions it has made to our rural and urban communities.

NCRC

Testimony

of

John Taylor

Executive Director

National Community Reinvestment Coalition

Washington, DC

The Subcommittee on Housing

of the

Senate Committee on Banking, Housing and Urban Affairs

September 15, 1992

Thank you for the invitation to comment on the performance of financial institutions in fulfilling their obligation to help meet the credit needs of their local communities.

NCRC

The National Community Reinvestment Coalition (NCRC) is well positioned to provide input on this subject, as the Coalition represents the largest and most comprehensive gathering of organizations involved in community reinvestment issues.

To date, some 137 organizations comprise the membership of NCRC. These organizations collectively cover every state in the country and represent the single largest community voice on the subject of community reinvestment. A complete list of the NCRC membership is attached to this document.

From this broad wealth of experience and knowledge, NCRC is able to provide empirical and irrefutable comment on low-income and minority people's experience with bank lending.

CRA WORKS

The commendable work of Congress which resulted in the Home Mortgage Disclosure Act (HMDA) and the Community Reinvestment Act (CRA) and their subsequent achievement in passing the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA) have produced positive and measurable results. Current estimates for bank commitments to low-income and minority communities and people total $30 billion.

This figure represents an amount resulting from CRA challenges, where a local financial institution responds to community protests with specific dollar commitments. It is estimated that an additional $30 billion has been provided to low-income and minority people and nonprofit developers not as a result of CRA challenges, but because of financial institutions being sensitized to the legal requirements of CRA.

CRA has resulted in the development of affordable housing in many of America's poor urban and rural communities. Nonprofit developers have relied upon CRA as the leverage to have financial institutions finance their efforts to address homelessness and the lack of decent affordable housing for some 15 years. Since passage of CRA, community developers have produced over 300,000 units of affordable housing. In addition some 90,000 new jobs have also resulted from community based initiatives financed by CRA-driven bank investments.

Financial institutions must provide the capital to address credit needs of the poor

The production of decent affordable housing and quality employment opportunities requires an initial investment on someone's part. It is clear from any accurate historical analysis of the federal government's recent investment in affordable housing, one obvious conclusion can be made. During the past 12 years there has been a radical shift in the directing of federal support for housing to other areas of the federal budget. Let us set aside the merits of these budget decisions (since this is not the point here) and consider two obvious results. First, there has been a dramatic increase in the number of people, families, who are unable to secure decent affordable housing, in many cases any housing at all. The second result is the shifting of a significant portion of the burden and responsibility for the provision of affordable housing from the federal government to the private sector. It is this point that is of obvious importance to these hearings.

The federal government has decided to not follow the example of many European countries, which have increasingly 'grant driven' economies, where housing, job development, training and other social needs are increasingly financed by the public sector. Very few private initiatives, to address social and economic ills, are present in these countries. It is expected that the central (federal) government is primarily responsible for providing solutions to such problems. The result of this policy is significantly higher taxes, and in certain European countries the income tax rate is as high as 40%-50%.

In the United States we have chosen to not match the tax rates of these countries, but to encourage partnerships with private sector investments and initiatives. In contrast to a 'grant driven' economy, we have chosen to support a 'capital driven' economy. Instead of tax increases of more immense magnitude we have chosen more modest increases and in the case of certain higher incomes and corporate incomes, decreases. It is within this framework and political structure that we hope to address our social and economic needs. Clearly CRA is not a substitute for government investments in affordable housing and other initiatives to help low-income and minority people. However it is equally clear that most low-income and minority people will not participate in the mainstream of the American economy without access to capital.

Capital is in the hands of America's roughly 12,500 financial institutions. Absent their interest in a community's economic revitalization or the production of decent and affordable housing, only limited success will be witnessed. It is the Community Reinvestment Act which mandates the interest of these institutions in addressing these community needs. Without a strong CRA there would be few examples of financial institutions addressing the needs of America's distressed urban, suburban and rural communities. Indeed it was because of the lack of such attention to certain neighborhoods' credit needs that CRA became law in 1977.

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Unless Congress is willing to reverse the notion of being a more and more 'capital driven' economy in favor of a 'grant driven' economy then we will increasingly rely upon financial institutions to play a major role in financing initiatives and efforts to address this nation's shame of homelessness and our growing unemployment crisis.

Is it fair to regulate the financial institutions and to require them to meet the convenience and needs of the communities they serve? Indeed, it is not only fair, but just and sound policy as well. One argument of the government's right to regulate is that it charters these institutions and as such has the ability to establish certain requirements and regulations. However it is the provision of insuring the savings of depositors (up to $100,000 per account) that gives the federal government the ultimate right to regulate these institutions. Since the taxpayer is on the hook for a financial institution's failings, Congress not only has a right, but a fiduciary responsibility as well to insure the regulation of these institutions. Indeed the American taxpayer and Congress are now witness to the extreme costs associated with insuring this industry with the current $400 billion savings and loan bail out, a figure which continues to grow.

Consider the corpcrate advantage of financial institutions, how well would any private corporation do if investors were told that their stock purchases were insured by the federal government?

It is this now costly government guarantee of depositors' funds that requires the federal government to regulate the safety and soundness of these institutions and which also allows us to require these financial institutions to meet the credit needs of the communities they serve. It does not call for making poor or risky loans, but the law does require that all people be treated fairly and in a non-discriminatory manner when seeking credit. This law is consistent with the principles established in our constitution and with the Civil Rights Act of 1866. It is policy adhered to throughout our country's history.

When one considers the corporate advantage given those who operate financial institutions along with the clear direction of our recent federal leaders to rely less on the government and more on the private sector for economic and social development, then it is clear the need for a sustained and unequivocal commitment from the financial community remains high.

No single piece of federal legislation is as important in promoting the commitment of financial institutional involvement in addressing economic needs as is the Community Reinvestment Act of 1977.

ARE THE BANKS COMMITTED TO CRA?

I purposely began this testimony with a discussion of the positive aspects of CRA, what has resulted from this legislation and why it remains a necessary and vital part of our economic well being.

Unfortunately, the current experience of NCRC and its members is that low-income and minority people's access to credit continues to be a very difficult proposition. It is the exceptional financial institution that takes CRA seriously and makes a sustained commitment to ascertaining the credit needs of low-income and minority neighborhoods. Instead we hear from groups nationwide that bankers are more concerned in filling their CRA files with information, rather than filling their portfolios with loans.

In fact many lenders have long been under the mistaken impression that merely having a CRA plan and making an effort to fill their CRA file with outreach and marketing information was sufficient to merit a 'satisfactory' rating from a bank regulatory agency. At our own NCRC annual meeting in February, 1992, a ranking officer of the Office of the Comptroller of the Currency confirmed what many of us feared when he noted that a financial institution could receive a 'satisfactory' rating with simply a good CRA plan.

This comment is made despite a clear statement from the Federal Financial Supervisory Agencies in April, 1989 that future plans for CRA commitments are not to be viewed as part of an institution's CRA performance. However, the impression by lenders that planning and marketing alone, not lending, continue to be such a pervasive industry standard, that the regulators felt compelled to issue another directive this summer (1992) specifically stating that adherence to the objectives of CRA involved making loans, not just planning and marketing.

NCRC Members from every region in the country continue to tell of their experiences with local financial institutions where a CRA officer attends a community meeting, politely introduces himself/herself to meeting participants, expresses interest in meeting community credit needs, but makes clear his/her inability to make loans, since he/she is a CRA officer and not a lending officer. Financial institutions fail to recognize the need for all lenders, management staff and board members to become knowledgeable of the requirements and objectives of CRA. Our members continue to inform us that for most lenders CRA continues to be operated through their public relations department rather than their lending department.

The recent record of ratings issued by the four bank regulatory agencies gives evidence to a reduced adherence to CRA by lenders. During the 1980's on the average between 1% to 2% of financial institutions received failing ratings from bank examiners. During 1990 and 1991 that figure has risen to an average of between 11% - 12%! This trend appears to be continuing into 1992. In the first half of 1992, failing grades were issued to 12% of all those banks examined during this six month period. In some cases the failure rate was dramatic. In Florida for example over 28% of the financial institutions examined this year received failing grades. Most of NCRC's members believe that the actual failing rate would wasn't such a 'pro-lender' attitude on the part of most bank regulators.

On the whole our experience nationwide continues to be that most financial institutions give CRA only minimal and peripheral treatment. Most lenders remain woefully ignorant of the objectives and requirements of CRA. Lenders spend little energy on assessing community credit needs, understanding the credit needs of low-income and minority borrowers and even less time lending actual dollars to these constituents.

<u>The alleged paperwork burden is really a ruse to weaken CRA</u>

The American Bankers Association (ABA) and the Independent Bankers Association of America (IBAA), trade associations for financial institutions, have been promoting the unsubstantiated argument that CRA creates a costly and overly burdensome task for local lenders.

There is simply no documented hard evidence that substantiates this claim. Further, our own field experience tells us that the reporting requirements associated with CRA are, for the average lender, minimal and inconsequential. The reporting requirements of CRA are clear and brief, requiring only the following.

1. The financial institution must maintain a public file, containing its two most recent CRA statements, its CRA rating and any comments it received relative to its CRA performance.

2. Lenders must post a CRA notice (the language of which is supplied by the regulators).

3. Finally, the lender must develop a CRA statement which defines the area they will serve, the type of loans they will make and include some language about CRA.

This is all the paperwork burden required by the Community Reinvestment Act of 1977. Beyond these requirements are the reporting requirements issued by the various bank regulatory agencies. According to the regulators these reporting requirements are hardly a burden and require only minimal amounts of reporting time from the lenders.

In fact in 1991 the Office of Management and Budget (OMB) studied the various consumer compliance costs associated with the regulatory responsibilities of financial institutions and concluded that of the six different bank reporting requirements the CRA requirements were the least burdensome of all. It is revealing that in spite of OMB's conclusions which show that several other reporting requirements precede the CRA reporting requirements in actual burden, CRA remains at the top of the lenders 'hit list' for legislative review.

NCRC has had members in various parts of the country visit their local institutions and they simply have not been successful in locating lenders who substantiated this paperwork burden claim.

In the Milwaukee area one of our members specifically set out to examine CRA files of area financial institutions in order to get a clearer picture of the reporting actually being carried out by the various institutions. In all, this group visited 90 financial institutions, their findings were informative. The average CRA statement of these 90 banks was just over 8 pages. Over 34% of the statements were four pages or less. Only 4% were over 20 pages in length. The researchers involved in this project reported that "while most lenders were polite and helpful, many indicated little if any understanding of CRA." The group further concluded that many lenders simply did not take CRA very seriously.

How can a paperwork burden be so onerous, so burdensome that on the average a bank requires only slightly more than 8 pages to write its CRA statement, the heart of any CRA examination. Lets consider this question from another perspective. Is it fair for the American public and Congress to ask lenders to provide about 8 pages of evidence per year to substantiate their community reinvestment activities in exchange for the continued financial guarantees (already exceeding $400 billion) to insure that depositors will continue to do business with those institutions? People we talk to in nearly every state think it more than fair.

The fact is that the CRA burden is minimal and always has been. The real story here is one of pure propaganda, promoted by those who wish to weaken CRA but who hide behind the sympathetic, but transparent shield of regulatory burden. OMB is not fooled, the Banking Regulatory agencies know the burden is minimal, the public knows, surely Congress knows as well.

Home Mortgage Disclosure Act needs to be improved

The Home Mortgage Disclosure Act of 1975 (HMDA) has been an invaluable tool in allowing community groups, public officials, regulators and citizens the opportunity to measure a bank's commitment to a given community or neighborhood. However a major shortcoming of this legislation is that it failed to include all Americans and in particular many rural communities are not currently covered by this law since it is limited to banks with $10 million or more in assets and in a Metropolitan Statistical Area. NCRC hears frequently of the many difficulties people in rural communities have in obtaining credit. Having access to HMDA would help clarify the lending picture in many of these small communities. This HMDA limitation should be corrected immediately.

The absence of the reporting of small business and commercial loans reveals yet another major shortcoming of HMDA. In all fair lending legislation we seek to promote the goal of financial institutions meeting the credit needs of a community. The credit needs of any community include business and commercial development needs. Without access to information which demonstrates a lender's record of performance in business and commercial lending then we shall continue to have only a partial picture of a lenders record of community reinvestment. The rising national unemployment rates should be a strong indicator of many communities' critical needs for financing of small business and commercial enterprises to respond and alleviate high unemployment rates.

There exists little or no sources available to community people to allow them to learn of a particular lender's loans to businesses. Unlike the housing market which requires recorded deeds and other records of housing transactions and loans, there is no such vehicle for business lending. It remains nearly impossible for communities to ascertain an accurate picture of a lenders business lending activities in a given community. With such an accurate picture, public officials, community people, business people and others would benefit. HMDA would be strengthened and more valuable to all citizens if such reporting was made available to the public.

Equally important is the need to increase the accessibility of the HMDA data. Currently the data collected by the Federal Reserve Board is provided to interested parties, including community groups, in a format which requires either expensive computer equipment (e.g. mainframe computer) or a complicated and convoluted transcription process. In either case the HMDA data continues to be inaccessible and not usable to the average consumer. In a meeting in spring, 1992 with Fed Governors LaWare and Lindsey, NCRC presented a suggested model for simplifying the dissemination of the HMDA data, along with several sources of potential private funding to assist in the data distribution. As of this date the HMDA data format remains identical and as inaccessible as in previous years. This must be rectified if the intent and spirit of HMDA is to ever be realized.

Similarly, it is important within the HMDA data to have accurate information on loan application processing time. One method to discourage and deny borrowers has been to respond slowly to their loan requests. This is particularly true for those seeking residential property loans, where commonly a date is set for purchase and sale. A good example of this problem is the experience of NCRC member Mary Compton, from Unidos Para La Gente in San Marcos, Texas. This organization helps working class Mexican-Americans gain access to credit for their various needs. This past year Ms. Compton approached officials in a local branch of Nation's Bank. After explaining to the lender her role was to assist the borrowers, unfamiliar with the loan application process, the borrowers and Ms. Compton began a long and arduous journey of telephone calls, paperwork and disappointments. The outcome of their experience was that the process for obtaining a home mortgage took over twelve months and still no bank commitments were made. Finally, the borrowers gave up and no longer pursued Nations Bank for financing.

While this bank did not actually deny a loan, it was clear from those involved in this experience that the process had the de facto result of loan denial. NCRC believes such occurrences are common and it is therefore imperative that the HMDA data made available include information on processing time. This requirement would add no extra time to the work of the reporting bank since such information is collected when a borrower fills out an application.

Finally, the accuracy of the HMDA data being released must be questioned. The Center for Community Change, an NCRC member, reported widespread reporting deficiencies in the 1990 HMDA data, citing missing information in various required reporting categories. Another NCRC member, the Pittsburgh Community Reinvestment Group studied the HMDA data reports of most of the financial institutions in the Pittsburgh, PA area. Their findings were astounding. PCRG matched the county records with the HMDA data reported to the Fed and found that at a minimum lenders erred at least 20% of the time and at a maximum one lender was more than 50% inaccurate in their HMDA reporting. Without the availability of accurate and complete information about a lender's performance it will remain a difficult and haphazard task for those involved in assessing any lenders community reinvestment performance.

The record on rural banks

The CRA record of rural banks is dismal. CRA consultant Ken Thomas, from Florida revealed in his research that small banks (under $100 million in assets) received 71% of all the failed ratings issued by the various bank regulators. The 1992 statistics for the first six months show our strong agricultural states, Florida and California leading all other states in garnering poor ratings.

Of all our 50 states it is Iowa which leads the nation in having the most CRA agreements, these resulting from community challenges. If rural lenders adhered to CRA why would a predominately rural state lead the rest of the country in this unwanted statistic?

NCRC has a cadre of organizations representing rural communities and people, like First Nations Development Institute, National Rural Development and Finance Corporation, NY State Rural Housing Coalition, Rural Opportunities Inc., Iowa Citizens for Community Improvement, North Carolina Low Income Housing Coalition, Community Reinvestment Alliance of North Carolina, Florida Federation of Community Development Corporations, and several other organizations. Their experiences with lenders in rural America is consistent. Fewer financial institutions pervade the rural landscape, competition is less, the credit choices for the rural consumer are less. Rural lenders are inclined to lend to the large scale farmer, ignoring the smaller family farmer. Farmers and consumers are hard pressed to be publicly critical of a lender's performance because of the tight knit nature of rural communities, where a high profile sometimes results in further ostracizing by other segments of the community. Contrast this situation to an urban environment where if someone is highly critical of a lender's performance, few people, if any, in his/her own community even know of the criticism. Furthermore, that same person could approach any number of other lenders if dissatisfied with one lender's performance. Additionally, rural lenders, in contrast to larger lenders, loan out a lower percentage of their funds. The loan to asset ratio for larger banks is nearly two-thirds, while their smaller counterpart lends at a ratio closer to only 50%.

The competition in rural America, including and in particular on Native American Reservations, is not comparable to that of suburban and urban America. Bank products and services are established with little or no competition present. The consumer has few options to shop around. It is because of this fact that rural banks are enjoying unprecedented profits and success. This fact prompted ABA President Alan Tubbs to note at this year's Agri-Bank Conference that the rural banks were in the best shape he had even seen them in.

Exacerbating the credit problems in rural America are the changes taking place in the banking industry as a whole. The concept of 'Bigger is Better' has taken hold and mergers and consolidations are providing even fewer and fewer choices to the rural consumer. Recent studies, including a study from the House Banking, Finance & Urban Affairs Committee, released in April, 1992, (Analysis of Banking Industry Consolidation issues) shows that such mergers and consolidations have produced none of the streamlined and reduced costs promised in consolidation.

Instead, tens of thousands of bank-related jobs have been lost, rural consumers are left without basic banking services or the choice to travel great distances. And NCRC members report increasing ignorance and insensitivity from lenders who neither live nor work in, or even near, the borrower's community. The larger financial institutions have board trustees who are unfamiliar, inexperienced and uncommitted to meeting the needs of the family farmer, rural entrepreneur and rural community as a whole. While these may be boom times for rural lenders, they are bust times for rural borrowers.

The notion that CRA reporting requirements for rural banks is a burden is simply inconsistent with current known experiences. NCRC members have been asked to speak with bankers about this alleged burden and have found no evidence of such a burden. We have attempted to locate lenders who are used as examples of having suffered through an alleged over-regulation process, but have been unsuccessful in getting any specific names of banks for this effort.

The fact is, a careful look at this alleged paperwork burden shows a complete lack of hard evidence to support this claim. Further, any examination of the Community Reinvestment Act disputes allegations that CRA requires extensive reporting. The paperwork burden argument is presented by self-serving bank trade associations desirous of continued federal government support and guarantees, but without any regulation or requirements relating to meeting the credit needs of all Americans.

Summary

The Community Reinvestment Act and the Home Mortgage Disclosure Act have been vital pieces of legislation which have produced measurable positive results. However, widespread unfair lending practices permeate our landscape. Most financial institutions continue to give only peripheral attention to the spirit and substance of the fair lending laws. This situation particularly worse in minority, low-income and rural communities. Unless the private financial community accepts its responsibilities relating to providing the needed capital to reverse distressed neighborhoods and deteriorating family farms, then America's economic problems will continue to worsen. Instead of meeting these challenges the bank trade associations are seeking to abandon CRA by hiding behind the false claim of paperwork burden. The bank regulatory and enforcement process is in need of substantial changes in order to effectuate a fairer and more equal lending environment. Further NCRC would like to offer its organizational resources to work together with Congress and others to develop policies and programs which will result in a more equal system of lending, with more useful and accurate reporting requirements.

ASSOCIATION FOR ENTERPRISE OPPORTUNITY

September 24, 1992

The Honorable Senator Alan Cranston
Subcommittee on Housing and Urban Affairs
Committee on Banking
United States Senate
535 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senator Cranston:

The Association for Enterprise Opportunity respectfully submits the following testimony as part of the record for the oversight hearings on the Community Reinvestment Act, held September 15, 1992. We would like to state our opposition to any changes in the CRA that would weaken the provisions as they relate to rural banks.

The Association for Enterprise Opportunity represents over 150 microenterprise and self-employment programs in 41 states working to assist low-income individuals, minorities, and women to start and expand their own businesses. We exist, in large part, because these individuals and communities face a credit gap. Banks are reluctant to lend to microenterprises without linkages to an intermediary because of concerns about risk, excessive transaction cost, and investment in low-income neighborhoods.

Our programs have emerged to meet needs unmet by banks and to develop partnerships with banks to serve these needs. These financial institutions are important partners. They provide us with assistance and capital for our lending activities, and in some cases provide our clients with low-cost banking services. But their willingness to work as partners with us is largely a result of the obligations they face to comply with the CRA. In fact, in seeking to move toward our goal of providing credit to people and communities with limited means, we would like to see a strengthening of the CRA to more explicitly recognize the importance of bank investment in economic development initiatives such as microenterprise programs, not a weakening of the Act.

Thank you for the opportunity to present our position to the Committee. Please do not hesitate to contact the Association should you or your staff have further questions about our statement.

Sincerely,

Beverly L. Smith
Executive Director

Robert E. Friedman
Chair, Board of Directors

Enclosure

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Statement of the Association for Enterprise Opportunity

Submitted to

Subcommittee on Housing and Urban Affairs
Committee on Banking, Housing and Urban Affairs
United States Senate

As part of the

Oversight Hearings on the Community Reinvestment Act
September 15, 1992

Senator Cranston and Members of the Committee: the Association for Enterprise Opportunity is submitting this testimony to state its opposition to any weakening of the current provisions of the Community Reinvestment Act as they pertain to rural banks.

The Association for Enterprise Opportunity (AEO) is a membership organization representing 150 organizations across the nation who are engaged in assisting people and communities with limited access to economic resources to start businesses. Our member organizations are located in 41 of the 50 states. A great many of these operate in rural areas. Typically, the services that these nonprofit or public agencies provide include training, management assistance, and importantly, access to credit for entrepreneurs who cannot gain access to traditional credit sources.

Many of our clients are low-income individuals; some of them are recipients of public assistance. In some cases, our clients have been operating their business when they come to us for assistance, but on a very marginal level. They seek our assistance in securing the capital to expand their activities. Other clients are seeking to start new ventures, but although they have skills in their chosen industry, they lack both management skills and access to capital that can allow them to create their own jobs and to add to our nation's economic activity. Our members vary the exact nature of their services according to the needs of their particular clients and communities; but access to financing is always a critical piece of the services they offer to both existing and potential business owners.

The microenterprise field is relatively new in this country, although decades old in the developing world. The oldest U.S. microenterprise programs are about 10 years old; most of the programs operating in the U.S. have been in existence only a few years. However, the size of the field has expanded rapidly in recent years. From a handful of programs ten years ago, we estimate that the field has grown to include about 200 programs today. In addition, as our programs and association receive media attention, we continually receive requests for information from new groups interested in starting a microenterprise program, and from low-income individuals seeking the services of such organizations.

Among the key challenges currently facing our field are the needs to secure financing for microenterprises, and funding to support the provision of technical assistance, training, and general operations of microenterprise intermediaries. Banks have increasingly played a role in helping to finance microenterprises and microenterprise intermediaries, as well as in providing other needed financial services to our clients. However, their support has been driven almost exclusively by their obligation to satisfy the requirements of the Community Reinvestment Act. Without those provisions, we believe that it is highly unlikely that banks will continue to support our programs, which play a critical role in meeting the capital needs of individuals and businesses to whom banks are unwilling to lend.

A variety of models have emerged for bank participation with microenterprise intermediaries. We would like to provide you with a few examples of roles that banks have played to date.

- In Iowa, banks provide loans to the clients of the Institute for Social and Economic Development (ISED), a microenterprise program operating throughout Iowa. Some loans are provided to clients with the back-up of a guarantee from the ISED program; other banks loan without the guarantee. The self-employment program provides the training and technical assistance that enable its clients to develop the business plans and skills required to obtain bank loans.

- The Working Capital program, which operates in rural areas in western Massachusetts, Vermont and New Hampshire, secures funding for its capital pool through loans from area banks. Private institutions lend the money to Working Capital, which in turn lends the funds to its clients through a peer-lending mechanism.

- The Womens' Self-Employment Project in Chicago has succeeded in getting banks to provide checking accounts to their program participants at a very reduced cost. This is important because entrepreneurs clearly need checking accounts -- and preferably separate business accounts -- to operate their businesses. However, for many small-scale, start-up businesses, the regular monthly costs of maintaining a business checking account are simply too high.

- The Detroit Self-Employment Project (DSEP) has two different arrangements with local banks. In the first, DSEP has deposited a foundation grant as a loan loss reserve with an area bank, which then makes loans directly to clients. In addition, four other area banks have formed a consortia to make loans to program clients. In their case, they also make loans directly to the clients, but with a 30% guarantee from the DSEP program.

Although each of these programs has developed different arrangements with local banks, each attest that the existence of the Community Reinvestment Act played a key role in the decision of the banking institutions to work with their program. The banks themselves acknowledge that they consider these loans too risky and too costly to undertake on their own, and that only with the existence of intermediaries which can provide technical assistance, loan loss reserves or guarantees to offset risk, and pressure in the form of the Community Reinvestment Act will they choose to work with and support microenterprises.

Finally, perhaps the most important role that banks can play is to make loans directly to our customers, without the intervention of our programs. Microenterprise programs are built upon the concept of graduation. We envision that after a period of working with a client, they will have the expertise and the business track record that will enable them to obtain a traditional business loan. But our experience thus far has taught us that too many banks remain unwilling to make loans to these commercial customers. As a result, both economic growth and economic opportunity are impaired.

As we have noted above, at the present time the primary incentive that banks have to work with our programs is the requirement that they comply with the Community Reinvestment Act. Trends within the banking industry have tightened the availability of credit for all small businesses. Bank acquisitions and consolidation of the industry have led to a pattern of centralization of commercial lending functions in headquarters cities, often far from small rural businesses. Bank failures and the economic recession have made smaller banks even less willing to take on the risk of small commercial loans. In the face of such trends, it is highly unlikely that banks would consider participation with microenterprise programs without the offsetting force of the CRA requirements.

Therefore, from the Association's perspective, the Community Reinvestment Act is critical to our ability to serve our clients. Rather than weakening the provisions as they relate to rural banks, we recommend clarifying and perhaps tightening current provisions. One specific step that we recommend is to clarify the law to state that participation in economic development activities such as microenterprise programs clearly counts toward fulfilling the requirements of the CRA. Many microenterprise programs currently face difficulties in securing local bank participation because banks are unsure whether they will receive CRA credit for such activities. Clarification of that point would be a simple, low-cost way of improving the chances that banks will become active participants in this growing number of development programs.

The microenterprise field has emerged in larger part because low-income individuals, minorities, women, and others residing in low-income communities cannot secure business financing from banking institutions. We have stepped in where banks will not tread alone. But the growth and survival of our alternative financial institutions depends in part on the degree to which banks work with us as partners. Any weakening of the current CRA requirements will remove the primary incentive that banks -- whether in rural or urban areas -- have to provide microenterprise programs with needed financial support. As a result, we strongly oppose any steps that would reduce the CRA requirements faced by banks in rural areas.

Thank you for allowing us to submit our statement. For further information on the Association for Enterprise Opportunity's position, please contact one of the following individuals:

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Testimony Presented to

the Subcommittee on Housing and Urban Affairs

of the Committee on Banking, Housing and Urban Affairs

by

the Association of Community Organizations for Reform Now (ACORN)

The Honorable Alan Cranston
Chairman

September 15, 1992

Introduction

ACORN appreciates the opportunity to submit testimony to the Subcommittee on Housing and Urban Affairs on the enforcement of the Community Reinvestment Act (CRA), and ways of increasing the flow of credit to underserved urban and rural communities.

We wish to especially commend Chairman Cranston, who has a long and distinguished record of working to promote affordable housing, for holding these crucial oversight hearings. We appreciate Chairman Cranston's leadership role in ensuring that important consumer protections were included in last year's banking bill, the Federal Deposit Insurance Corporation Improvement Act (FDICIA). Your leadership and advocacy on behalf of low- and moderate-income families will be sorely missed.

ACORN

ACORN, the Association of Community Organizations for Reform Now, is the country's largest grassroots organization of low- and moderate-income families. Founded in Little Rock in 1970, ACORN has grown to a membership of 100,000 member families in 26 states and the District of Columbia.

ACORN members work on a wide range of issues that affect the everyday quailty of life in their neighborhoods, including access to affordable health care, neighborhood safety, and drug prevention. ACORN Housing Corporation develops affordable housing in a dozen cities, and performs loan counseling for thousands of low-income families every year. ACORN was the first community group to challenge a bank merger application, and the first to secure a CRA agreement. Since 1980, ACORN has secured over two dozen CRA agreements with lenders from Phoenix to Flatbush that have resulted in nearly $800 million in loans in underserved neighborhoods.

Summary of Testimony

Our testimony today has 7 principal points:

(1) The Community Reinvestment Act (CRA) should be viewed as an elaboration of decades long public policy principles, which hold that depository institutions, due to the unique public benefits conferred on them and their special purpose as capital intermediaries in the macro-economy, have an affirmative responsibility to meet the legitimate credit needs of all neighborhoods and the productive economy;

(2) The CRA has proved to be a remarkably potent tool for lessening poverty and promoting economic development, and has leveraged billions of dollars in private investment in underserved urban and rural areas through partnerships between lenders and low- and moderate-income communities;

(3) However, there remains alarming evidence of pervasive redlining by lenders, underscored by analysis of 1990 HMDA data, and some evidence that the situation has deteriorated in recent years, due in large part to broader changes in the structure of the banking industry;

(4) Problems of credit availability remain the principal obstacle to job creation, neighborhood revitzalization, and community development in low- and moderate-income communities in underserved urban and rural communities, and public policy is unlikely to be able to solve problems of poverty without a concerted effort to increase credit availability in distressed areas;

(5) Enforcement of the Community Reinvestment Act (CRA) has been scandalously poor. Regulators have issued "inflated" ratings in the face of stark evidence of redlining, have minimized opportunities for public participation in the regulatory process, and have rarely taken proactive steps to correct identified violations;

(6) Proposals to exempt depository institutions from the CRA based on their size, location, most recent CRA rating, special purpose, or other criteria are misguided and unjustified and would exacerbate the acute distress experienced by poor urban and rural communities;

(7) Congress can take several steps to increase the availability of credit in low- and moderate-income communities, but in lieu of better enforcement and strengthened laws, we are likely to see more dramatic and sweeping attempts to get depository institutions to meet the credit needs of communities.

Summary of Recommendations

While ACORN believes that many of the necessary reforms must occur at the regulatory, rather than the statutory level, there are several important steps Congress could take to enhance the flow of capital to underserved communities. Specifically, Congress should:

(1) Significantly Strengthen Community Lending Requirements as a Condition of New Bank Powers, Particularly Interstate Branching;

(2) Expand Community Support Requirements to Non-Bank Players in the Mortgage Lending Chain, Including Mortgage Companies, Appraisers, the Secondary Mortgage Market Entities, and the Private Mortgage Insurance Insdustry;

(3) Level the Playing Field Upwards By Imposing Community Support Requirements on Non-Bank Financial Intermediaries, Including Finance Companies, Insurance Companies, Money Market Mutual Funds (MMMFs), and Securities Firms;

(4) Increase Disclosures of Lending Activity by Depository Institutions, Including Disclosures of Small Business and Consumer Credit;

(5) Increase Opportunities for Participation by the Public in the Regulatory Process;

(6) Require Regulators to Make Greater Use of CRA Performance Data in Conducting a CRA Examination, and Specify What Data Should Be Disclosed in the Publicly-Available Portion of CRA Evaluations; and

(7) Punish Violators of the CRA, Possibly Through the Imposition of Civil Money Penalties, or Through a Budget-Neutral System of Fines and Rebates.

I. The Community Reinvestment Act: History & Policy Background

The Community Reinvestment Act (CRA) was enacted in 1977 in response to widespread evidence of neighborhood "redlining" --the bank practice of denying credit to whole portions of a city based on stereotypes about the creditworthiness of people residing there.

In crafting the CRA, Congress recognized that a wide array of public benefits conferred on the banking industry mean that depository institutions have a unique responsibility to promote neighborhood economic health. Banks are publicly-chartered corporations which benefit from the public guarantee of deposit insurance, and access to the Federal Reserve's discount window. In the Bank Holding Company Act, Congress explicitly required the regulatory agencies to take into account the impact of bank mergers on the "convenience and needs" of affected communities when considering merger applications.

The Community Reinvestmnent Act, then, is best viewed as a modern elaboration of longstanding public policy principles which hold that depository institutions --because of the unique public benefits conferred on them and their special significance in promoting economic vitality-- have an obligation to meet legitimate credit needs in all the communities they serve, including low- and moderate-income neighborhoods.

And, it is important to note that the Community Reinvestment Act (CRA) was enacted as a modest and conservative alternative to the use of credit allocation techniques. In response to widespread concern in the 1960's and 1970's that the financial system was doing a poor job of meeting the needs of the productive economy, and housing for low- and moderate-income Americans, Congress considered legislation that would have required banks to lend for certain "national priority purposes," using differential reserve requirements administered by the Federal Reserve as a lever. By comparison to the more blunt instruments of credit allocation, CRA appears a remarkably market-oriented, and non-bureaucratic means of ensuring that legitimate credit needs are met by the industry.

Recent history has only underlined the case for the public mission of the industry.

A study by the Securities and Exchange Commission last year revealed that deposit insurance is significantly underpriced --with premiums between 30 and 70 basis points below estimated market rates-- and represents a massive annual subsidy to the industry amounting to nearly $20 billion. The huge contingent liability incurred by taxpayers in the form of deposit insurance has been made painfully obvious in the last decade, with bailout costs for the S&L industry expected to reach $1.4 trillion, and a $30 billion loan to recapitalize the depleted Bank Insurance Fund. There is considerable anecdotal evidence that depoitory institutions are responding to projected increases in premiums by "passing through" the costs to consumers, particularly low- and moderate-income consumers, who have the least market clout.

Thus, in view of the massive public subsidies and supports enjoyed by the industry in recent years, there is a compelling case for substantially strengthening the public obligations of depository institutions to match this increaed level of public support.

II. The CRA: An Anti-Poverty Program That Works

CRA has played a major role in the revitalization of thousands of neighborhoods around the country. In the face of declining government support for economic development in the 1980's, CRA has fostered many productive and profitable partnerships between lenders and low- and moderate-income communities that have helped bridge the gap. These partnerships have in turn resulted in the development of thousands of rental and owner-occupied units of affordable housing, the start-up of thousands of small businesses, including many minority-owned businesses, and the creation of thousands of new jobs.

And the intangible achievements are perhaps even more impressive. Many neighborhoods have been stabilized and turned around, thanks in large part to the availability of credit made possible by the CRA. And, thousands of families have been empowered to seek and to find the American dream of homeownership, while contributing to the development of the neighborhoods in which they were raised.

While much more clearly needs to be done to stem the cycle of despair that continues to plague many urban and rural communities, we should all recognize and celebrate the important progress that has been made. In our view, CRA is arguably the most successful anti-poverty program developed since the range of programs enacted as part of the "War on Poverty," precisely because it engages the ingenuity of lenders, government, and, most importantly, the energies and talents of low- and moderate-income people themselves. The partnerships among all these parties fostered by CRA are a model for grassroots community economic development that should be nourished, replicated, and supported by the Congress and the Administration alike.

We have appended testimony delivered to the House Subcommittee on Economic Stablization at a Field Hearing in Philadelphia last year, which describes in detail ACORN's community reinvestment model and the success of partnerships developed over the past decade with several area lenders. [Appendix 1] Also attached is a New York Times article which describes ACORN's community reinvestment model. [Appendix 2]

III. Continuing Problems of Credit Access in Low- and Moderate-Income and Minority Communities

Despite steady progress and impressive achievements, abundant anecdotal and statistical evidence points to massive problems of credit access in many communities around the country, and the devastating effects of redlining on the economic and social health of low- and moderate-income neighborhoods.

The widely publicized analysis of the "new" 1990 HMDA data by the Federal Reserve revealed shocking disparities in the treatment of minority and white applicants for home loans. In general, the study found, minority applicants were rejected between two and four times as often as white applicants of comparable income. And upper-income African-Americans were actually rejected more frequently than low- and moderate-income white applicants.

These results held true with only minor variations for all classes of lenders: commercial banks, thrifts, savings banks, and mortgage companies. A study of the 1990 HMDA data by the Federal Reserve Bank of Boston revealed that, while discrepancies varied somewhat from city to city, the general pattern of disparate treatment held true in every region of the country.

ACORN's own study of the 1990 HMDA, Banking on Discrimination, a study of 20 banks in 10 cities, revealed that some banks actually rejected minority applicants five, seven, or even ten times more frequently than white applicants, and further, that some institutions received shockingly few applications from minorities. For instance, only 4% of applications received by Bank of America in Oakland in 1990 were from African Americans, though African-Americans comprise over 40% of the area's population.

A subsequent ACORN study, Take the Money and Run: Deposit Siphoning from Minority Neighborhoods in 14 Cities, revealed that in all but one city examined, banks reinvest deposits taken in white communities at a far higher rate than deposits taken in minority neighborhoods. For every dollar on deposit in white communities, banks reinvested 8 cents for housing related loans, compared to only 4 cents in minority communities. In New Orleans, banks reinvested 16 cents of every dollar on deposit in white neighborhoods, compared to only one cent for every dollar on deposit in minority neighborhoods. Only in Philadelphia, where ACORN and other groups have built longstanding and successful partnerships with area lenders, was the pattern exceptional.

While the availability of credit for single-family home loans

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is clearly inadequate, credit availability for other classes of loans is far worse. Bank financing of multi-family affordable housing is minimal as a percentage of assets, and declining. An analysis of the reports of condition filed by the 10 largest banks reveals that multi-family loans --low-income or otherwise-- comprise less than 1% of the gross assets held by these institutions in any given year.

Substantial anecdotal evidence suggests that the availability of credit for minority-owned and inner-city businesses is almost non-existent, while small businesses in general are experiencing a "credit crunch". Further, anecdotal information strongly suggests that a wide range of community institutions vital to neighborhood well-being --ranging from child care facilities to mental health centers-- find it nearly impossible to secure lines of credit from lenders. Additionally, we suspect that consumer credit --ranging from credit cards to personal loans-- is difficult or impossible to obtain for creditworthy minority and low- and moderate-income persons.

Unfortunately, there is some evidence that problems of credit availability are getting worse --not better. Financial deregulation in the 1980's created powerful disincentives for community lending, while the rise of the powerful secondary market entities have further eroded the willingness of lenders to engage in portfolio lending, often a prerequisite for successful community development initiatives. And increasing banking industry concentration --together with regulatory policies like risk-based capital standards-- has furthered the standardization of loan products and the centralization of loan decision making processes. Thus, problems of credit availability are directly related to broader public policy decisions about the evolution and structure of the financial industry, and, to date, these decisions have shown remarkably little sensitivity to the impact of bank reform on community lending.

There is, in fact, a danger that we will shortly become a nation of two financial marketplaces, separate and unequal. Thanks in large part to financial deregulation, 20 million American households now have no account relationship with a bank whatsoever, according to the most recent Federal Reserve Survey of Consumer Finances, and the number has risen sharply over the past two decades. In addition, a recent study by Swarthmore economist John Caskey indicates that while the number of branches in wealthy neighborhoods doubled between 1970 and 1989, the number in low-income neighborhoods declined in absolute terms over the same period.

At the same time, unregulated, "fringe" bankers have stepped into the void left by mainstream lenders. The number of pawnbrokers nationwide has increased by 60% in the last 4 years, while lease-to-own stores, check cashing stores, and second mortgage companies have also proliferated. These lenders offer terms far less favorable than mainstream banks, sometimes charging interest rates of 200% per year for what amount to low-balance, collateralized personal loans. Unscrupulous fly-by-night second mortgage companies were the subject of exposes in several cities last year that revealed a pattern of financing by mainstream lenders themselves unwilling to engage in the inner-city market, coupled with usurious rates and terms, and vulture-like foreclosures on vulnerable homeowners.

In the broadest sense, problems of access to credit remain at the heart of the dilemmas of inner-city economic development. And while a portion of the banking industry has "gotten the religion" about CRA, and a deccade of experience with community lending has allayed fears about the risk and return associated with lending in underserved areas, such institutions remain the exception, rather than the rule.

IV. Consequences of Redlining for Community Economic Development

Historical patterns of disinvestment have set in motion a spiral of urban decline and decay that has proven difficult to reverse. Redlining has resulted in widespread abandonment, urban flight of working- and middle-class families, and the erosion of municipal tax bases. As Mayor Raymond L. Flynn of Boston has pointed out on several occassions, the availability of credit for economic development impinges directly on the ability of local governments to collect revenue, and thereby on the ability of localities to provide necessary city services.

Lack of access to credit has a "ripple" effect, impacting on the viability of whole communities. The inability of anyone in a community to get a mortgage often leads to abandonment, which in turn leads banks to shun small businesses and other borrowers in an area. The abandoned property is taken off the city's tax rolls, and frequently becomes a haven for drug abuse and crime, thereby lessening the quality of life for everyone. And the individual denied the loan is barred from accumulating assets, which could have been used to leverage other opportunities, such as starting a business, or financing an education.

And the availability of credit in underserved communities is often a controlling factor on the effectiveness of government programs. The value of housing subsidies are greatly enhanced by leveraging made possible when they are combined with private financing. And job training programs are only relevant in the context of a growing economy, led by small businesses financed by lenders.

Congressman Tom Ridge has pointed out that a neighborhood without credit is like land without rain: it quickly becomes a very barren place.

V. Enforcement of CRA by Federal Banking Agencies

The bank regulatory agencies charged with enforcing the CRA constitute the principal obstacle to a more vital and effective Community Reinvestment Act. From the Act's enactment, the agencies have refused vigorously to enforce the Act. Indeed, the regulators frequently appear to regard themselves as management consultants to the institutions that they are charged with regulating.

Perhaps the most compelling case for regulatory non-feasance in enforcement is the distribution of CRA ratings issed by the regulatory agencies since July, 1990, when ratings first became public. Despite overwhelming statistical and anecdotal information that the bulk of the industry is doing a poor job of meeting its community reinvestment obligations, 87% of all institutions rated between July, 1990 and June 30, 1992 have received "satisfactory" or better ratings.

In addition, only a handful of applications have ever been denied by any of the agencies on the grounds of poor community lending performance. Since 1988, the Federal Reserve has only rejected 2 applications, and the FDIC none, on CRA grounds. To our knowledge, the regulators have collectively used their authority to issue cease and desist orders to institutions in flagrant violation of the Act on only two occassions.

In short, then, it has become virtually impossible to fail a CRA exam, and there is no punishment for those few institutions that do poorly. And for institutions regulated by the OCC, there may be as many as <u>seven</u> years between CRA exams.

An analysis of the evaluations themselves reveals wide discrepancies in the quality of CRA exams. Some evaluations clearly involve nothing more than a cursory inspection of the bank's own claims about its performance, with little or no independent verification or contact with members of the affected community. Indeed, the majority of CRA evaluations that we have seen often include no or virtually no discussion of actual data pertaining to the distribution of loans in a given community. Often, the discussion as to the geographic distribution of credit extentions and denials is confined to a terse comment about the whether or not the bank's record is "reasonable," without any supporting documentation or analysis.

Two particular concerns about the ratings process are the relative inattention to available data in evaluating bank performance under the 12 assessment factors, and also the reluctance of the agencies to solicit imput from affected communities in the course of the supervisory process.

First, while examiners often comment on the "reasonableness" of a bank's penentration of the low- and moderate-income market, rarely is supporting statistical evidence --for example, the number of applications received, the number and dollar volume of loans originaed, and the number rejected, for various loan types-- included in the publicly available portion of the evaluations.

ACORN understands that the intent of a provision in FDICIA requiring examiners to include data in the publically-available portion of the CRA evaluation was to increase the consistency of evaluations. To our knowledge, the regulators have not responded agressively to this mandate, and have in fact backtracked from earlier policy statements urging lenders to geocode loans.

Second, examiners frequently appear to rely exclusively on bank documentation of community reinvesment initiatives, without soliciting community input during the examination process into perceptions of bank performance. ACORN has on several occassions found itself misleadingly listed in bank CRA statements, without having been contacted by an examiner to verify the alleged "partnership."

Apart from corroborating bank statements, contacts with community groups can be a vital source of information on bank performance. Many non-profit developers and community-based organizations have a excellent sense of which lenders are aggressively participating in community development initiatives, and which are not. In addition, it is hard to conceive how an examiner would come to a conclusion about the nature and extent of community credit needs without contact with residents of low- and moderate-income communities.

ACORN notes that there appears to be some discrepancy between regulatory efforts in this regard. The OTS, in response to questions posed by the Subcommittee, stated that it required examiners to make contact with community groups, while the OCC appeared to suggest that this is an exceptional practice, and is only done "if substantive CRA concerns are raised and not adequately addressed by the bank." [response to question 13.d, p 16]. We should stress that most community groups in low- and moderate-income neighborhoods are strapped for time and resources, and are unlikely to write up comments for an examiner's convenience on a lender's performance. Indeed, barring active solicitation of comments, the examiner is unlikely to get the views of low- and moderate-income residents at all.

I might add that ACORN was somewhat amused to find that one of the three principal ways the FDIC solicits public comment is through its innovative "Chamber of Commerce Program." While the views of a community's business elite are no doubt important, we must question whether such contacts provide access to diverse segments of the community which doubtless may have different perceptions of needs and performance.

CRA's greatest success has been the productive and profitable partnerships it has fostered between diverse agents --lenders and community organizations. Yet, the regulators seem to go out of their way to minimize public input. In only a handful of cases have the regulators granted public hearings on merger applications -even those "mega-mergers" that aroused widespread community alarm in 8 or 10 states. And despite the agencies' knowledge of the resource constraints of community groups --low-income organizations do not have sophisticated computers or high-priced analysts-- the regulators have rarely granted extentions of the public comment period on significant merger applications.

What positive work has been done by community groups and lenders over the years, then, has been achieved despite the efforts of the agencies, which have made themselves an obstacle to the hard work of neighborhood revitalization.

VI. Comments on Proposals to Exempt Certain Institutions from the Requirements of the CRA

The Community Reinvestment Act requires depository institutions to meet the credit needs of all the communities they are chartered to serve, including low- and moderate-income neighborhoods.

While the CRA has been the subject of a massive disinfomation campaign over the past several years, its intent and requirements are straightforward. Congress has recognized since the 1930's that banks are not like any other commercial enterprises. They are publicly chartered to meet the "convenience and needs" of their communities, and are the beneficiaries of a wide array of public benefits. Furthermore, Congress has recognized that access to credit is the lifeblood of any community --urban, suburban, or rural.

Recognizing that credit needs vary greatly between communities, Congress did not attempt to specify particular kinds or volumes of credit that would constitute compliance with the Act. Instead, the CRA was designed to engage the ingenuity of banks themselves to ascertain and meet credit needs in their communities.

CRA is also, in its way, a conservative and market-oriented law. Rather than prescribing specific kinds of credit extentions, the law requires institutions to be involved in their communities and to assist in their economic development.

In this context, the bankers' assaults on the CRA are seriously misguided. If the CRA is ever weakened or repealed, Congress will undoubtedly devise --and community groups will lobby for-- a far more elaborate system of credit allocation to meet the needs of small businessmen, farmers, and low- and moderate-income families that will make CRA seem tame indeed by comparison. And the bankers may be assured that any such alternative system would be far less market-oriented, and leave institutions with far less discretion in their lending policies, than does the CRA.

Thus, we believe that it behooves both the banking industry and the market-oriented regulators to support CRA. It was not so long ago, after all, that legislation to allocate credit and enact usury laws were seriously considered by the Congress.

Compliance Requirements

The Community Reinvestment Act has drawn considerable fire from the banking industry over the past several years, under the guise of the so-called "regulatory burden" that it imposes on insured depositories.

In our view, the focus on CRA in discussions of regulatory burden is frankly laughable. The agencies themselves admit that compliance with CRA requires minimal effort. The Office of the Comptroller of the Currency estimates that a bank can fully comply with the CRA in one hour, and the FDIC's estimate is two hours. An OMB study found that the CRA was in fact the least burdensome law on the books.

And the idea that banks are invaded by armies of regulators at examination time is equally farcical. According to figures provided by Glenn Loney, examiners spent only 24 hours on average actually inside an institution regulated by the Federal Reserve when conducting a CRA exam in 1990.

The requirements for compliance with CRA are indeed minimal. CRA requires an institution to:

--post a notice in the lobby of each branch;

--maintain a public comment file; and

--prepare and update a statement that includes a map defining its local community and describes the types of credit it is prepared to extend in the community.

Let me stress that, according to the law and the regulations, any other documentation is optional, including the preparation of an expanded CRA statement.

Some institutions do in fact produce far more documentation to demonstrate compliance, but in our view, this is often a way of evading rather than complying with the law. CRA is not about documenting charitable activities, nor should it be about slick brochures with minority families on the cover.

Indeed, consumers should not have to pay for the printing costs for bank brochures --brochures that are printed to avoid having to make loans.

Part of the problem is generated by the various "consultants" to the industry who have generated thousands of pages in the form of compliance guides, the sum of whose advice to bankers is to deluge examiners with more paperwork than they would ever hope to corroborate independently. Organizations like Barefoot & Associates, and the bank trade groups, have done more damage to the compliance process than any individual bank or community group could ever do.

CRA was designed to make community lending an integral feature of the overall business strategy of depository institutions, rather than a "special program" that is peripheral to the main business of banks. In our view, the regulators and the consultants have encouraged the "ghettoization" of community lending by focussing on the development of elaborate internal procedures and processes, rather than actual performance.

Comments on Certain Proposals to Exempt Small Banks from CRA

In our view, CRA is best viewed as part of the charter obligation on all depository institutions to meet the "convenience and needs" of the communities they are chartered to serve. Thus, we would only be prepared to support proposals to exempt small institutions from CRA if these same institutions were required to turn in their charters, give up taxpayer-backed deposit insurance, and denied access to the Federal Reserve's discount window. If the banks are so concerned about regulation, we should seriously consider stripping away the institutional support of the industry, and let them compete in a truly free market.

In our view, the public purposes of the industry arise from implicit taxpayer support of the industry, and this support is not related to the asset size of depository institutions.

One of the principal objections that some small banks make to CRA is that they do not have the capacity to perform community development activities --or to document their efforts-- that their larger counterparts possess.

Contrary to myth, the agencies have long recognized this reality. Assetment Factor K under the CRA requires the regulator to assess "the institution's ability to meet various community credit needs based on its financial condition and size, legal impediments, local economic conditions and other factors." And the examiners simply do not expect the same things from small institutions that they do from large ones. To cite but one example of the different expectations, examiners may expect a large institution to have conducted some form of computerized analysis of the geographic distribution of its loans, but only expect that a small institution will perform a rough analysis with a map and push pins.

And examiners do in fact spend far less time examining small banks than large banks. The Fed reported spending more than 10 times as many hours on average examining banks with assets of greater than $1 billion as banks with assets of less than $25 million (223 hours versus 22 hours). Indeed, all the regulators devote far more hours to each compliance exam for larger institutions than for smaller ones.

One of the principal myths being circulated by the trade groups and certain sectors of the industry is that small banks already serve their communities, and that they therefore deserve some sort of exemption from or merit lesser requirements under the CRA than their larger peers.

In our view, this is an altogether fallacious contention, for several reasons:

(1) According to figures supplied by bank analyst Ken Thomas, 88% of the lowest possible CRA ratings issued since 1990 have been to banks with assets of less than $100 million, while such institutions comprise only 77% of the industry.

(2) The loan-to-deposit ratios of the nation's smallest banks are substantially below those of their largest peers, ranging from an average of 63% for institutions with assets of greater that $10 billion to 55% for banks with assets of less than $100 million, according to a recent House Banking Committee Report, "Analysis of Banking Industry Consolidation Issues." Indeed, the primary business of many small banks -particularly in recent years-- has been to purchase government securities.

(3) Even those small banks that extend credit solely within their community --or a bank with a loan-to-deposit ratio of 100%-- may "redline" predominantly minority or low- and moderate-income neighborhoods. There is no reason to expect that smaller institutions would --purely as a result of their asset size-- be any more or less likely to meet the credit needs of low- and moderate-income areas within their service area. The fact that the ownership of a bank may be local does not imply that decision makers run in social circle wider than the local Rotary Club or country club. In fact, owners and managers of small institutions are likely to come into contact mostly with the business elite of the city and town, and many be utterly unfamiliar with credit needs in the low-income, minority areas.

<u>Comments on Certain Proposals to Exempt Institutions Serving Rural Areas from CRA</u>

While the nature of credit needs in rural and urban areas may differ significantly, proposals to exempt institutions from the CRA on the basis of the size of the communities they serve are likely to exacerbate the problems of population loss, unemployment, and a lack of suitable and affordable housing that plague many rural communities. There are several reasons why exempting rural institutions would be poor public policy:

(1) The agencies have at least formally recognized the different nature of credit needs in rural communities. An article by James Pilkington, an FDIC official, has written a good guide to compliance with CRA for rural institutions, which is sensitive to the relative lack of community development initiatives and community groups in rural areas. There may be individual instances where examiners have applied an "urban" CRA model to rural communities, but this is the result of poor supervision and training, and does not warrant wholesale exemptions from the statutory requirements of CRA.

(2) Community reinvestment may take on added significance in rural areas because in many rural communities, the banking market is dominated by a handful of small institutions. The refusal of a single bank to extend credit, therefore, has even more devastating consequences than in a large metropolitan area, where consumers of credit have more options. The farm crisis in the midewest in the early 1980's was precipitated in part by the monopoly of area institutions who kept their deposit windows up, but shut their loan windows down.

(3) In addition, problems of rural poverty are frequently as severe --if not as visible-- as in urban areas. There is a desperate need in many parts of rural America for affordable housing --both single- and multi-family-- and a need for the development of job-creating enterprises to help stabilize withering communities. The "hidden" nature of rural poverty increases the need for local bankers to visit the local trailer park or drive down the back roads. And the lack of community organizations in many areas only accentuates the need for the regulatory agencies to act as a watchdog over banking practices.

(4) While some rural communities may be relatively homogenous, most are not. Rural communities in the south and elsewhere have substantial minority populations which have historically had great difficulty in obtaining credit. In addition, Indian Reservations in the plains states and the southwest are sometimes excluded from a rural bank's delineation of its community, or denied credit altogether. There is, then, a very tangible counterpart to the problem of urban redlining in rural areas. On of the very few denials of merger applications by the Federal Reserve in recent years on CRA grounds came in the case of an application last year by a Montana institution that had excluded an Indian Reservation from its lending area.

<u>Comments on Certain Proposals to Give Certain Institutions a "Safe Harbor" from CRA Challenges</u>

Of all the proposals to make statutory changes to CRA, proposals to give banks a "safe harbor" from CRA challenges are by far the most bizarre and the least meritorious. There are several reasons why this proposal for regulatory forbearance should by rejected by the Congress out of hand:

(1) CRA ratings are an unreliable indicator of bank performance. As has been argued earlier, examiners tend to give institutions vastly inflated ratings, which frequently correspond to neither the institution's record of making loans, nor to widely held community perceptions. The outrage in California and elsewhere about Bank of America's receipt of an "outstanding" CRA rating, which allowed it to successfully complete a merger with Security Pacific, revealed how disparate community and regulatory perceptions may be.

(2) Banks effectively experience a policy of regulatory forbearance already. The agencies have denied applications on CRA grounds on only a handful of occassions. Since 1988, the Federal Reserve has only rejected two applications on CRA grounds, while 109 applications were protested by community groups or others. And, the agencies have <u>never</u> denied an application for an institution with an outstanding CRA rating. The "regulatory burden" here is not on banks --which get a free ride-- but on the public, which has virtually no influence over the regulatory process.

(3) The performance of institutions may change over time, and an institution may have improved or worsened its record since its last examination. There is often a substantial lag time between CRA exams, as much as 7 years in the case of national banks examined by the OCC. Thus, the recent record of a bank seeking approval of a merger application may not be accurately reflected in its last exam. Public comment is acknowledged by the regulators to be a valuable additional source of information to supplement a dated or faulty CRA evaluation.

(4) Only a handful of merger applications are ever protested by community groups or others. The Federal Reserve --which reviews applications for mergers involving Bank Holding Companie-- reported, for example, that of 6335 applications received between 1988 and 1992, only 109, or 1.7%, were protested on CRA grounds.

(5) Public comments on merger applications impose no significant delays on merger applications. Data supplied by the Federal Reserve indicates that it takes 75 days on average to process a non-challenged application, compared to 73 days for a challenged applications. If anything, this underscores the problem of regulatory inattention to community input.

<u>Why All the Fuss Over CRA?</u>

If CRA in fact poses an extremely minimal burden on insured depository institutions, the question naturally arises why the bankers are so intent on crafting various exemptions, or scrapping the law altogether.

There are several reasons, but by far the most important is the requirement that banks disclose their CRA ratings to the public, enacted as part of FIRREA. Prior to public disclosure, most banks had little to fear from CRA, unless they were about to file an application to merge or expand. This was especially true of the smaller institutions, which rarely if ever have applications pending.

Now, however, all depositors, large or small, may place their money based on the CRA performance of a lender. So, while banks have little to fear from the regulators, they have a great deal to fear from the market.

Few bankers will publicly admit that what they fear most is adverse publicity or depositor selection based on CRA performance. However, it is interesting to note that many banks with high ratings are actually publicizing their performance to attract depositors. A recent guide to CRA published by the American Bankers Association noted that: "if your rating is high, your bank's reputation is enhanced in the local market area. As such a high rating may be a useful marketing tool . . . By the same token, a low rating can be detrimental to your bank's image and can hurt business as a result."

Indeed, CRA ratings provide bank customers with another source of information that may be used to make market choices, depending on the inclinations and preferences of individuals. The increasing sensitivity of depository institutions to this kind of market scrutiny is, in our view, a healthy development.

Another reason for hightened attention to CRA among bankers is that the whole evaluation process has been overhauled since the passage of FIRREA. Consequently, many bankers' unfamiliarity with the new process has led them to panic. We suspect that once all institutions have experienced one examination, some of the anxiety with the new procedures will lessen.

Finally, we would point out that just as the loudest special pleaders for industry deregulation are the weakest and least well-capitalized banks, so too the most active banks in this debate are frequently those that have never reconciled themselves to CRA. Our experience with banks across the country suggests that there is a "Silent Majority" of institutions that have learned to live with the law, and a sizable minority who are enthusiastic boosters of CRA as good business practice. The trade groups, unfortunately, are representing the views of the most shrill and ideological fringe of the banking community.

VII. Recommendations for Reform

While ACORN believes that many of the reforms that are needed must take place at the regulatory and supervisory level, there are several steps Congress can take to increase the flow of capital to underserved communities nationwide.

(1) Significantly Strengthen Community Lending Requirements as a Condition of New Bank Powers

We have argued repeatedly that trends in community reinvestment are influenced greatly by broader structural changes in the industry, and public policy decisions about these issues. Yet Congress has persisted in contemplating broad reforms of the industry -- including interstate branching, repeal of Glass-Steagall, etc.-- without serious consideration of the impact of such changes on the availability of credit in low- and moderate-income neighborhoods.

In particular, interstate branching raises grave concerns about increasing economic concentration, standardization of loan products and centralization of loan decision making processes. While ACORN remains opposed to interstate branching, we strongly urge the Congress to consider modernizing community reinvestment laws if branching legislation is contemplated. In particular, we suggest that Congress require regulators to:

·demonstrate that applicant banks have not engaged in a pattern or practice of branch openings or closings that has the effect of excluding low- or moderate-income or minority communities before approving an application. ACORN has been concerned for several years that many banks are attempting to avoid their community lending obligations by closing or refusing to open branches in underserved areas. And interstate branching offers ominous opportunities for banks to selectively purchase or "cherry pick" branch networks in wealthy communities, while closing branches in poor communities.

·collect more information about deposit-taking and loan origination activity on a state-by-state basis, for a variety of loan types, to allow monitoring of deposit flows, and identify cases of deposit siphoning. Because call report data is currently collected for each bank susbidary, interstate branching will entail a massive loss of data as Bank Holding Companies with several subsidiaries convert to single institutions.

(2) Expand Community Support Requirements to Other Players in the Mortgage Lending Chain

Depository institutions have long argued that other players in the mortgage lending chain play some part in the phenomenon of mortgage discrimination. We agree, and believe that all these players must be brought under effective federal regulation. We recommend that the Congress:

·Enact the Government Sponsored Enterprises legislation before the end of this session, which would dramatically increase the commitment of Fannie Mae and Freddie Mac to affordable housing;

·Subject Private Mortgage Insurance (PMI) companies to HMDA, and require them to affirmatively market and write policies in underserved communities

·Tighten regulation of the appraisal industry to address the problem of "low-balling."

·Require HUD to develop a process for recertifying mortgage banks that are FHA lenders, to ensure that mortgage bankers are not "creaming" the high end of the market (a problem which is exacerbated by increases in the FHA loan limits). Such a "community support recertification" process would require HUD to ensure that individual mortgage companies are not discriminating, and are meeting the housing credit needs of all the neighborhoods --including low- and moderate-income neighborhoods-- in metropolitan areas where they originate a significant volume of mortgages. The process should allow for public comment and public hearings on the community support performance of mortgage banks applying for recertification. FHA is a federal program which confers substantial benefits to mortgage companies, and Congress can reasonably expect mortgage companies to support the needs of low- and moderate-income households.

(3) Level the Playing Field Upwards By Imposing Community Support Requirements on Non-Bank Financial Intermediaries

Depository institutions have long complained that regulation of the industry places them at a competitive disadvantage as regards other financial intermediaries. We agree, but firmly believe that the playing field should be levelled up, to impose community support and disclosure requirements on non-bank intermediaries, rather than levelled down, to reduce the existing obligations on depository institutions.

While there are a variety of mechanisms that might be employed, financial intermediaries that could be subject to federal community support requirements include: insurance companies, money market mutual funds, securities firms, and finance companies (e.g., GMAC, GE Capital).

(4) Increase Disclosures of Lending Activity by Depository Institutions

Given the poor performance of the bank regulatory agencies at enforcing CRA, the strongest tool available for increasing community lending has historically been the disclosure of loan originations on a census tract basis. Such disclosures allow lenders, government, and community groups to identify weaknesses in bank performance, and to identify underserved markets.

HMDA has been a remarkably powerful tool. The release of the 1990 data unleashed a wave of industry task forces, individual bank initiatives, and the like to stem the tide of bad publicity associated with revelations of disparities in mortgage lending.

We beleive that Congress should increase the scope of loan disclosures, including:

•Amending HMDA to include data on the number and dollar volume of loans originated to small businesses on a geographic basis;

•Requiring lenders to report marketing and origination of consumer credit products on a zip code basis.

In addition, it appears that the FFIEC is likely to subvert Congressional intent in FDICIA by refusing to collect data on loans to minority-owned small businesses in reports of condition. If this occurs, we urge Congress to amend the provisions to require collection of such data.

(5) Increase Opportunities for Participation by the Public in the Regulatory Process

Congress should require examiners to solicit public input during the examination of individual institutions, and especially to meet with leaders and representatives of low- and moderate-income and minority groups. Such meetings could be used to identify credit needs, verify bank statements, and gather information about the public perceptions of bank performance.

In addition, we believe that there is a vital need for "watchdogs" in the regulatory apparatus to monitor compliance and enforcement activities, and strongly suggest increased requirements for representation of low- and moderate-income and minority persons in decision making positions within the agencies.

(6) Require Regulators to Make Greater Use of CRA Performance Data in Conducting a CRA Examination

While the FFIEC has expended considerable energy unearthing the significance of Section 221 of FDICIA, which requires a study of regulatory burdens on the industry, we have noticed no comparable buzz of activity around Section 222, which requires the inclusion of data on the performance of insured depositories in the publicly available portions of CRA evaluations.

This provision was included in FDICIA to require the inclusion of data, where applicable, for each of the 12 assessment factors under CRA. The intent was to rationalize and standardize the evaluation process across agencies.

Our review of dozens of CRA evaluations reveals wide discrepanices in the quality and content of examiners' reports. Some exams are pro forma, and clearly involve little work by the examiner in independently corroborating a bank's statements, and frequently appear to involve little or no analysis of HMDA data.

Inclusion of actual lending data in evaluations would have two principal advantages. First, it would discourage depository institutions from collecting endless documentation about irrelevant activities. Second, it will result in a more standardized and fair system of assigning CRA ratings.

While we would not support establishing a fixed threshold or numerical test, we do believe that requiring examiners to include actual data on the geographic distribution of loan originations and denials would ensure a greater consistency in the process.

ACORN believes that the regulators are unlikely to enforce Section 222 of FDICIA, and therefore suggest that Congress specify in statute the exact nature of the data that must be included in the public portions of CRA evaluations. This would pose no additional burden on depository institutions, but would require regulators to justify their conclusions under each of the assessment factors, and perhaps give lenders more guidance as well.

We should note that while the banking trade groups often claim to desire more emphasis by regulators on performance, these same trade groups lobbied vigorously against an amendment offered by Rep. Richard Neal last year to FDICIA that would have required regulators to include a specific number of data elements in their evaluations (the number and dollar volume of small business and home mortgage loans originated, on a census tract basis, for example).

(7) Punish Violators of the CRA

The regulators have rarely exercised their authority to issue cease and desist orders to recalcitrant poor performers under CRA. There is a sizable portion of the industry that has not even paid lip service to compliance. We believe that it may be necessary to impose civil and monetary penalties on poor performers, or to

institute a budget neutral system which rewards banks in compliance and penalizes institutions with poor records.

Conclusion

In our view, it is frankly astounding that given the massive levels of taxpayer support of the banking industry in recent years, the trade groups have the nerve to pursue an agenda of further deregulation in general, and weakening CRA in particular. To put the matter rather starkly, if "workfare" is appropriate for families on AFDC, workfare is equally appropriate for the banking industry, whose tenure on the public dole will be of far greater cost to the taxpayers.

We are also somewhat discouraged by a never-ending cycle of neglect that seems to characterize public policy with regard to issues of poverty. The events on Los Angeles focussed the attention of the country on the hard realities of life for millions of Americans. We believe there is broad public support for an aggressive and activist response to the urban crisis, and are frustrated by the lack of a coherent Congressional response.

The issues with regard to CRA are stark and simple. CRA is a success story of anti-poverty policy, but has been undermined at every step by regulatory agencies that have seemingly been captured by the institutions they are charged with supervising. The question at this juncture, it seems to us, is not one of fine tuning, but whether the political will exists to respond to a dramatic crisis with significant reform in a timely fashion. We urge the Congress to reject the entreaties of the special interests, and to get about the business of supporting neighborhood revitalization.

These hearings are an excellent first step toward that end.

Testimony
Submitted by

George Butts
President
ACORN Housing Corporation
Philadelphia, PA

on

Mortgage Credit Access in Philadelphia
and
Community Lending Strategies

to

Subcommittee on Economic Stabilization
of the
Committee on Banking, Finance and Urban Affairs
U.S. House of Representatives

The Honorable Thomas Carper
Chairman

April 24, 1992

Mr. Chairman, Members of the Subcommittee, I am George Butts, President of the ACORN Housing Corporation of Philadelphia, PA. ACORN sincerely appreciates the opportunity to testify today at this hearing on economic conditions in the greater Philadelphia area, and I am particularly grateful that you, Mr. Chairman, have chosen to hold this hearing in my own community of North Philadelphia. There is nothing like getting a first hand view of the challenges that face us here in Philadelphia.

This hearing is an important step in identifying how the federal government can better assist local communities, like North Philadelphia, in developing, promoting and sustaining successful strategies of economic development and revitalization. Healthy regional economies are built not only on a foundation of local community stability and economic opportunity, but equally on the active support of the federal government as a financial and economic partner.

Today I have four principle recommendations:

1) more rigorous federal enforcement of laws designed to ensure equal access to credit, irrespective of a borrower's race, religion, sex, ethnic origin or the location of their residence or business;

2) removal of federal disincentives --and creation of positive incentives-- to spur capital investment in distressed communities;

3) effective regulation of non-lender participants in the extension of mortgage credit, including the private mortgage insurance industry, the appraisal industry, and the secondary mortgage market, to remove barriers in the initiation of local partnerships to revitalize neighborhoods; and

4) a substantially increased federal commitment to assist non-profit loan counseling directed at low- and moderate-income homebuyers.

ACORN

ACORN, the Association of Community Organizations for Reform Now, is the country's largest grassroots organization of low- and moderate-income people. Founded by a group of welfare mothers in Arkansas in 1970 in pursuit of social justice, ACORN has grown to spawn over 400 neighborhood chapters in 35 cities and 26 states across the nation. Here in Philadelphia, we have a half-dozen neighborhood chapters located in the southwest and northern parts of the city. ACORN members work on a broad range of issues that affect their everyday quality of life, including affordable housing, neighborhood safety, unemployment, and environmental degredation.

For well over a decade, though, ACORN has been at the forefront of community-based efforts to ensure that low- and moderate-income neighborhoods obtain life sustaining credit from private federally-chartered banks and savings and loan associations. These efforts have led to over 30 agreements with private lenders that have resulted in commitments for billions of dollars in loans to underserved and historically redlined communities from Philadelphia to Phoenix and from St. Paul to Dallas.

Introduction: Capital Investment in the Inner City

The story of urban decline is the story of capital disinvestment, public and private.

In communities like this in North Philadelphia, it is evident that capital of any kind is --and has been, for many years-- in short supply. There is scarcely any private capital investment to foster micro-business development or assist existing business in expansion. Lenders --mortgage bankers, savings and loans and commercial banks-- are reluctant to extend mortgage credit and, then, only after prolonged prodding by community organizations like ACORN.

Frankly, Mr. Chairman, the federal government must also share in the blame for what has transpired in our communities. Public capital support for community revitalization has virtually evaporated. The effects of draconian cuts in support for affordable housing are now being felt in increased abandonment and homelessness. Empowerment is a noble idea, put into practice by ACORN members everyday in their neighborhoods, but it is immoral for the government to preach empowerment while slashing support to communities and families in need.

And, while community groups have grave reservations about the manner in which some Community Development Block Grant (CDBG) monies have been spent by local governments over the years, the reduction in federal funding of CDBG has eroded the quality of life in this community. Many of our streets are best described as potholes separated by patches of pavement. Curbs are crumbling. Street lights go unlit. And, children can no longer play in safe city parks.

The results of public and private disinvestment from urban areas over the past decade have been devastating. Our youth are unemployed, our businesses are stunted and our homes are in disrepair. Any serious strategy for neighborhood revitalization must feature measures to increase <u>both</u> public and private capital investment in our neighborhoods.

Redlining and Urban Decline

Philadelphia currently has more than 21,000 abandoned houses. At the same time, the city has tens of thousands of families living in overcrowded and substandard housing. The roots of this contradiction lie in the practice of "redlining" --literally the practice whereby bankers draw bold red lines around certain parts of a city map, and refuse to lend to anyone living there.

What are the consequences of redlining? Lack of access to credit from local lenders sets in motion a tragic cycle of decline --as you can see around us today-- that is difficult to turn around. But, it can be turned around --block by block and neighborhood by neighborhood-- if lenders, community groups, and government are willing to do their part.

Access to credit is the lifeblood of any community --urban, suburban, or rural. Conversely, the denial of credit to whole neighborhoods and classes of persons fosters unemployment, poverty, and economic decline.

Without access to credit, families cannot maintain their homes, and new families cannot purchase homes. "Redlining" is perhaps the principle cause of urban flight in America, and has materially contributed to the erosion of municipal tax bases. It is not uncommon for working-class families to try to buy a home to contribute to the development of their neighborhoods, only to be denied a loan, and forced to leave the neighborhood in which they were raised.

Urban flight, in turn, has eroded the tax bases of municipalities, leaving them less well equipped to provide the basic services necessary for community economic development.

In addition, access to credit is ultimately a question of access to jobs in inner-city neighborhoods. When job-creating mortgage and small business loans are not available, local youth are condemned to the welfare rolls, placing further strains on all levels of government.

ACORN Banking Model

The good message is that it is possible to turn neighborhoods around block by block. Working with the Community Reinvestment Act (CRA), we have developed successful and innovative strategies to stem urban decline, foster low-income homeownership and help banks meet their obligations to communities where they draw deposits.

The innovative and successful programs we have developed here in Philadelphia would not have been possible without the CRA. Over its 15 year history the CRA has fostered creative partnerships between lenders and community-based organizations to assist financial institutions in tapping underserved banking markets, to promote low-income homeownership and affordable rental opportunities and to pump stabilizing and desperately needed capital into communities like North Philadelphia.

These success stories have not been created over night. It has been a painstaking process with often reluctant and entrenched bank management. The willingness of lenders to tool up and make the internal bank commitment to meeting credit demand in underserved communities is dependent on senior bank management acknowledging first that communities like North Philadelphia are legitimate banking markets. It is ironic that a most conservative, market oriented law, the CRA, has been called by so many other names by banking trade associations in Washington.

Perhaps the single greatest obstacle to promoting community reinvestment are the pernicous myths and stereotypes about low- and moderate-income and minority families maintained by bankers and policy makers alike. First, low-income people are not dead beats, but rather an underserved market. Our experience here and around the country has conclusively demonstrated that families earning between $12,000 and $25,000 per year can indeed own their own home, pay their bills on time and thus provide profit making opportunities for lenders.

Second, lending to low- and moderate-income people is actually less --not more-- risky than lending to upper-income, suburban families. Data supplied by the Private Mortgage Insurance industry shows that low-balance mortgages --generally held by low- or moderate-income families-- are actually less risky than high-balance mortgages --generally held by higher-income families. (See Appendix A). When you think about it, this fact should come as no surprise. For low-income families, homes are not investments. They are the principle place of residence for low-income people, and, in many neighborhoods, a home is the only asset that can be used to leverage future wealth, educational opportunities, and employment.

Lastly, there is nothing charitable about CRA lending. It is good business for bankers as well as communities. While short-run returns may be slightly less, the long-term returns are tremendous. Mortgage lending in inner-city areas improves the "bankability" and business viability of whole neighborhoods, thus expanding opportunities and markets. And, let's keep in mind that no bank to date has ever gone broke because it helped too many low-income families aquire homes.

ACORN's Three Point Program for Community Reinvestment

Philadelphia ACORN has pioneered a three-part model for community reinvestment that has since been replicated across the country, and is now up in running St. Louis, MO, Pheonix, AZ, Dallas, TX, Washington, DC, Chicago, IL, Brooklyn, NY, Minneapolis/St. Paul, MN, and Des Moines, IA.

(1) Underwriting reform

Bank commitments and promises to do better will have little impact if an institution offers only mortgage products that are suited to suburban markets, not to an inner-city mortgage market characterized not by new tract homes but existing and aging housing stock. To do business in our neighborhoods, a lender must have suitable products to sell.

Keep in mind that most bankers are from suburban and affluent communities, and that their only contact with our neighborhoods may be driving by on the way to work. Consequently, the products offered by lenders often reveal a strong bias to suburban, affluent families, and the criteria employed are not good measures of creditworthiness in the inner-city context.

Underwriting reforms that are critical include: lower downpayment requirments; non-borrower source for closing costs; admission of food stamps toward income calculations; recognition of non-traditional markers of credit history; demonstration of income continuity, not job continuity; and, sweat equity contributions by borrowers.

Abandonment

Here in Philadelphia, a critical underwriting reform focuses on relaxation in what is commonly known as the "abandonment rule." In fact, one of the greatest shortcomings of the Deleware Valley Mortgage Plan --a bank constorium effort of area lenders-- is its continued subscription to a prohibition on granting credit to applicants who seek to finance a home on a residential block with more than 10% abandonment. This rule essentailly institutionalizes a practice of neighborhood credit denial --or, redlining.

In block after block and in neighborhood after neighborhood in North Philidelphia, abandonment rates exceed these arbitrary levels. There are countless blocks with a half dozen, 8 or even 10 abandoned homes in which a stable demand exists for housing by low-income city residents. While, admittedly, these blocks may not be on the top of the list of a suburban homeowner, they are prime real estate for low-income families who view these neighborhoods as desirable communities and abandomed homes as desirable starter homes.

Appraisals

"Low-balled" appraisals, or understated valuations of property, have prevented thousands of low-income families from obtaining credit in North Philadelphia. Many lenders will not make loans with a Loan-To-Value ratio of greater than 90% or 95%. So, a low-balled appriasal, by underestimating the value of the property, limits the ability of the borrower to get the necessary financing.

Accurate, property-specific appraisals that take into account the condition of a home and its resale value in the context of a viable local market is a necessary component of mortgage credit access in our communities. Appraisal assessments must reflect market value --not the bias of suburban real estate perspectives and prejudice. An accurate property specific-appraisal will ensure that a bank is able to recoup its investment should default occur without the imposition of income and racially discriminatory 'neighborhood factors' too often employed by the appraisal industry.

Income continuity

Low-income people are far more likely to change jobs than are high-income people, because of the seasonal or temporary nature of many low-wage jobs, or because for individuals making close to minimum wage, the prospect of a marginal increase in pay will cause them to shift jobs.

Yet, most lenders require people to have between two and five years at the same job to qualify for a loan. We have seen many cases though our loan counseling operations where a person has been turned down for credit because they changed jobs frequently, even though they have always maintained a steady stream of income, which may have actually increased over time.

We insist that lenders measure income continuity --and not job continuity-- in mortgage products targeted at inner-city communities.

Credit History

When the Federal Reserve released the HMDA data last year, which showed a shocking record of discrimination in the banking industry, we were outraged that the first response of both the banking trade groups and the Fed itself was not to work constructively for solutions, but to allege through wild speculations on human nature that minorities are less creditworthy than Americans in general.

That is a pernicious and even racist sterotype with no basis in fact. There is no statistical evidence to support the claim that minorities are less creditworthy than other borrowers. Once again, the resort to such explanations reveals a great deal about the prejudices that continue to bedevil bankers and regulators.

However, it is true that minorities often have no credit history, or lack traditionally recognized markers of credit history. In many ACORN neighborhoods, there are simply no bank branches, and everyone does their banking business with predatory check cashing stores or pawnshops who do not report to credit bureaus. And, while credit-card issuers market credit cards to students and upscale communities, you will rarely receive such a solicitation if your mailbox is in a minority neighborhood. To put this another way, the historical pattern of redlining has ensured a lack of developed credit histories in minority neighborhoods.

So, the lenders that we work with here in Philadelphia use a borrower's rent and utility payment history as a proxy for the conventional credit history. In our neighborhoods, this has proven a far better measure of creditworthiness than the traditional credit report. If hardworking, poor families have paid their bills on time for many years, this is a greater accomplishment than it is for upscale consumers with plentiful resources, and banks simply must come to grips with the fact. And, while it is fashionable to bash poor people in Congress these days, the fact is that most of us work hard, support families, and we pay our bills on time every month.

Food Stamps

Many low-income households get by by combining a wide variety of income sources, including food stamps, unemployment, or even public assistance. Given the extensive unemployment in our neighborhoods, this should come as no surprise.

Yet many lenders refuse to accept non-traditional sources of income in calculating a borrower's household income. We have gotten many lenders to include food stamps, and there is no evidence that this increases the riskiness of a loan portfolio.

(2) Community-based marketing and outreach

The second important element of a community lending program is the establishment of community-based marketing and outreach. Here we are talking about something more than the occasional advertisement in a community newspaper or the slick brochure with the minority family on the cover that collects dust in the branch office, both of which we have found not to be effective tools for lenders in tapping mortgage demand in underserved markets.

Rather, we have found that lenders must establish on-going relationships with community-based institutions like community organizations to carry out grassroots marketing and outreach programs.

Most low-income and minority consumers have a deep-seated distrust of the banking industry, or at the least very little familiarity with it since there are far more pawnshops in our neighborhoods than there are bank branches. In addition, there is a wide culture chasm between bankers and low-income and minority families. Coming from different worlds, the minority consumer and the bank official do not understand or trust each other easily.

Community-based organizations are the necessary intermediaries in this process, and can breach the chasm of distrust and apathy that separates our neighborhoods from bankers. A low-income family is far more comfortable coming to the ACORN office to hear about how to get a loan, than to a bank branch, where they feel unwelcome.

ACORN actively promotes the opportunities and benefits of homeownership in our neighborhoods. When we have worked out a solid loan product with local lenders that will work in our neighborhoods, we use a wide array of techniques to cultivate the low-income market, including--

--community meetings in low-income neighborhoods, held at schools or churches;

--homebuyer shows in low-income neighborhoods, which assist real estate agents to market property to low-income families;

--bank fairs where a dozen area banks have booths and materials describing their services to thousands of low-income families, and where low-income families can go to credit counseling and homeowner counseling workshops.

(3) Loan Counseling

Community organizations speak the language of low-income families, because we are led by and comprised of neighborhood residents, and are actively involved with other local institutions, such as churches and schools. We are less intimidating to applicants who do not have positive images of the banker from the other side of town who has historically redlined their neighborhoods. We are, therefore, in a position to bridge the gap, and to improve the quality of loan applications delivered to banks while assisting low-income families in realizing their dreams of homeownership.

Our loan counseling operations here and in 12 other cities pre-screen applicants for banks with whom we have CRA agreements. We look at the income, indebtedness, and credit of applicants, determine whether they can realistically hope to own a home in the short term, and assist them in putting together an application. Some would-be borrowers need to clear up minor credit blemishes. Others may need to accumulate more savings for a downpayment. Whatever the individual case, we lay out a map for low-income families to own their own home on a time frame that is realistic for them and is prudent for our lenders.

We reduce banks' costs of doing business by pre-screening applicants, and reduce their rejections of minorities by helping applicants meet necessary requirements. After many years, the lenders we work with here in Philadelphia understand that low-income lending is good business, not charity.

In sum, our program model is based on establishing long-term partnerships between community-based organizations and lenders.

Banks can't do it on their own and we don't have access to the capital without banks. And, the performance of loan portfolios of banks we work with shows that prudently underwriten loans in the inner-city can and do perform well, in many cases better than standard suburban mortgages.

It would be nice if what is being accomplished here in Philadelphia could be observed elsewhere in the country. Unfortunately, responsible and creative bankers are few and far between. Even here in Philadelphia, far more can and should be done. But, we have a model here that is slowly being replicated across the country.

Many have objected to the ongoing conflict between minority communities and lenders. We are here to tell you that --given the intransigence and prejudice that pervades most of the industry-- that conflict is necessary and inevitable. What we must ensure, however, is that that conflict results in lasting, and mutually beneficial partnerships, as it has done here in Philadelphia.

Recommendations

ACORN recomends a number of federal initiatives that could assist in the development of partnerships like those I have described today. These recommendations are modest and are directed at maximizing resources of the public and private sectors to fostering economic development and opportunity.

(1) Enhanced Enforcement of Fair Lending Law.

The modest success we have had here in Philadelphia has been dependent on the legal handles we have in the Fair Housing Act, the Equal Credit Opportunity Act and the Community Reinvestment Act. For the most part, these laws have been unenforced by federal regulators. To the extent they have been enforced, it has been by community organizations and other members of the public. We would like to spend our scarce time and resources on helping banks do business in our communities, not enforcing laws the Congress has directed the administrative branch to implement.

Greater oversight and sympathy for enhanced enforcement of fair lending laws in the Congress will send clear signal to both bureacrats and the industry that fair lending is the law of land. Bank regulators and the Department of Justice must be more aggressive in eradicating clear violations of fair lending law. Few violations of fair lending law are ever referred to DOJ and even fewer are acted upon. The consequence of lax enforcement is here for you to see today.

(2) Promote Incentives for Community Lending

Federal banking policy must be made more consistent and rational. Banks receive a contradictory set of directives from federal regulators. Through the CRA, they are told meet the banking needs of their entire community, on the one hand, and, on the other, they are told to hold significantly higher reserves against mortgage loans than over non-loan security investments. This crazy-quilt patchwork of inconsistent regulation hampers community lending like we have outlined today. Reforming risk-based capital requirments to remove unnecessary barriers to mortgage capital provision is an agenda ACORN shares with the banking industry.

On the other hand, efforts like Congressman Ridge's Bank Enterprise Act, which will provide financial incentives to lenders who engage in community banking efforts, are equally important. However, the structure of incentives must be carefully crafted to ensure both efficiency and the fostering of the very partnerships we have described today. It is a bank's long-term engagement with the community that is the key to success. Additionally, such incentives should not be seen as a substitute for adequate enforcement of existing fair lending law. The proper balance will include a little carrot and a little stick.

(3) Regulating Other Players in the Mortgage Market

Secondary Mortgage Market

Fannie Mae and Freddie Mac continue to present major obstacles to community lending. At this point, we daresay that banks are being held back in their efforts to do business in our neighborhoods by the policies of these federally-chartered corporations.

I would point out that the Fed's analysis of HMDA data shows that while abysmal, the banking industry is making more mortgages to low-income and minority consumers than Fannie and Freddie are willing to buy. As a consequence, lenders must portfolio their CRA loans, and eventually they come up against a liquidity problem. If banks and communuity groups can make community lending happen, the least that we can expect from federal agencies, that receive billions of dollars of annual taxpayer subsidy, is that they get out the way, and let us do it.

The Congress must ensure that these taxpayer subsidized institutions are channeling public resources to assist local lenders, not stifle their efforts to help communities like North Philadelphia. The affordable housing requirements contained in the GSE legislation pending in Congress are a first step, but more needs to be done in this area.

Appraisal and PMI Industries

Similarly, the appraisal industry and the private mortgage insurance industry impact on mortgage lending in low-income and minority communities remains relatively unexplored by the Congress. But, on the street, as I have pointed out today, these industries play a critical role in determining who gets a loan and what neighborhoods can be ignored by mortgage capital. Both industries remain poorly regulated at the federal and state level.

(4) Establish a Home Owners Counseling Fund

Finally, the development of community-based organizations' capacity to be partners with lenders will require federal financial assistance. We propose that the Congress establish and appropriate funds for community-based loan counseling operational and capacity building support. A very modest amount of money allocated through an autonomous program at HUD or through local jurisdictions under the HOME program will go a long way to assisting lenders in identifying and meeting community credit demand.

CONCLUSION

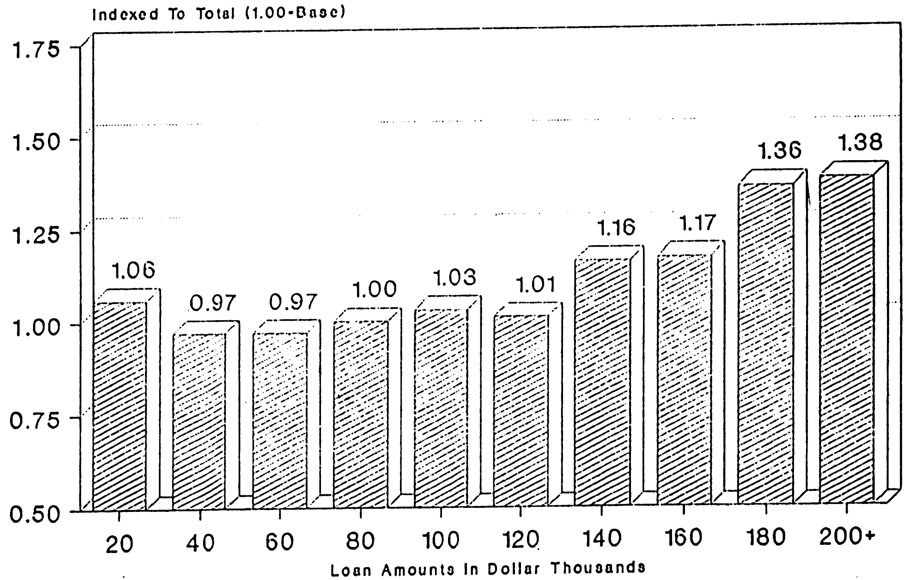
The credit needs are great here in North Philadelphia and in communities like this across the country. Public and private disinvestment has left visibly deep scars and has presented us with a formidable challenge. But, as I have shown today, it is possible for communities and bankers to work toegther to promote economic opportunity and to begin to turn neighborhoods around. The odds are long, but not impossible.

A little helping hand from the federal government in the ways we have suggested will greatly assist us in getting on with the hard work that we must do ourselves to improve economic conditions here in Philadelphia.

I thank you for the opportunity to testify today.

EXHIBIT A

Incremental Risk Of Higher Loan Amounts
Privately Insured Mortgages: National



Source: MICA
Fixed Rate, Non-Investor
Years 79-87, As Of 6/89

MEMORANDUM

Date: 6/19/92

To: Joe M. Cleaver
Executive Secretary
Federal Financial Institutions Examination Council
2100 Pennsylvania Ave., NW
Suite 200
Washington, DC 20037

From: Association of Community Organizations for Reform Now (ACORN)

re: **Reporting of Information on Small Business and Small Farm Lending by Banks, Thrifts, and U.S. Branches and Agencies of Foreign Banks.**

(FR Docket No. 92-11766)

Thank you for the opportunity to comment on proposed changes to the Reports of Condition and Income filed by insured commercial banks and FDIC-supervised savings banks, to the Thrift Financial Report filed by savings associations, and to the Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks filed by U.S. branches and agencies of foreign banks. Chris Lewis or Deepak Bhargava are available at (202) 547-9292 to answer any questions you may have or provide additional information on the comments and recommendations made in this memorandum.

I. Introduction.

We believe the proposed changes --with revision-- to the Reports of Condition and Income will be a key to effective monitoring of depository institution credit extension to the small business sector. It is imperative that the ultimate reporting changes reflect the public need for detailed information on the flow of capital to small businesses, particularly micro-enterprises and minority-owned small businesses.

Adequate and accessible data on small business and small farm lending will provide depository institution management with new marketing tools and assist regulatory personnel and the public in their assessment of individual financial institution compliance with relevant law and general charter obligations associated with the receipt of taxpayer-subsidized federal deposit insurance -- including, but not limited to the Community Reinvestment Act of 1977. Such information will also provide policy makers and the public with a reliable source of information on small business capital flow upon which to base future public policy.

II. Background.

In including Section 122 in the Federal Deposit Insurance Corporation Improvement Act of 1991, the Congress responded to long standing concerns of the accessibility of bank credit for small business development and expansion.

The prominent role of insured depositories in the extension of credit for small businesses is attested to by the Federal Reserve's 1989 National Survey of Small Business Finances. The Fed's survey showed that for firms with fewer than 500 employees, a majority are dependent on depository institutions as a source of credit. For the 51.9% of small business that have annual sales of less than 250 thousand dollars, over a third are reliant on depositories as a source of credit. And, for small businesses with annual sales between $1 million and $10 million --the firms that employ almost 40% of American workers in the small business sector-- dependency on depositories as a source of credit ranges from two-thirds to almost 95% of businesses.

The 1989 survey also highlights the particular vulnerability of smaller sized businesses who lack access to non-bank sources of credit. Small business with annual sales of less $100,000 are 5 times more likely to lack access to credit from non-depository sources. This data underscores these firms dependency on local depository institutions as a source of credit for day-to-day business operations, capital investment, expansion and start-up funding.

Concerns about small business credit accessibility have risen dramatically over the last decade as small businesses and small farms have adapted to dramatic structural transformation and consolidation in the banking industry. These ongoing changes -- particularly mergers and acquisitions-- combined with allegations of 'credit constriction' during the current recession have sparked new assertions and anecdotes of credit inaccessibility for small businesses.

However, all queries concerning the state of credit availability to the small business sector have lacked --until FDICIA-- reliable and timely background data.

Recognizing the critical role that insured depositories provide in the extension of credit to small businesses, the Congress acted in FDICIA to guarantee that there is a stable and reliable source of information on trends in small business lending.

In drafting this legislation, the Congress specifically highlighted the need for data collection on small businesses that face particular barriers to credit access. These small businesses were identified in the legislative history as start-up businesses and minority-owned small businesses.

III. Specific Comments.

A. Minority-Owned Businesses.

The proposal does not require reporting of lending to minority-owned small businesses. This omission conflicts with the legislative history of the provision and ensures that the Federal Reserve Board will be unable to carry out obligations under separate Section 477 of FDICIA.

The need for a separate breakdown for lending to minority-owned businesses could not be more evident today. The Congress has long recognized the difficulty that minority-owned small businesses have had in obtaining credit. This public policy demand is reflected in a number of federal initiatives designed to facilitate capital provision to minority-owned businesses. These efforts respond to the clear public need for assurances that depository institutions are operating in a non-discriminatory manner and that equal access to small business credit, irrespective of the race of the borrower, is guaranteed by the market.

FDICIA clearly sought to improve the availability of data on credit flow to minority-owned small businesses. The final rule implementing Section 122 should require separate reporting for minority-owned small businesses in each size category.

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B. Definition of Small Business and Small Farm.

The proposed changes to Reports of Condition and Income define small business by reference to the annual sales of a business. We strongly support this definition and believe that it most accurately reflects the financial identity of a small business. We endorse the $10 million annual sales cap for the definition of a small business.

The request for comment suggests that a 'three-year average of annual sales' may be an optional substitute for reporting institutions. We oppose this option on the ground that the intent of Section 122 is to seek information on the general provision of credit to the small business sector by insured depositories and not to the extension of credit to any specific small business. A three-year average would tend to inflate any single depository institution's lending to small business in any given year and would dilute the specificity and value of the reported data.

The proposed changes would require separate reporting by three different size categories of small business. We believe that this stratification is insufficient and should be expanded to include information on loans to businesses with annual sales of less $100,000 and to start-up small businesses (See paragraph C).

The legislative history, as noted above, clearly reflects a concern for obtaining data on credit accessibility to truly small businesses. A single catch-all category of lending to businesses with annual sales of less than $250,000 will gloss over great diversity in credit need within the small business sector and inadequately reflects the intent of Section 122.

The final rule implementing Section 122 should require separate reporting for businesses with annual sales of less than $100,000.

C. Lending to Start-Up Small Businesses.

Small business finance experts have long agreed that larger banks do not make genuine commercial loans to small businesses in amounts less than $100,000. If smaller loans are extended, they tend to be heavily collateralized with personal assets and are underwritten more on the basis of the collateral, than on any judgement about the business prospects of the borrower.

Lending policies that focus on more wholesale evaluations of the small business economy, particularly in minority communities, result in inefficiencies and gaps in the extension of credit to credit worthy small business borrowers. These lending strategies preclude smaller-sized loans, much start-up and expansion financing and credit extension to minority small businesses.

Urban minority start-up businesses face the double burden of seeking debt financing in more concentrated bank markets where larger institutions dominate and with limited personal collateral --due to lower rates of urban minority homeownership.

The final rule implementing Section 122 should require reporting of data on lending to small businesses in existence for less than a year.

D. Geographic Distribution.

The proposed changes do not include collecting information on the geographic extension of small business credit. In fact, the request for comment suggests that the 'geographic location' of the lending institution could be a 'suitable proxy' for the geographic location of small business borrowers.

This is a facile proposal that warrants immediate dismissal. Insured depositories routinely make loans all across the country -- and many all across the globe. To suggest that knowledge of the mailing address of the corporate charter holder provides even the slightest clue as to the geographic distribution of small business credit is to deny the basic reality of capital mobility in today's financial market place.

The final rule implementing Section 122 should require separate reporting of small business lending on a SMSA by SMSA basis for each individual depository reporter.

E. Interest and Fee Income.

The proposed changes include information on 'estimated amounts' of interest and fee income on loans to small business as required by Section 122. This information is critical to determine the relative profitability and risk of small business lending and to identify if depositories --particularly larger banks-- are cross-subsidizing their wholesale lending with usurious profits from their retail small business customers who often do not have the benefit of alternative sources of credit --both depository and non-depository.

The proposed interest and fee income is not broken down by size of small business category. We strongly recommend that all reported information on interest and fee income should be broken down by each size of small business category.

We are opposed to the proposal that interest and fee income data be 'estimated'. The public and bank examiners have no less of an interest in accurate financial data than the shareholders of insured depositories --shareholders who do not accept estimates of income and expense.

F. Effective Date.

The request for comment suggests that proposed small business lending changes to Reports of Condition and Income will not become effective until June, 30 1993. We oppose this inordinately prolonged effective date. Depositories are fully capable of developing sufficient tracking systems to comply with proposed reporting changes by the end of this calendar year.

The final rule implementing Section 122 should be effective with the reports of condition prepared as of December 31, 1992.

Thank you for this opportunity to comment.

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON BANKING, FINANCE AND URBAN AFFAIRS

ONE HUNDRED SECOND CONGRESS

2129 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6050

June 9, 1992

Mr. Joe M. Cleaver
Executive Director
Federal Financial Institutions
  Examination Council
Suite 220
2100 Pennsylvania Avenue
Washington, D.C. 20037

Dear Mr. Cleaver:

This is to respond to the Federal Financial Institutions Examination Council's (FFIEC) request for comment regarding proposed changes to the Report of Condition and Income. These report revisions were required by the Federal Deposit Insurance Corporation Improvement Act (FDICIA).

On March 27, 1992, I joined with other Members who serve on the Committee on Banking, Finance and Urban Affairs in the U.S. House of Representatives to write to the Federal Reserve Board Chairman, Dr. Alan F. Greenspan, to stress the importance of implementing Sections 122 and 477 of FDICIA to permit regulatory personnel and the public easy access to the information about commercial lending activities within financial institutions.

After reviewing the FFIEC proposal, with certain exceptions, I found the call report changes generally adequate for the purpose of providing the regulators and the public with significant information and analysis. I commend FFIEC's recognition of the need to coordinate Section 122's requirement to collect small business loan information with Section 477's provisions directing the Federal Reserve to provide Congress with an analysis of the availability of credit for small businesses and farms.

A major concern, however, is the lack of necessary coordination between the collection and analysis requirements relating to the credit needs of minority businesses. Section 477 specifically requires the Federal Reserve to include in their annual report information on credit availability for minority-owned small businesses. FFIEC recognizes this requirement but, unlike the coordination which appears in other areas, proposes that the

Federal Reserve obtain minority-owned small business loan information be obtained from other sources, such as existing or new surveys.

May I remind FFIEC that the FDICIA requires the Federal Reserve to publish an annual report on credit availability. I cannot justify reliance on alternate sources for information about minority lending. Given the annual requirement for analysis of this data, it make clear sense that a steady and reliable source of minority loan information be included in the call reports. The recent unrest in minority neighborhoods in Los Angeles and other American cities is a sharp reminder of the critical need for regulators and taxpayers to have reliable information about whether or not the minority business community has access to adequate credit.

If it is feasible to require the number and amount outstanding of loans to small businesses be reported in three size categories to permit the Federal Reserve to use this additional information to satisfy their publishing requirements, it seems reasonable that minority business loan information be included in the call report requirements.

Another concern is the assumption that the geographic location of a lending institution is a "suitable proxy" to assess the availability of credit in specific regions of the country. While I recognize the problems associated with using the call reports to determine the geographic distribution of loans, I cannot accept the bland statement that the address of an institution is sufficient to assess the availability of credit in specific areas. Studies conducted by the Banking Committee and data collected under the Home Mortgage Disclosure Act indicate that banks and branches of banks can and do exist in areas essentially devoid of credit. It would not be burdensome if the call report, at a minimum, indicated whether the small business and minority loans were in-state or out-of-state.

It is also disturbing that the proposed regulations do not address collecting data on loans to "start up businesses" - small businesses in existence for less than a year. One of the persistent criticisms reaching this Committee has centered on the lack of funds for new businesses. In both urban and rural areas, development depends heavily on start up businesses. If the nation is to depend on credit flowing only to existing enterprises, economic activity will be sadly diminished. Data on credit for start up businesses is critical if the intent of Congress is to be met.

Regarding the effective date, the proposed date of June 30, 1993 is much too extended. If this time frame remains in the final regulations, it will mean that more than nineteen months will have lapsed between Congressional action and a reporting of the required data - an unacceptable delay.

In conclusion, I cannot stress the importance of the information which must be collected. I have long held that commercial lending, particularly to small businesses, is a most vital component of the total picture of credit availability in the United States. It is my purpose to ensure that the information we are to receive and review will guarantee that fair opportunities for credit all available to all who qualify.

Sincerely,

Henry Gonzalez

Henry B. Gonzalez
Chairman

HBG:rlm

WRITTEN TESTIMONY

of the

INDEPENDENT BANKERS ASSOCIATION OF AMERICA

regarding

COMMUNITY REINVESTMENT ACT (CRA)

before the

SUBCOMMITTEE ON HOUSING

of the

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

UNITED STATES SENATE

SEPTEMBER 15, 1992

The Independent Bankers Association of America (IBAA) is pleased to submit testimony to the Senate Banking Subcommittee on Housing as part of its oversight hearing on the Community Reinvestment Act (CRA). The IBAA is the only national trade association which exclusively represents the interests of the nation's community banks.

We hope that today's hearing is an indication of recognition that CRA, like many other recent laws, is well-intended but is the wrong solution. We hope that this is the beginning of a dialogue which will lead to an effort to identify the dangers to consumers from the tremendous regulatory burden facing bankers today from laws like CRA. It is our belief that working together, consumers and bankers can redesign CRA so that it becomes both meaningful to consumers and less painful to bankers.

For years, bankers have complained that CRA is one of the most onerous regulations they have to comply with and offers little benefit to their customers. Community bankers have pointed out that they are lenders with knowledge of local communities, businesses, and economic conditions. As a result, they serve the credit needs of the local community exceptionally well.

On behalf of its members, the IBAA has urged Congress to consider the contribution this nation's community bankers make to their communities. We have made the case that all banks are not the same and that the rules applying to big and small, rural and urban, should reflect these differences to the extent possible. To that end, we have supported legislation to reduce the burden associated with CRA by providing for exemptions, self-certification, and safe harbor protection.

The IBAA also has consistently encouraged the agencies to find ways to reduce the burden imposed by CRA regulations and examinations. Many community banks lack the staff required to create the extensive paper trail that has become necessary to document their CRA activities. CRA has become a true regulatory burden as a result of unnecessary documentation requirements. We have urged examiners to focus on actual community service rather than documentation of these services.

IBAA remains opposed to laws imposing public disclosure of examination results. These disclosures weaken consumers' privacy protection and can unjustly jeopardize community confidence in a bank. Public disclosures of CRA are an ineffective supervisory tool. We will vigorously oppose any additional public disclosure requirements.

We have also protested over the unfairness of penalizing banks under CRA for not engaging in mortgage lending or other particular types of lending that, by charter or policy, the bank has elected not to do. It has been the IBAA position that CRA evaluations should consider the credit programs that the bank offers to its community and how those programs meet existing credit needs. Foremost among IBAA's positions, we have strongly advocated that any CRA programs or requirements satisfy the requirements of safety and soundness.

The first step toward reducing the burden of CRA while making it meaningful, however, must be a recognition of the problem. In fact, it appears that there is a growing recognition by all parties--Congress, regulators, bankers, and consumers--that there is a problem with CRA. Many believe that CRA has not accomplished its goal of ensuring that the credit needs of communities are being met. Others have observed that CRA has merely generated a race to produce the greatest papertrail.

Documentation has become the goal of CRA, not performance. According to a 1991 study by the Community Reinvestment Institute, documentation is the biggest factor in determining a bank's CRA rating. The Institute concluded that a bank's lending record was practically irrelevant in determining its performance. The study also found that the largest banks have disproportionately higher CRA ratings than smaller banks because they have greater resources to devote to record keeping. In response to this a cottage industry has sprouted up around the country, as several "experts" are teaching bankers how to document banks' CRA activities. Like SAT or bar exam cram courses, the goal is to train bankers on how to pass their exams, not on how to meet the real goals of CRA.

Even the consumer groups are observing problems with CRA. At a recent House Banking Committee hearing, Peggy Miller of the Consumer Federation of America testified "that a number of the consumer and community groups that have stood behind CRA over many years have felt that since regulations were drafted...it appears that it depends upon the examiners but some of the examiners are requiring virtually the same thing out of small banks as they require out of Citibank, and that was never the intent, at least our intent."

Regardless of intent, it is a tragic fact that CRA and overregulation in effect are threatening to regulate many community banks out of existence. Many are no longer able to carry the regulatory burden, provide their customers with the same level of service that they have been accustomed to, and still charge a competitive interest rate or service charge which would allow the bank to remain profitable. Consolidation of the industry is being forced through regulation, and the ones who will suffer are the consumers, farmers, and small businesses.

And according to a July 30, 1992 Wall Street Journal article titled "Regulations Drive Lending to Non-Banks," the regulatory squeeze "is driving commercial lending into the Commercial Credits and Prudential Capitals of the world." The author cites not only the regulatory pressures on commercial banks, but the fact that its competitors are not subject not similar regulatory treatment, thus affording them a considerable competitive advantage.

Fact Versus Fiction

With a recognition by all parties that CRA, for whatever reasons, is not accomplishing its goal, it is also important to discuss some of the recent initiatives to change CRA. For example, as recently as last week, the Banking Superintendent of New York State promoted his recommendations for revisions to CRA.

During the 102nd Congress, several bills to redesign CRA have been introduced by Senators Dole, Kassebaum, Mack, Shelby, Cochran, and on behalf of the Administration. These bills would provide exemptions, safe harbors, self-certification, or alternative evaluations for small banks. CRA proponents have characterized the bills as gutting CRA. Instead, the exams for the thousands of smaller banks take up much valuable examiner time that would be better focused on large institutions.

During the debate over FDICIA in the House Banking Committee in 1991, CRA received considerable attention. Rep. Paul Kanjorksi (D-PA) sponsored an amendment to exempt small banks from CRA and to provide a safe harbor. As a part of his effort, Rep. Kanjorski prepared a fact sheet which explored many of the arguments, parts of which answer some of the questions posed for this hearing and therefore discussed in the following paragraphs.

One of the more popular approaches this Congress to revising CRA is to provide small banks, which by their very nature serve their communities, with an exemption from CRA. It has been asserted that the small bank exemption will "gut" CRA. Nothing could be further from the truth, however. Even though such a provision would exempt the majority of institutions, these institutions only account for 10 percent to 20 percent of all the banking assets in the nation.

The proposal to provide a "safe harbor" has drawn similar criticism. But all of the safe harbor proposals would not allow institutions to qualify unless they have been examined recently and found to be in full compliance with CRA. Should an institution's CRA rating drop, and it is then no longer in compliance, it would lose its safe harbor. The safe harbor would in fact strengthen CRA by providing banks added incentives to encourage compliance and additional penalties for non-compliance.

It has also been asserted that CRA exemptions will lead to rampant redlining and other forms of discrimination in lending. This is a baseless argument. CRA by itself does not prohibit redlining or discrimination. It does prevent an institution from establishing or acquiring a branch or other institution if it is not meeting its community's needs.

Other federal laws, such as the Equal Credit Opportunity Act and the Fair Housing Act, prohibit discrimination. All depository institutions are subject to the ECOA and other federal consumer protection laws designed to prevent discrimination.

Finally, because most small banks already are actively involved in community lending, it is a waste of time and money to continue to require them to comply with its provisions. It is well recognized that most of the problems that CRA were meant to address are in urban areas with diverse populations with varying income levels. Rural and smalltown bankers should not be penalized for problems existing for the most part in metropolitan areas.

Furthermore, CRA is completely unnecessary when applied to community banks. For decades, bank examiners have insisted that smaller banks not make loans outside their "trade area." This policy prevents banks from making loans in unfamiliar markets. The natural result of this policy, which was firmly in place long before CRA, is that to prosper a community bank has had to make local loans--in CRA terms, "reinvest in its community."

Grant Thornton Survey

To document what had heretofore been anecdotal evidence of the degree to which bankers felt about CRA, as only one of several elements contributing to the regulatory burden, IBAA contracted with the nationally respected firm of Grant Thornton to conduct a survey aimed at quantifying the extent of the feeling and the burden itself.

The IBAA Regulatory Burden Survey involves three phases. Phase One, an opinion survey of community bankers across the country, has been completed, with responses from 2,000 bankers from all 50 states. The results of Phase 1 were used to develop the field tests which are the basis of Phase 2. Phase 3, a statistical survey, will be launched following the field tests with the goal of developing sound, quantifiable cost data from all community banks.

Phase One results show that community bankers overwhelmingly consider the Community Reinvestment Act the most burdensome and aggravating regulation. (Following CRA, in order of the most burdensome, are: Truth in Lending; appraisal requirements; call reports; formal policies; and the Real Estate Settlement Procedures Act. The attitudes of bank examiners also was ranked often by survey respondents as burdensome.)

The survey results indicate that there are some differences among the agencies in their enforcement of particular regulations, including CRA. Regardless of regulator, however, banks in all categories--those regulated by the FDIC, the Fed, and the OCC--agreed that CRA is the most burdensome of the regulations they must comply with. Federal Reserve-regulated community banks had the strongest response to CRA, with 79.5 percent of those respondents noting it as the most burdensome regulation. Between 74 percent and 75 percent of the banks regulated by the FDIC and the OCC ranked CRA as the most burdensome.

The survey results also varied among banks of different asset sizes. For example, 77.5 percent of banks between $100 million and $149 million in assets ranked CRA as most burdensome, compared to 71.67 percent of banks with assets less than $25 million, 67.16 percent of banks with assets between $150 million and $199 million and 63.4 percent of banks with assets greater than $500 million.

The ranking of CRA as the most burdensome regulation is not surprising. After Congress in 1989 ordered the results of CRA examinations to be made public, a signal was sent to the regulators to "get tough" in their CRA exams. Unfortunately, the pendulum has swung too far and community banks are suffering from "CRA overkill."

Phase 3 of the survey should be complete by the end of the year. At that time we will have figures to document the actual cost of the regulatory burden.

Access to Capital

Among the issues being explored in this hearing is whether there are particular problems that rural communities confront in obtaining access to capital. There is certainly more difficulty than in the past. The reasons are many--among them are consolidation of the industry which results in bigger banks that do not service most rural populations; and, increased regulations which result in inhibiting the ability of banks to make loans.

The recently-passed FDICIA includes many new provisions which will make lending even more difficult. Chief among them is Section 304, pertaining to real estate lending standards. In reaction to abusive practices of some banks, the regulatory agencies have overreacted by proposing highly restrictive loan-to-value criteria--lending ratios that will hamstring real estate and agricultural lending.

The problem with this unfortunate provision is that it will shut the door to housing and real estate lending except for well-capitalized institutions. Adequately capitalized institutions need not apply under the proposed regulations. This will hurt the thousands of American communities served by only one bank or savings and loan.

The impact of this harmful provision would be somewhat softened by S. 2967, the "Credit Availability and Regulatory Relief Act of 1992 (CARRA)," which would extend the effective date of Section 304. Outright repeal would be even more welcome.

Conclusion

The Community Reinvestment Act is symbolic of a larger problem both in banking and business in general. While Congress has passed laws with the best of intentions, it has often failed to consider that the regulations which follow may cause businesses to shrink, close, or cut back on benefits--or banks to make fewer loans, which in itself results in fewer jobs for Main Street℠ America.

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This point was eloquently made recently in a June 1, 1992 Wall Street Journal article by former presidential candidate and Senator George McGovern entitled "A Politician's Dream Is A Businessman's Nightmare." Reflecting on his years in Congress, followed by a shattered dream when he declared bankruptcy on his Connecticut hotel, McGovern observed the following:

> ...my business associates and I also lived with federal, state and local rules that were all passed with the objective of helping employees, protecting the environment, raising tax dollars for schools, protecting our customers from fire hazards, etc. While I never doubted the worthiness of any of these goals, the concept that most often eludes legislators is: "Can we make consumers pay the higher prices for the increased operating costs that accompany public regulation and government reporting requirements with reams of red tape." It is a simple concern that is nonetheless often ignored by legislators.
>
> ...In short, "one-size-fits-all" rules for business ignore the reality of the market place. And setting thresholds for regulatory guidelines at artificial levels...takes no account of other realities, such as profit margins, labor intensive vs. capital intensive businesses, and local market economics.
>
> The problem we face as legislators is: Where do we set the bar so that it is not too high to clear? I don't have the answer. I do know that we need to start raising these questions more often.

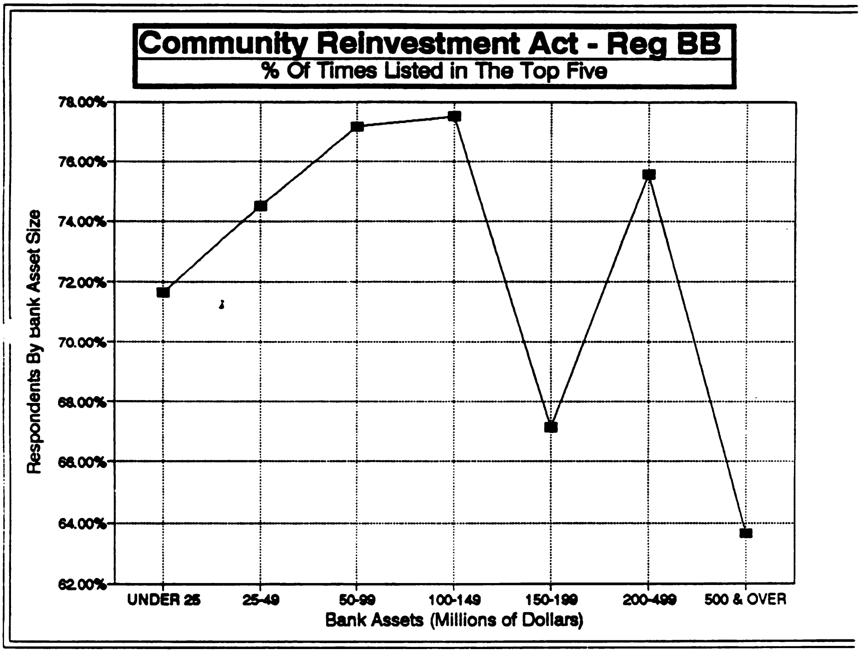
We are grateful that some in Congress and the Administration have begun to ask these questions. The most immediate way to lower the bar would be to pass S. 2967, the "Credit Availability and Regulatory Relief Act of 1992 (CARRA)."

IBAA Regulatory Burden Survey Analysis

File Name:ASSET.WQ1

BANK'S ASSET SIZE

Regulatory Description	UNDER 25	25-49	50-99	100-149	150-199	200-499	500 & OVER	TOTAL
Community Reinvestment Act - Reg BB	71.67%	74.54%	77.16%	77.50%	67.16%	75.58%	63.64%	74.39%
Truth in Lending (Reg Z)	25.48%	27.66%	37.04%	35.00%	37.31%	30.23%	27.27%	30.55%
Real Estate Settlement Procedures Act (RESPA)	31.18%	29.30%	25.51%	20.63%	22.39%	11.63%	9.09%	26.94%
Appraisal Requirements	23.57%	27.66%	26.34%	24.38%	22.39%	23.26%	18.18%	25.45%
Expedited Funds Availability Act (Reg CC)	26.05%	22.16%	27.16%	26.25%	22.39%	26.74%	18.18%	25.08%
Bank Secrecy Act	12.74%	20.70%	26.75%	34.38%	46.27%	45.35%	54.55%	23.43%
Call Reports	17.49%	16.85%	15.43%	20.63%	14.93%	13.95%	9.09%	16.74%
Formal Written Policies	25.10%	21.61%	18.72%	13.13%	11.94%	4.65%	9.09%	19.93%
Loans to Insiders-Lending Limitations (Reg O)	17.49%	16.30%	16.46%	14.38%	11.94%	16.28%	9.09%	16.31%
Home Mortgage Disclosure Act (HMDA)	7.60%	13.92%	15.02%	12.50%	16.42%	19.77%	27.27%	12.75%
Consumer Compliance Regulatory Exams	14.64%	9.71%	12.55%	12.50%	13.43%	9.30%	27.27%	12.27%
Examiners' Attitude	13.31%	10.07%	11.93%	11.88%	2.99%	4.65%	0.00%	11.05%
Equal Credit Opporunity Act (Reg B)	7.03%	8.42%	8.02%	10.00%	10.45%	3.49%	0.00%	7.86%
External Audit by CPA Firm	9.13%	7.51%	4.53%	5.00%	5.97%	2.33%	9.09%	6.70%
Safety & Soundness Regulatory Exams	7.41%	6.23%	5.76%	8.75%	13.43%	3.49%	9.09%	6.80%

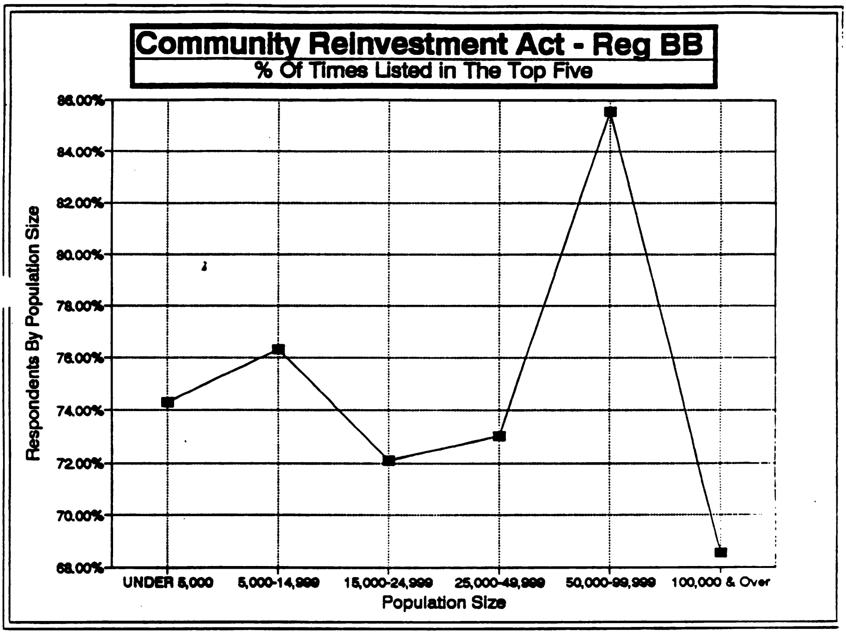

Community Reinvestment Act - Reg BB
% Of Times Listed in The Top Five
78.00%
76.00%
74.00%
72.00%
70.00%
68.00%
66.00%
64.00%
62.00%
Respondents By Bank Asset Size
UNDER 25
25-49
50-99
100-149
150-199
200-499
500 & OVER
Bank Assets (Millions of Dollars)

IBAA Regulatory Burden Survey Analysis

File Name:POP.WQ1

Population Size

Regulatory Description	UNDER 5,000	5,000-14,999	15,000-24,999	25,000-49,999	50,000-99,999	100,000 & Over	TOTAL
Community Reinvestment Act - Reg BB	74.29%	76.32%	72.11%	72.99%	85.57%	68.53%	74.37%
Truth in Lending (Reg Z)	28.42%	38.60%	30.61%	34.31%	27.84%	25.89%	30.58%
Real Estate Settlement Procedures Act (RESPA)	33.65%	27.78%	17.69%	18.98%	19.59%	9.64%	27.01%
Appraisal Requirements	27.27%	26.02%	25.17%	26.28%	17.53%	19.80%	25.52%
Expedited Funds Availability Act (Reg CC)	25.39%	26.02%	27.21%	19.71%	25.77%	24.87%	25.20%
Bank Secrecy Act	16.51%	27.19%	27.21%	31.39%	41.24%	31.98%	23.28%
Call Reports	17.24%	15.79%	17.01%	17.52%	15.46%	16.24%	16.78%
Formal Written Policies	24.45%	18.42%	23.13%	10.22%	12.37%	10.15%	20.09%
Loans to Insiders-Lending Limitations (Reg O)	15.67%	18.13%	15.65%	17.52%	14.43%	16.75%	16.30%
Home Mortgage Disclosure Act (HMDA)	10.45%	13.74%	12.93%	10.95%	19.59%	19.80%	12.73%
Consumer Compliance Regulatory Exams	13.90%	8.77%	14.29%	10.95%	11.34%	9.64%	12.20%
Examiner's Attitudes	10.34%	11.40%	10.20%	14.60%	10.31%	12.18%	11.03%
Equal Credit Opporunity Act (Reg B)	7.73%	10.82%	5.44%	5.84%	5.15%	8.63%	7.94%
External Audit by CPA Firm	8.36%	3.22%	6.80%	7.30%	4.12%	4.57%	6.61%
Safety & Soundness Regulatory Exams	6.27%	7.31%	6.12%	8.76%	6.19%	8.12%	6.82%

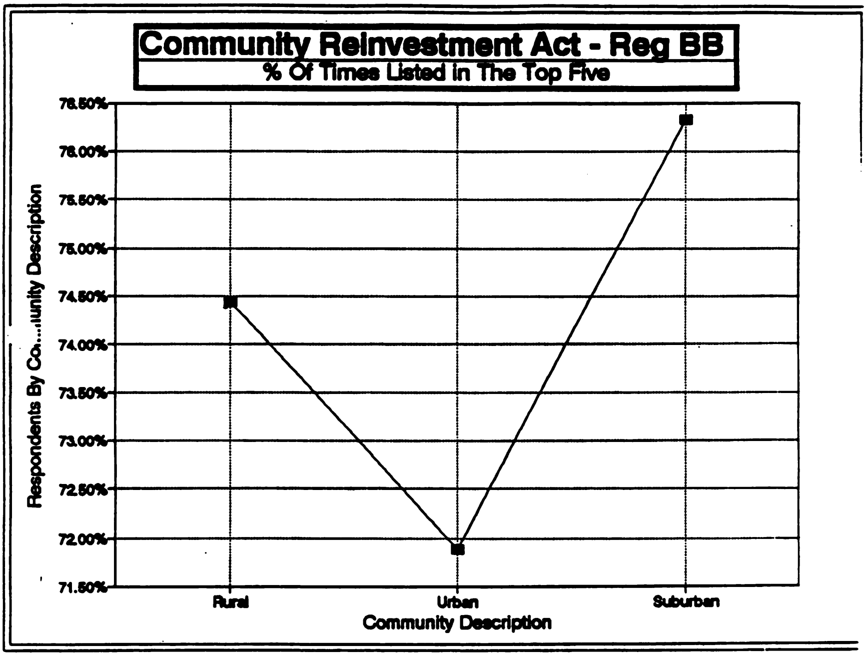

Community Reinvestment Act - Reg BB
% Of Times Listed in The Top Five
Respondents By Population Size
86.00%
84.00%
82.00%
80.00%
78.00%
76.00%
74.00%
72.00%
70.00%
68.00%
UNDER 5,000
5,000-14,999
15,000-24,999
25,000-49,999
50,000-99,999
100,000 & Over
Population Size

IBAA Regulatory Burden Survey Analysis

File Name:Comm.WQ1

Community Description

Regulatory Description	Rural	Urban	Suburban	0	0	TOTAL
Community Reinvestment Act - Reg BB	74.44%	71.88%	76.33%			74.48%
Truth in Lending (Reg Z)	30.40%	32.29%	29.67%			30.47%
Real Estate Settlement Procedures Act (RESPA)	31.48%	9.38%	18.00%			27.06%
Appraisal Requirements	27.51%	16.15%	22.67%			25.57%
Expedited Funds Availability Act (Reg CC)	25.34%	23.44%	25.00%			25.09%
Bank Secrecy Act	20.79%	29.17%	31.33%			23.34%
Call Reports	16.68%	16.67%	16.67%			16.68%
Formal Written Policies	22.89%	11.46%	12.33%			20.03%
Loans to Insiders-Lending Limitations (Reg O)	16.25%	17.19%	16.00%			16.30%
Home Mortgage Disclosure Act (HMDA)	10.47%	20.31%	18.33%			12.73%
Consumer Compliance Regulatory Exams	12.71%	8.85%	12.67%			12.31%
Examiners' Attitude	10.54%	10.42%	14.00%			11.08%
Equal Credit Opporunity Act (Reg B)	7.87%	4.69%	10.33%			7.94%
External Audit by CPA Firm	7.22%	5.73%	5.33%			6.77%
Safety & Soundness Regulatory Exams	6.35%	7.29%	8.67%			6.82%

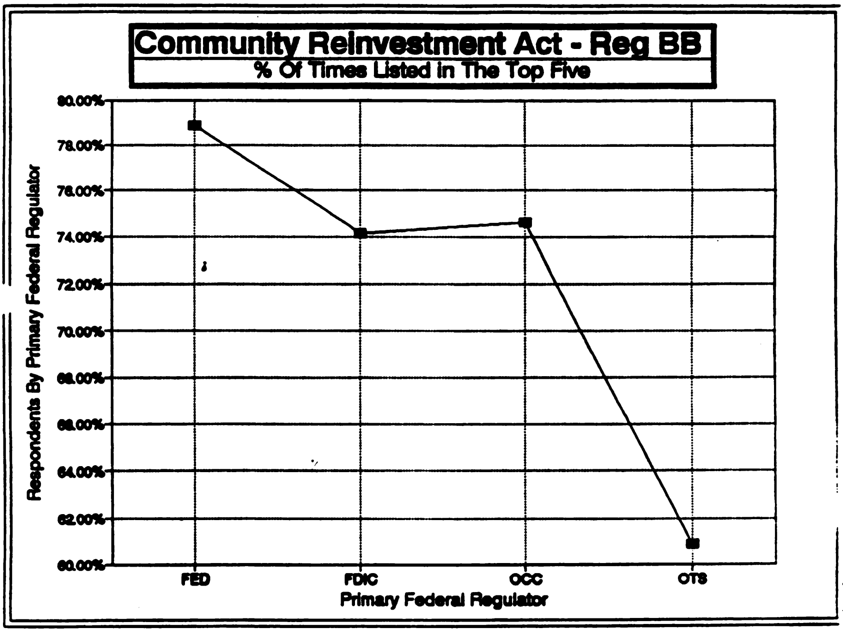

Community Reinvestment Act - Reg BB
% Of Times Listed In The Top Five
76.50%
76.00%
75.50%
75.00%
74.50%
74.00%
73.50%
73.00%
72.50%
72.00%
71.50%
Respondents By Co....unity Description
Rural
Urban
Suburban
Community Description

IBAA Regulatory Burden Survey Analysis

File Name:REGU.WQ1

Primary Federal Regulator

Regulatory Description	FED	FDIC	OCC	OTS		TOTAL
Community Reinvestment Act - Reg BB	78.88%	74.15%	74.64%	60.87%		74.53%
Truth in Lending (Reg Z)	39.13%	30.85%	26.09%	47.83%		30.38%
Real Estate Settlement Procedures Act (RESPA)	18.63%	30.24%	23.18%	13.04%		26.96%
Appraisal Requirements	22.36%	25.59%	26.82%	17.39%		25.57%
Expedited Funds Availability Act (Reg CC)	35.40%	22.96%	27.01%	17.39%		25.15%
Bank Secrecy Act	23.60%	20.42%	29.38%	13.04%		23.22%
Call Reports	16.15%	16.91%	17.15%	0.00%		16.71%
Formal Written Policies	16.15%	20.33%	20.07%	30.43%		20.02%
Loans to Insiders-Lending Limitations (Reg O)	16.15%	18.84%	11.68%	0.00%		16.28%
Home Mortgage Disclosure Act (HMDA)	11.80%	12.18%	13.87%	21.74%		12.76%
Consumer Compliance Regulatory Exams	14.29%	11.66%	13.50%	0.00%		12.28%
Examiners' Attitude	8.70%	8.85%	15.88%	8.70%		10.89%
Equal Credit Opporunity Act (Reg B)	13.04%	8.06%	6.39%	0.00%		7.90%
External Audit by CPA Firm	4.35%	7.89%	5.29%	4.35%		6.78%
Safety & Soundness Regulatory Exams	8.07%	6.66%	6.20%	21.74%		6.83%


Community Reinvestment Act - Reg BB
% Of Times Listed In The Top Five
80.00%
78.00%
76.00%
74.00%
72.00%
70.00%
68.00%
66.00%
64.00%
62.00%
60.00%
Respondents By Primary Federal Regulator
FED
FDIC
OCC
OTS
Primary Federal Regulator

IBAA INDEPENDENT BANKERS ASSOCIATION OF AMERICA

GrantThornton

Accountants and Management Consultants

The U.S. Member Firm of Grant Thornton International

Regulatory Burden: A National Opinion Survey of Community Banks

In June 1992, the IBAA began a three-part comprehensive study on regulatory burden. Almost 10,000 banks received the Phase 1 Opinion Survey on regulatory burden and 1,915 responses were tabulated. (Over 2,100 responses were received in total.) The 20 percent response rate provides a statistically sound basis to make conclusions on community banks' opinions on regulatory burden.

Community bankers overwhelmingly named the Community Reinvestment Act (CRA) as the most burdensome *and* the most aggravating regulation. After CRA, the top 10 burdensome regulations varied slightly in their ranking, based on demographic factors such as asset size, number of employees, community, and primary regulator. Making the top 10 list for burden were the Truth in Lending Act, Real Estate Settlement Procedures Act, Expedited Funds Availability Act, Appraisal Requirements, Bank Secrecy Act, Call Reports, Formal Written Policies, Loans to Insiders, and Home Mortgage Disclosure Act.

Several regulations and policies that received high aggravation ratings did not make the top 10 list for burden. The most aggravating regulatory burden was Consumer Compliance Regulatory Examinations. Other top aggravating regulatory burdens not considered in the top 10 most burdensome regulations include Safety and Soundness Exams, Geographic Loan Coding, 1099 Reporting and Examiners' Attitudes.

The results of the Phase 1 survey were used to develop Phase 2 of the IBAA study–field tests. Currently, Grant Thornton representatives are visiting several community banks to determine actual dollar costs for the most burdensome regulatory items. Phase 3, a statistical survey, will be launched following the field tests with the goal of developing sound, quantifiable data from all community banks. Good cost data on regulatory burden will be the strongest argument for reducing or eliminating unnecessary or redundant laws and regulations.

In the early fall, community banks will receive the Phase 3 survey. We strongly urge you to complete this survey. The results of Phase 3 will provide community banks the data needed to argue that the costs of the regulations facing the banking industry far outweigh any limited benefits. Reducing regulatory burden is a priority for the IBAA and we are very appreciative of your efforts to provide us with the quantifiable data needed to make our arguments stronger.

THE NUMBERS REFLECT THE RESPONSES RANKING EACH ITEM NUMBER ONE, OR MOST BURDENSOME OR MOST AGGRAVATING.

Regulatory Reports

	Cost	Aggravation
1. Applications (All Types)	362	297
2. Bank Holding Company Reports (FRY-6, Y-9C, Y-9LP)	135	77
3. Consolidated Reports of Condition and Income (Call Reports)	913	753
4. Home Mortgage Disclosure Act (HMDA)	232	501
5. Report of Transaction Accounts, Other Deposits and Vault Cash (FR 2900)	78	135
6. Shareholder Reporting	59	22
7. Other ______ (Please specify)	16	25

Examinations & Audits

	Cost	Aggravation
8. Consumer Compliance Regulatory Exams	315	1,076
9. EDP Regulatory Exams	9	45
10. External Audit by CPA Firm	891	90
11. Holding Company Regulatory Exams	5	21
12. Safety & Soundness Regulatory Exams	560	562
13. Other ______ (Please specify)	22	25

Lending-Related Regulations

	Cost	Aggravation
14. Community Reinvestment Act (Reg BB)	914	1,341
15. Equal Credit Opportunity Act (Reg B)	18	16
16. Fair Housing Act	13	15
17. Flood Disaster Protection Act	13	29
18. Real Estate Settlement Procedures Act (RESPA)	294	193
19. Truth in Lending Act (Reg Z)	518	207
20. Other ______ (Please specify)	9	9

Other Consumer Protection Regulations

	Cost	Aggravation
21. Americans With Disabilities Act: ATM Access	454	313
22. Electronic Funds Transfer Act (Reg E)	258	195
23. Expedited Funds Availability Act (Reg CC)	801	936
24. Fair Credit Reporting Act	114	171
25. Fair Debt Collection Practices Act	33	45
26. Right to Financial Privacy Act	31	42
27. Unfair and Deceptive Practices Act (Reg AA)	12	30
28. Other ______ (Please specify)	29	33

Supervisory Policies

	Cost	Aggravation
29. Disaster Recovery Plan	533	391
30. Documentation of Adequacy of Loan Loss Reserves	318	354
31. Federal Reserve Policy on Daylight Overdrafts	18	30
32. Funds Management	218	137
33. Generally Accepted Accounting Principles (GAAP)	275	234
34. Geocoding/Geographic Loan Coding	373	599
35. Selection of Securities Dealers and Brokers	13	25
36. Other ______ (Please specify)	3	6

Informational Reporting

	Cost	Aggravation
37. 1099 Reporting	1,287	678
38. Asset Growth	11	18
39. Backup Withholding	89	261
40. Bank Secrecy Act	283	592
41. Market-Value Disclosure	73	189
42. Occupational Safety and Health Administration	14	37
43. Other ______ (Please specify)	3	7

Safety & Soundness

	Cost	Aggravation
44. Affiliate Transactions	46	54
45. Appraisal Requirements	1,229	994
46. Brokered Deposits	7	11
47. Concentrations of Credit	32	44
48. Dividend Restrictions	10	24
49. Limits on Loans to One Borrower	65	56
50. Loans to Insiders-Lending Limitations (Reg O)	238	462
51. Risk-Based Capital/Equity Capital	110	127
52. Other ____ (Please specify)	4	3

Other Regulatory Constraints

	Cost	Aggravation
53. Capital and Strategic Plans	139	77
54. Environmental Lender Liability	263	210
55. Examiners' Attitudes	191	556
56. FASB Statements	142	170
57. Formal Written Policies	806	615
58. Informal Regulatory Directives	43	53
59. Regulatory Enforcement Actions	146	108
60. Other ____ (Please specify)	5	3

Most Burdensome Regulations

Regardless of category, which of the preceding regulatory items are the most costly and the most aggravating to your bank? The top ten varied slightly based on demographic factors. However, cost was most burdensome regardless of how it was cut.

1. Community Reinvestment Act - Reg BB
2. Truth in Lending
3. Real Estate Settlement Procedures Act
4. Appraisal Requirements
5. Expedited Funds Availability
6. Bank Secrecy Act
7. Call Reports
8. Formal Written Policies
9. Loans to Insiders Lending Limitations
10. Home Mortgage Disclosure Act

Demographic Data

To help in our analysis of aggregated responses, please answer the following questions. All individual responses will be held in strict confidence.

1. **Which ONE of the following terms best describes your community?** 1,385 Rural 192 Urban 300 Suburban

2. **What is the approximate population of your community?**
   957 Under 5,000
   342 5,000 - 14,999
   147 15,000 - 24,999
   137 25,000 - 49,999
   97 50,000 - 99,999
   197 100,000 or more

3. **Which ONE of the following terms best describes your bank's structure?**
   655 Individual bank without a holding company
   1,007 One-bank holding company
   22 Chain bank
   192 Multi-bank holding company

4. **What is your bank's total asset size?**
   526 Under $25 million
   546 $25 million - $49 million
   486 $50 million - $99 million
   160 $100 million - $149 million
   67 $150 million - $199 million
   86 $200 million - $499 million
   11 $500 million or more

5. **Where is your bank headquartered?** State responses received from all 50 states

6. **How many full-time employees do you have?**
   352 Under 10
   714 10-24
   467 25-49
   223 50-99
   130 100 or more

7. **Which ONE of the following terms best describes your principal lending focus?**
   673 Agribusiness
   490 Real estate
   288 Commercial
   189 Other (please describe): ______
   212 Retail

8. **Which is your primary federal regulator?**
   161 Federal Reserve
   548 OCC
   1,141 FDIC
   23 OTS

9. **Which ONE of the following statements best describes your bank's organization:**
   98 We have a compliance department headed by an officer.
   311 We do not have a compliance department, but we have a compliance officer dedicated to handling all regulatory issues.
   219 Our CEO handles all compliance issues.
   1,113 One of our other bank officers handles compliance issues in addition to his or her other responsibilities.
   29 A non-officer (such as a head teller) handles compliance issues in addition to his or her other responsibilities.
   107 Other (please describe): ______

10. **Optional: Is your bank under any regulatory directives, formal or informal?** 284 Yes 1,516 No

11. **Are you an IBAA member?** 1,593 Yes 268 No

STATEMENT OF ALAN R. TUBBS

on behalf of

THE AMERICAN BANKERS ASSOCIATION

submitted to the

HOUSING AND URBAN AFFAIRS SUBCOMMITTEE

of the

SENATE BANKING, HOUSING AND URBAN AFFAIRS COMMITTEE

SEPTEMBER 15, 1992

Mr. Chairman and members of the Subcommittee, I am Alan R. Tubbs, president of the Maquoketa State Bank in Maquoketa, Iowa, and president of the American Bankers Association. The American Bankers Association is the national trade and professional association of America's commercial banks, from the smallest to the largest. ABA's member banks represent about 90 percent of the industry's total assets; about 94 percent of our members are community banks with assets of less than $500 million.

The American Bankers Association (ABA) commends this Subcommittee for holding hearings on the impact of the Community Reinvestment Act and appreciates this opportunity to submit a statement for the record presenting the views of our members on the very important issues of local credit availability and community involvement.

Bankers have a strong commitment to their communities. You need only look at the rapid response of bankers in Florida to the needs of the residents hard hit by hurricane Andrew to see that bankers take this commitment very seriously, and that they recognize the important role they play in local economies in towns and cities across the country. Banks have pledged millions of dollars in loans to help the residents of south Florida rebuild homes and businesses that were devastated by the storm, and local bank employees worked around the clock to restore access to financial services for their customers.

Another illustration of bankers' long-term commitment to serve their communities is the industry's positive actions in the area of minority and low/moderate income mortgage lending. As I will discuss in more detail later in this statement, the American Bankers Association has undertaken a comprehensive program which we believe will make the complex process of buying and financing a home fairer, less intimidating and more accessible to all creditworthy Americans. The ABA has established a Center for Community Development within the association for the sole purpose of facilitating the flow of mortgage funds to minorities and low/moderate income neighborhoods.

The Community Reinvestment Act

The Community Reinvestment Act says that each bank should help to meet the credit needs of its community -- including the low and moderate income areas. I am in complete agreement with this philosophy, and I am willing to bet that virtually all bankers feel the same. The profitability of every bank, especially community banks like mine, rests squarely on the health and vitality of our local residents and local businesses. We recognize that there is a strong link between the availability of all types of credit -- be it for mortgages, businesses or consumers -- and healthy communities.

The problem with CRA is not that it "requires" bankers to invest in the community -- they do that anyway. The problem is that CRA has grown into a such a compliance nightmare for banks that it is robbing time and resources that could otherwise have been invested in the community. Bankers have been accused of trying to "gut" CRA by asking for regulatory relief. Let me assure you that it is not our intent to "gut" CRA, nor to excuse banks from the spirit of community reinvestment -- but we do believe that it will be in everyone's best interest look for ways to eliminate the tremendous and largely unnecessary paperwork burden that has grown out of CRA.

Ironically, the legislative history of CRA clearly indicates that it was not intended to impose any new record keeping requirements on the industry. But in fact, record keeping is now what CRA is all about. What a bank is actually doing in its community is almost irrelevant -- what counts is the thickness and neatness of the CRA files and whether or not they contain the right documentation.

The result is that over the years, CRA has become bogged down in red tape. Even worse, rather than fostering a cooperative spirit among lenders and the communities they serve, it has become a vehicle for confrontation and mistrust between community groups and banks.

Community banks like mine are particularly hard hit by the excessive paperwork and documentation requirements of CRA compliance. In an institution with only a handful of loan officers, and a total staff of perhaps 10 to 15 employees, the necessity to geo-code each loan and to document all community lending activities presents substantial problems. Compliance with these regulations absorbs real resources and costs real money. Mr. Chairman, in your letter of invitation you asked if there were ways to improve the enforcement of CRA. My answer is that we *must* find a better way -- because the road we are on now is too expensive, too time consuming, and is simply wasting too many precious community resources.

Banks, particularly large banks, are also distressed by the fact that even a satisfactory or outstanding CRA rating does not protect them from a community group protest against a merger or acquisition application. This clearly sends the wrong message. What incentive is there to work hard to achieve a high rating and to establish a superior record in community lending? Surely it is reasonable to expect that good performance would protect an institution from CRA protests for some length of time. The way the system works now, a community group can delay a proposed merger or acquisition for an institution that received a satisfactory or even an outstanding CRA rating the day before.

Bankers across the country are clearly frustrated and angry at what they perceive as regulatory overkill in the area of CRA. There are many bankers out there working hard to serve their communities -- they are civic-minded citizens and good businessmen trying to do their job. They are far more eloquent in their pleas for a return to rational and reasonable regulation than I am, so let me take this opportunity to share with you some of their words on how CRA regulations are affecting their operations and their ability to serve their communities.

A $22 million bank in the West writes:

> Our bank has always prided itself in lending out between 65 and 80 percent of its deposits in our small town and the immediately surrounding area (farm loans, etc.). In addition, we participate in most civic endeavors in our community. While we did receive a "Satisfactory" rating at our most recent compliance examination, the examiner pointed out several areas where we need to improve our documentation. She stated that there are banks that lend out a smaller percentage of their deposits in their communities but receive higher ratings because of immaculate CRA files. If that isn't putting paperwork ahead of the consumer I don't know what is.

A $113 million bank in the Southwest writes:

> One of our biggest problems is the Community Reinvestment Act (CRA). The Community Reinvestment Act is virtually meaningless to banks in communities the size of mine... we cannot afford to discriminate. There are not enough good loans to go around. Believe me, no matter what part of town an individual lives in, his race, color, religion, etc., if he has good credit and a meaningful request, it will be funded. The Community Reinvestment Act adds absolutely nothing, but requires hours upon hours of time and thousands of dollars in documentation expenses to comply with.
>
> This bank underwent a Community Reinvestment Act examination a few months ago. We had two national bank examiners spend <u>three weeks</u> with us to examine all of our paperwork, plans, etc. Of course, we were found to be satisfactory, but think of the cost it entailed to have our policies, procedures, action plans, etc., all documented according to the regulations, not to mention the cost of sending two full-time people away from their homes to this bank to examine our CRA file.

This is ludicrous and a waste of taxpayers' money, not to mention a waste of our money and efforts.

A $25 million bank in the West writes:

One of the reasons [the economy] is suffering is because bankers no longer have time to be bankers. Instead, we must study, train and supervise our officers and staff for unnecessary regulations.

A case in point is the Community Reinvestment Act. CRA examiners pay no attention to the actual lending that a bank does. Instead, they focus exclusively on pretty files full of surveys, news clippings and demographics. Most community banks know their community intimately and they eagerly serve the lending needs of the community. They don't need reams of paper and sophisticated studies to do their job. What they need is the time to solicit loans, make loans and properly supervise loans.

A $7 billion bank in the West writes:

[My bank] supports the spirit and intent of CRA and endeavors to provide banking services to all sectors of the communities it serves. However, CRA compliance has taken on a life of its own, with burdens, including answering to consumer groups, which far exceed the benefits.

For example, Section 804 of the Community Reinvestment Act requires financial institution supervisory agencies to assess an institution's record of meeting the credit needs of its community. The combination of the regulations promulgated, the various policy statements, and most recently the expectations of the examiners, have shifted responsibility for documenting this assessment process from the agency to the bank. In the absence of the bank generating substantial and convincing paper trails evidencing detailed activity, a bank is considered in non-compliance with CRA regardless of actual compliance efforts. While the examiner's assessment process should include all evidence, often an examiner will disallow or substantially discount any evidence of compliance outside the so called "CRA documentation file." There appears to be a prevalent presumption (not supported in law, policy or regulation) that if the bank does not write it down and put the memorandum in the CRA file, an event did not occur -- a difficult presumption to overcome.

The tremendous amount of paper work associated with documenting CRA activities and the need to develop and analyze community demographics, geo-analysis and other related data, has diverted management's time from actually serving the community and has greatly increased the cost of those services that do result. We recommend that the responsibility for documenting this assessment process be returned to the agency where the statute originally placed it and that CRA activities be refocused away from compliance nitpicking to providing services to all consumers.

A $140 million bank in the West writes:

I am writing to you to express my concern over the excessive paperwork and red tape that is obstructing both the economic growth of banks today, as well as the burden it places on our ability to serve our customers and the communities therein.

The success of our bank depends upon its ability to serve the communities surrounding us and with all of the CRA regulations now in effect and the paperwork that must be done, we spend more time "proving" that we are serving the communities. It is extremely frustrating to spend so much time and money executing the necessary paperwork that could be better spent meeting the needs of our customers and promoting economic growth. 31% of our bank's profits this year alone have gone to CRA staff salaries, training, materials, etc.

A $28 million bank in the Mid-west writes:

Because I am a small bank I will not be successful if I do not serve the community in which I operate. However, because of the documentation guidelines of the CRA I estimate that I spend approximately 200 hours per year in documenting compliance with this particular regulation. It certainly seems that an examiner wanting to review my compliance with CRA could just as easily review all applications and determine if those [loans] that are turned down are turned down for valid reasons in view of similar type loans that were approved.

As a community bank, the employees and I do a significant amount of work in our community. We assist charitable organizations in raising funds, we lend a helping hand in many organizations and have a true interest in serving those living and/or doing business in our community. If we could somehow reduce the paperwork and red tape necessary to operate our small bank we would have additional money and time to use in benefiting the community in a much greater way.

A $1.5 billion bank in the Southwest writes:

One of the most difficult and exasperating areas of regulation is CRA -- Community Reinvestment Act. The documentation burden that this Act has created rivals the New York City telephone book. The banks are required to document all areas of their community involvement, compile detailed statistical analyses to prove their actions, dedicate staff resources to developing,

> understanding and maintaining the records. The really sad reality of all this work is that the only people who have ever looked at our CRA records have been bank examiners.

I could go on, Mr. Chairman, but I'm sure you get the idea. Bankers are upset with the way CRA is being interpreted and enforced. These comments make it clear that there is no problem complying with the spirit of CRA -- bankers understand their communities' need for credit and are dedicated to serving those needs. As I said at the beginning of this statement, the problem with CRA is the complex and often confusing web of regulations which have grown up around it.

The Competitive Impact

The regulatory costs of complying with CRA raise the operating costs of banks; however, other financial firms offering virtually identical products are free to compete for bank customers without the same regulatory impediments and costs. As competition in financial markets continues to grow, the banking industry is finding the burden of regulation an increasingly heavy load to carry. We cannot continue to provide services to communities across the country if we remain shackled to the regulatory block while our competition is free to respond to new opportunities and to operate without the compliance burden placed on banks.

Let me give you an example. While I am spending time documenting my community lending activities, my non-bank competitors such as Edward D. Jones are out there selling my customers money market funds and CDs. The same is true for the local credit union, the insurance agency, and the farm credit system, all of whom are free from the costs involved in documenting compliance with CRA. Furthermore, because CRA compliance drives up my costs relative to these competitors, funds are being pulled out of banks and flowing to these financial service providers who are not required to reinvest money back into the community.

Let me quote a few banker letters on the subject of the competitive impact of CRA. A $675 million bank in the Southwest writes:

> We have always felt strongly that a financial organization must maintain an active role in the communities it serves. After all, a bank can only do as well economically as the community in which it is located. Under CRA we now have the cost of creating mountains of paperwork to document our performance. Nonetheless, that is acceptable as long as <u>ALL</u> financial institutions are required to do so. There are many types of financial organizations vying for consumer deposits these days. It is time that brokerage firms, money fund management firms and insurance companies be required to invest in the communities from which they receive funds. It is laughable that banking, with its long record of

community stewardship, is the only financial industry subject to CRA. These other financial institutions control a greater portion of our nation's investment capital today than ever before.

A $50 million bank in the Mid-west writes:

During the next three months, I estimate that 50% of my time will be spent on regulatory compliance issues. What is really sad and ironic is that my time will not be spent on regulations which affect the safety and soundness of the bank's loans and other assets. Rather, it will be spent on regulations such as the Community Reinvestment Act ...

What would I normally be doing with this lost 50% of my work week? I would be calling on existing and prospective customers, making loans or working to develop new deposit and loan products to more effectively compete in the marketplace - the real heart and soul of banking. Isn't that what banking is all about?

This scenario is especially discouraging when I consider that many of my competitors - insurance companies, mutual funds, stock brokers - are not [subject to CRA]... they happily suck an increasing share of the deposit base out of my community, never to return in the form of loans or other investments.

The Burden of CRA Documentation and Other Regulatory Red Tape is Not Just a Banker Issue

The banker comments cited above regarding the time and expense involved in documenting compliance with CRA and the implications of competing with financial service providers who are not subject to the same rules are illustrative of a broader problem with the growing burden of regulatory red tape. Should anyone other than bankers be concerned about this burden? The answer is a resounding yes -- all bank customers should care. In fact, anyone interested in the health of their local economy should care.

Simple economics tells us that, other things being equal, reducing the paperwork burden will free up bank resources for lending and reduce the cost of bank credit. The reverse is also true. If the regulatory burden -- including the red tape involved in documenting compliance with CRA -- continues to rise, more and more real resources will be devoted to non-productive paperwork. This will leave fewer resources for the core business of banking, which is making loans and providing high quality financial services to our customers.

Ultimately, a good portion of the cost of unnecessary paperwork must be paid by the consumers of bank products. The resulting higher price of bank products will make them less competitive, and some customers, particularly more sophisticated customers, will shift their business to financial service providers who are not subject to the costs imposed on banks. Others, like consumers and small businesses who have less access to alternative sources of credit, will find bank loans more expensive and more difficult to obtain. Clearly this is not a desirable result, and it is certainly not what CRA was intended to accomplish.

In today's economic environment, the impact of the growing burden of regulatory red tape on the cost and availability of bank credit is masked by weak loan demand in many parts of the country. But when the economy strengthens and loan demand picks up, the costs and constraints imposed on banks by the tangled web of regulatory paperwork will certainly be felt in the economy. In the long run, the paperwork burden will erode bankings' ability to support the economic growth of towns and cities across the country.

These are important issues that should concern us all -- bankers, bank customers, and policymakers alike.

Collecting Data on Small Business and Small Farm Loans Will Not Increase Credit Availability

There has been a lot of controversy lately over whether there is a lack of credit -- especially for small businesses and small farms -- and whether it is inhibiting the recovery. In an effort to calculate the amount of credit currently outstanding to these types of entities, Congress included two provisions in the Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) which direct financial institutions to provide bank regulators with information on their small business and small farm lending practices.

However well-intentioned, these provisions will not provide policymakers with useful information on credit availability. But they will impose another layer of unnecessary red tape on both banks and their small businesses/small farm customers. The provisions direct banks to categorize their small business/small farm loan portfolios based on annual sales of the business, and requires banks to estimate interest and fee income and net charge-offs for various categories of these loans. In many cases, compliance with these regulations will necessitate new computer systems; in all cases, significant personnel costs will be incurred to compile the data. And in the end, the required disclosures will provide little, if any, useful information on credit availability.

Again, let me quote some bankers on this issue.

A $50 million bank in the central region writes:

The small business and loan data (Section 122) of the FDIC Improvement Act of 1991 requires that data concerning loans to small business and small farms be collected with the Call Report. There is not enough room here to detail what is required except to say that it is lengthy. The only way for me to comply with the provisions of Section 122 would be to go through every loan file in the bank and check the financial statements of every farm or business borrower. I estimate that this would take [two people] at least one day apiece each quarter.

The burden [of preparing the Call Report] will increase dramatically if Section 122 is allowed to go into effect as scheduled. Please vote to repeal Section 122 of the FDIC Improvement Act of 1991 so that a banker can spend more time meeting the needs of his community and less time meeting the needs of the government.

A $26 million bank in the West writes:

The proposed regulation requiring us to track loans made to small businesses and small farms is another unnecessary burden. Again, we make all these types of loans that we can prudently make. To monitor and track these credits to comply with the proposed regulations will be very costly to our bank. When one compares the benefit that is derived from imposing these regulations to what the cost of monitoring and tracking, it is simply a big waste of time and effort, especially for the smaller sized banks.

As these two bankers pointed out, heaping additional reporting requirements on banks will not increase credit availability. In fact, it is likely to have the opposite effect -- the added costs of collecting and reporting this data will tend to decrease the availability of bank credit and increase its cost. This burden will be in the millions of dollars and will produce information that is almost worthless, since it will pick up only part of small business lending.

Clearly there are more efficient, less costly ways to determine the credit environment for small business lending than increasing the reporting burden on banks and their customers. In fact, several sources of meaningful information on credit availability to small businesses and small farms already exist. For example, the National Federation of Small Business Foundation publishes a quarterly economic report on small business which includes information on credit conditions and on the general economic activities of small businesses. In addition, the Federal Reserve currently conducts a number of surveys on credit extensions and the credit climate. Both of these sources provide timely data on the terms and conditions of small business lending and the availability of credit, and may well provide adequate data to address policymakers needs in this area.

The Impact of the Regulatory Burden on the Availability of Credit

There are steps Congress and the regulators can take that will improve the climate for bank lending. In particular, reducing the crushing burden of regulatory red tape will go a long way toward freeing up real resources to support the provision of financial services to bank customers. Based on a survey of about 1,000 banks, we estimate that the industry spent approximately $10.7 billion last year on compliance. This is a very big number -- it amounts to about 12 percent of total industry operating costs and nearly 59 percent of total industry profits last year. Clearly imposing costs of this magnitude on the industry has a negative impact on the availability and cost of bank credit.

To make matters worse, there is clearly a bias against lending in the recently-passed FDIC Improvement Act. Whether intended or not, the loud and clear message bankers are receiving from the regulators and the Congress is that only minimal levels of lending risk will be tolerated. On the surface, this certainly seems reasonable -- there is little doubt that economic consequences of a banking system with too much risk are not acceptable. But just as too much risk is undesirable, a regulatory policy that discourages banks from making loans also has serious economic consequences. Wringing out every risk from bank loan portfolios means that fewer loans will be made, and that only the very best credits will be funded. All others -- especially small businesses, which are among the riskiest of all bank loans -- will face higher prices and reduced availability of credit. The marginal borrower may not find funding at all.

The lending environment has also been affected by an emphasis on higher and higher capital levels. Over the last several years, banks have been adjusting to higher, risk-based capital requirements. Even before these new standards are fully phased in, there is pressure to meet even higher standards. This pressure is clearly evident in the avalanche of regulations that have been adopted or proposed, including those related to brokered deposits, prompt corrective action, interbank liabilities, state bank activities and investments, and even loan-to-value ratios which are pushing banks toward a new "minimum" standard called "well-capitalized."

While all bankers support solid capital levels, the question is what is the right balance and over what time period. We need to take a close look at how higher *de facto* minimum capital levels reallocate credit away from lending toward securities and raise the price of credit for bank borrowers. I emphasize "*de facto*" because the combination of various new regulations is, as a practical matter, raising the *de facto* level well above the "adequate" standard. In this context it is important to realize that bank capital, despite well-known problems in the industry, is at an all time high -- $248 billion.

The American Bankers Association's Center for Community Development

As I mentioned at the beginning of this statement, the ABA is undertaking a major initiative to facilitate increased mortgage and small business credit availability to minorities and low/moderate income neighborhoods. Last May, the American Bankers Association announced plans to establish a Center for Community Development within ABA. The Center is now up and running, and is actively working with bankers, secondary market agencies, appraisal groups, and community groups to find ways to make the home financing process fairer, less intimidating and more accessible to all creditworthy Americans.

The Center grew out of recommendations by ABA's Mortgage Lending Task Force that I appointed last year. The Task Force was comprised of bankers representing all regions of the country and including CEOs and community lending specialists. These bankers were charged with finding constructive ways to promote sound lending to minority and low/moderate income communities in order to better meet the needs of the people of these communities.

The Task Force began by taking a top-to-bottom look at the mortgage lending process. They talked with others who play critical roles in the housing finance process including realtors, appraisers, private mortgage insurers, and secondary mortgage market agencies to see how to work together to make the process of buying and financing a home fairer, less complex and less intimidating.

Community and fair housing groups also play an important role in these issues. These groups work in the communities and with the people we are trying to reach -- their insights into neighborhood dynamics and social trends are a very important element in designing practical programs that will actually be successful in increasing the flow of mortgage funds to minority and low/moderate income areas. Because using the resources of community/fair housing groups to bring potential applicants and lenders together is clearly a productive approach, the task force met with six of the major consumer/fair housing organizations, including the Center for Community Change, Association of Community Organizations for Reform Now (ACORN), Consumer Federation of America, National Fair Housing Alliance, Neighborhood Reinvestment Corporation, and National Center for Neighborhood Enterprise. ABA's Center for Community Development intends to continue the dialogue with these and other community groups and to solicit their input as we search for solutions that will increase credit availability to minority and low/moderate income borrowers.

The task force also met with representatives from the Federal Reserve, the FDIC, the Comptroller, and the Department of Housing and Urban Development to discuss how they see the problem, and look at some of the difficulties in interpreting and enforcing the HMDA and CRA statutes.

These discussions with other participants in the "housing chain" revealed several very important areas of agreement among us. Most importantly, we all agree that there is a need to increase the availability of mortgage funds to minorities and to people in low/moderate income neighborhoods. We agree that an inter-industry initiative involving all members of the housing chain including realtors, appraisers, lenders, private mortgage insurers, and secondary mortgage market agencies is necessary if we are to be successful. We agree that lenders, private mortgage insurers and secondary mortgage market agencies need to guard against inadvertent policies that may act as barriers to minority and low/moderate income borrowers, and to carefully review their underwriting criteria to make it as flexible as possible. And lastly, we agree that borrowers need a better understanding of how to make the home financing process work for them -- things like what size mortgage they can afford, how to document their creditworthiness, and what to do if they feel they have been discriminated against.

These three areas -- inter-industry cooperation, lender education, and borrower education -- form the basis for the efforts of ABA's Center for Community Development. Some of the Center's goals in these areas are:

▸ **Inter-Industry Cooperation**

Expand work with secondary market agencies and others in the housing finance chain to revise underwriting criteria that discourage lending to minorities and low/moderate income neighborhoods

Work with the appraisal industry to increase the pool of appraisers with expertise in appraising properties in low/moderate income neighborhoods, especially in inner cities

Enhance the communication and working relationship between banks and national and local community and fair housing groups to encourage constructive and effective joint efforts

▸ **Lender Education**

Increase lender awareness of secondary market education and lending programs targeted to low/moderate income markets

Collect and analyze performance data on low/moderate income mortgage portfolios

Identify non-standard approaches to determining credit worthiness and loan documentation to eliminate factors that have the effect of discriminating against low/moderate income and minority applicants

Provide guidelines and additional training materials to enhance fair lending compliance and evaluation of anti-discrimination efforts

▸ **Borrower Education**

Provide information on current borrower education programs available nationwide in which banks may participate

Develop materials that will help banks establish their own borrower/consumer education efforts

The Center for Community Development is an expression of ABA's commitment to promote sound, non-discriminatory mortgage and small business lending and to increase the availability of credit in minority and low/moderate income communities. The investment of time and energy required to carry out this commitment will reap tangible rewards for home-buyers, for large and small communities across the country, and for all participants in the housing and housing finance industry. I have attached a copy of the Center's mission statement to this testimony.

Conclusion

Bankers believe in community lending -- lending for housing, small business growth, farm operations. And we believe in doing our share to revitalize low-income neighborhoods with sound, non-discriminatory lending programs. We believe in community development because these are our communities. We live and work in them, and we want them to be as strong and vital as possible.

But over the past decade, the amount of paperwork involved in complying with regulations such as CRA has reached crisis proportions. In fact, the over-all burden of unnecessary red tape that each bank must deal with on a daily basis has grown so large that it is undermining the ability of banks to serve their customers and to meet the credit needs of their communities.

The cost of unnecessary paperwork and red tape is a serious long-term problem that will continue to eat away at the competitiveness of the industry and erode its ability to support the economic growth of towns and cities across the country. I cannot emphasize too strongly that unless something is done to reduce the burden, bank customers -- particularly consumers and small businesses who have few alternative sources of credit -- will find bank credit increasingly expensive and difficult to obtain in all phases of the business cycle.

A program for reducing paperwork and red tape has been developed by the American Bankers Association and the state bankers associations. This program would significantly reduce the burden of unnecessary paperwork without eliminating such safety and soundness provisions as risk-based premiums, annual supervisory exams, strong capital rules, annual audits, enhanced authority to restrict or close troubled institutions, strong supervisory and criminal sanctions, federal oversight of state-granted powers, restrictions on brokered deposits, FDIC back-up enforcement authority or appraisal reform.

The retention of these provisions, as well as a whole host of other supervisory tools held by the regulatory agencies, ensure that passage of the proposed program will pose no additional risk to the deposit insurance fund. In fact, the program would help protect the deposit insurance fund by enabling the banking industry to compete without the dead weight of excessive compliance costs; only a competitive industry can hold and attract capital, which is the first line of protection for the insurance fund. At the same time, the program will substantially reduce the extensive paperwork costs imposed on banks, allowing the industry to better meet the needs of its customers and the economy.

The American Bankers Association is willing and anxious to work with this Subcommittee, the Congress and the regulators to scale back the paperwork burden.

MISSION STATEMENT

The creation of the Center for Community Development Lending is an expression of the ABA's commitment to find constructive ways to promote sound mortgage lending to people in minority and low- and moderate-income communities.

The Center will be designed to function as a clearinghouse for a wide variety of information and products designed to help bankers better serve the credit needs of their minority and low/moderate income communities. In doing so, the Center will draw upon the resources of the entire housing chain, from the homebuilders, realtors, and appraisers to the mortgage lenders, mortgage insurers and secondary mortgage market agencies to find innovative ways to increase the availability of mortgage loans to all creditworthy applicants.

Our goals include:

- Educating lenders about the types of products and programs available to help them design sound minority and low/moderate income mortgage lending programs suited to their particular community's needs.
- Acting as a liaison between lenders and other key players in the housing finance chain to eliminate obstacles that may be present in these areas.
- Provide a clearinghouse of information on borrower education and outreach programs developed by ABA and/or a variety of agencies and community groups.

The Center will continue to work to fill the gaps in the available materials and as the ABA gains more insight into how we can best help member banks, the Center will expand it's activities to provide more "hands on" assistance.

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