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Statement by

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I appreciate the opportunity to appear before this subcommittee to discuss the Community Reinvestment Act and the current efforts of the agencies to strengthen and improve its administration. This statute has become an extremely important part of the landscape of financial institution supervision in recent years. Across our nation it has affected the relationship between thousands of banks and thrift institutions and their communities--particularly low- and moderate-income neighborhoods. Institutions both large and small have struggled with the law's demands. Local groups have aggressively used it--particularly in the applications process--to prompt commitments for increased lending to those who may have been overlooked before. The regulators have sought to enforce the law fairly and fully in the face of the enormous diversity which exists among America's communities and its financial institutions.

The results of CRA have seldom been to the full satisfaction of either the covered institutions or community groups, and the President has directed the agencies to conduct a thorough reexamination of our supervisory approach. This is a zero based review which will take into account the views of all affected parties. In doing so, it is important to start from a common understanding of the road we've traveled since the statute was enacted in 1977.

Impact of CRA

While the total impact of the CRA is very hard to measure, I believe a fair assessment would have to conclude that

it has generally made many depository institutions more responsive to the needs of their communities. Of course, the level of effort has varied widely among institutions. Certainly it has not cured the disinvestment that plagues many of our cities. But CRA has, in my view, been very instrumental in opening channels of communication between banks and thrifts and segments of their communities that were previously underserved. New relationships have been established with community groups and individuals, new products have been designed and marketed, and many thousands of credit applications have been taken from those who previously had no banking relationship. Most importantly, I am convinced that thousands of loans have been made throughout the country that would not have been made but for the CRA. I have personally traveled to many communities and toured numerous projects that are now helping to stabilize and revitalize communities as a result of CRA. In addition, numerous witnesses from consumer and community organizations at hearings we have held recently have testified to the valuable contributions CRA has made.

But exactly what is the overall level of that lending? I do not know, and I suspect no one does. The community groups who track lending agreements with institutions point to over \$30 billion in commitments for new credit. Many of these commitments cover several years and therefore extend into the future. Moreover, I know of no overall assessment of the extent to which the commitments have been realized. While formal commitments to

community groups get considerable media attention, I suspect that most CRA related activity goes on outside the high profile negotiated agreements that receive so much attention. My own belief is that the true impact of CRA has far exceeded any number derived strictly from the formal commitments. If the figure is, for example, double the committed amount, it is a formidable amount indeed, and this fact should not be overlooked as we evaluate CRA's effectiveness.

Whatever the degree of new lending attributable to CRA, it has not been accomplished without numerous problems, which I will refer to later. But before doing that, there is an important point about CRA that's often lost in the debate about its flaws. If this Federal statute has, in fact, had the considerable impact I have described, it's important to note that this has been accomplished without a huge appropriation of government dollars, and without legions of bureaucrats to administer the program. These, of course, are very significant and topical matters--as current as the recently announced campaign to "reinvent" government in ways that emphasize these very characteristics.

CRA established a national goal and put considerable power in both supervisory agencies and the public to enforce it, but left the details of how this goal would be accomplished to local communities and depository institutions. CRA counted on the unique economic needs, and the give and take in the local social and political scene, to define the specifics of the CRA

program for each community. No one in Washington has yet been employed to decide how much or what type of CRA lending should be made in the individual communities you represent. To my way of thinking, that has been a considerable strength of the law. In any review of CRA I believe we must acknowledge the value of this approach, at the same time that we search for improvements.

Need for Improvement

But all is not perfect as you well know. The flexibility that I've referred to has come with a price. Bankers and many community groups alike complain that the standards are too vague. Our own examiners would be more comfortable as they go about their very difficult job of assessing compliance if the rules of the game were more precise. Despite the ever increasing efforts of the agencies over the years to define more specifically the various levels of performance used in our rating system, we are constantly faced with questions about "how much is enough," what loans get CRA credit, and exactly what "weight" different categories of loans will receive. Living with the current uncertainty makes bankers nervous, community groups dissatisfied with their ability to hold institutions accountable, and everyone involved concerned about assuring fair and consistent evaluations by the agencies. And believe me, no one would be happier than those in my agency, who are charged with the day-to-day enforcement of the law, if we were "going by the book."

There also appears to be common agreement that too much emphasis has been placed on paperwork and process as opposed to performance. There is undoubtedly some truth to this despite the agencies' efforts to assure otherwise. But, it is important to keep in mind that, in some sense, the focus on process is a natural outgrowth of leaving the definition of an appropriate level of performance up to the needs of the community and the capacity of its institutions. Nevertheless, the concern about focusing on paperwork rather than results is widespread enough to require careful evaluation.

And, of course, there are other criticisms as well-- that CRA is "too much stick and too little carrot" and that we must search for more incentives to encourage good performance, that too many institutions receive satisfactory or better ratings, and that either too much or too little emphasis is given to CRA in the context of application processing. Suffice it to say that there are numerous areas of controversy where improvements may be desirable.

Thus, we have what to me is a rather confusing scene. On the one hand, we have an important national program that appears to have stimulated considerable lending and revitalization in low-income and minority communities. And it has done so in a period of great shortage of federal dollars, and without the rules and red tape that bedevil so many government efforts. On the other hand, I know of no other regulatory area where there is such common agreement that all is not right and

that some "reform" is necessary. My overall sense, however, is that in focusing so much on the imperfections of CRA, we may have lost sight of its considerable benefits.

Review Process

But surely we can do better. And, it was in response to widespread concern that the CRA can be improved that the President issued his charge to the agencies to rethink their administration of this law. In the President's CRA reform request, he asked the agencies to address several specific areas. These include:

- developing new regulations and procedures that replace paperwork and uncertainty with greater performance, clarity, and objectivity;
- developing a core of well-trained CRA examiners;
- working together to promote consistency, and even-handedness, to improve public CRA performance evaluations, to institute more effective sanctions against financial institutions with consistently poor performance, and to develop more objective, performance-based CRA assessment standards that minimize the compliance burden on financial institutions, while stimulating CRA performance.

As you are aware, we are presently working with the other agencies to carry out the President's initiative. Working together is not new to us in this area. To promote uniformity in the approach to CRA, the Board, along with the other banking and

thrift regulatory agencies, have worked through the Federal Financial Institutions Examination Council, or FFIEC, for some time. For example, through the FFIEC the agencies developed a common approach to the regulation, interagency CRA examination procedures, a uniform format for CRA public disclosures, and other regulatory material. We have a commitment to cooperation and uniformity, and I am confident that together we can meet the President's goals and that any revision of CRA will be adopted on a common basis.

Initially, our focus has been on assuring wide public input. The agencies have held public CRA meetings across the country to solicit comments on how to improve the CRA process. We have heard the views of over 250 bankers, community groups and small business owners, as well as members of the general public. From these meetings, we have been told what is working with CRA, what is not working, and what we need to consider to "fix" it. I can tell you that many of the stories I have heard--from bankers, small business owners and community groups--have been compelling. The stories, however, point up as many differences in perspective between the various groups, as they do common concerns.

For example, while many may agree that it's important to find new incentives to encourage better CRA performance, there is great disagreement about what they might be. Very understandably, banks which have sought and achieved an "outstanding" rating would like to see this rewarded with a "safe harbor" from protests. Community groups, to put it mildly, do

not favor the idea. While there is common concern about paperwork, there is a growing recognition that any movement toward more quantifiable standards may require more, not less, data, and this is not a happy thought for many. Likewise, concern about the disproportionate burden on small institutions has caused some to suggest a small institution exemption. Others find this untenable. The idea of more precision in the requirements has widespread support, but difficult and controversial issues arise when it comes to defining what the specific numbers might be or even the process by which they might be set. Moreover, there is broadbased concern that in attempting to be precise, we may fall into the credit allocation trap. In short, although there may be widespread agreement that CRA requires some major repairs, there is very little agreement about the appropriate fix.

At this point, we are still analyzing the information we've collected and it would be premature for us to offer any proposals. The Board along with the other agencies will continue this process of assessing the various arguments and concerns. I expect that a proposal will be published for additional public comment in the next few weeks.

You've asked whether the statutory language will permit the necessary reforms. There may or may not be a constructive role for legislation at some point, but it seems premature to make that judgment now. We will be in a much better position to

provide meaningful thoughts on whether legislation is needed at a later date.

Fair Lending Enforcement

Finally, you have asked for information on the steps we have taken to assure compliance with fair lending laws.

Initially, let me say that no single consumer compliance issue is of more concern to the Board, and me personally, than assuring that the credit granting process is absolutely free of unfair bias.

Fairness in assessing credit applications, without regard to race, sex or other prohibited bases, is absolutely essential in our country. Let no one have any misunderstanding on the point. Racial discrimination, no matter how subtle--and whether intended or not--cannot be tolerated. It robs the lending industry and our economy of growth potential, and harms both individuals and society.

We have a coordinated approach to this issue at the Federal Reserve which focuses both narrowly on examination for compliance with fair lending laws, and more broadly at trying to assure that credit is made widely available to low- and moderate-income areas of our country--including those with substantial minority populations. Our approach to fair lending issues is thus a comprehensive one that goes beyond examinations. It also involves an aggressive program to investigate consumer complaints, provide consumer and creditor education, and gain insight through research. Let me describe each segment briefly.

In the research area, the Boston Federal Reserve Bank study is well known. In my view, despite its shortcomings, that study has done more than any other single effort to advance our understanding--and increase our concern--about fair lending in the mortgage market. Other research pieces on HMDA data, household debt, credit shopping practices, the secondary market and other related subjects have also added to our knowledge. Within the next few weeks we will be releasing a comprehensive report to Congress comparing the risks and returns of lending in low income, minority and distressed neighborhoods compared with those in other communities. This too will advance our knowledge of the problem and how to help solve it.

With regard to examinations, the Board supervises approximately 1000 state member banks for compliance with fair lending laws. This involves consumer compliance examinations, consumer complaint investigations, and community affairs efforts. The consumer compliance examinations are conducted by examiners at the Reserve Banks who are specially trained in consumer affairs and civil rights examination techniques. The Board and each of the Reserve Banks also have staff members who deal with consumer complaints. In addition, the system has a substantial Community Affairs program, many of whose activities help to advance fair lending. The Board provides general guidance and oversight to Reserve Banks in these areas.

The Board first established a specialized consumer compliance examination program in 1977. Through it, the twelve

Reserve Banks conduct examinations of state member banks to determine compliance with consumer protection legislation by using a group of specially trained examiners. The scope of these examinations specifically include the Equal Credit Opportunity and Fair Housing Acts. From the beginning, the examiners were instructed to place special emphasis on violations involving potential discrimination of the kind prohibited by those statutes.

The Federal Reserve System's consumer compliance examinations are scheduled at regular intervals and are comprehensive. Each state member bank is examined on a regular basis. An average of two-thirds of state member banks are examined each year. In general, examinations are scheduled every eighteen months for a bank with a satisfactory record. A limited number of banks with exceptional records can be examined every two years. Those banks with less than satisfactory records are to be examined every six months or every year, depending on the severity of their problems.

The examination procedures focus primarily on comparing the treatment of members of a protected class with other loan applicants. First, the bank's loan policies and procedures are reviewed. This is done by reviewing bank documents, as well as interviewing loan personnel. During this phase, the examiner will seek to determine, among other things, the bank's credit standards. After the standards have been identified, the examiner will determine whether those standards were, in fact,

applied uniformly using a sample of actual loan applicants. Special note will be taken of applications received from minorities, women, and others whom the laws were designed to protect. This means that the examiner is looking at the same information that the bank used to make its credit decision, including credit history, income, and total debt burden. If those standards appear not to have been used, or not used consistently, this would be discussed with lending personnel and a more intensive investigation would typically be undertaken. Finally, an overall analysis of the bank's treatment of applications from minorities, women, and others with the characteristics described in the fair lending laws is conducted to determine whether there are any patterns or individual instances where such applicants were treated less favorably than other loan applicants.

Another regular part of the examination includes conversations with persons in the community knowledgeable about local credit needs. The examiners will routinely ask about public perceptions of the availability of credit to minorities and low- and moderate-income persons. This information may suggest that a particular area of the bank needs additional scrutiny and may provide insights into how the bank is serving the credit needs of its local community, particularly those protected by the antidiscrimination statutes. Violations found through the techniques described above require correction by the

institution, notification to the applicant and referral to the Department of Justice in appropriate cases.

As you know despite these efforts we have rarely found evidence that we can be sure proves racial discrimination. Consequently, we have been concerned about providing examiners with better tools to help them get the job done. Recently, the Federal Reserve System developed a computerized model for using HMDA data in connection with the fair lending portion of the examination. This model allows examiners to match minority and nonminority pairs of applicants with similar credit characteristics, but different loan outcomes, for a more extensive fair lending review. Once the pairs are selected, examiners pull the credit files for the applicants to determine if discrimination played a part in the credit granting process. While a comparison of minority and majority applicants has always been a part of the Federal Reserve's fair lending examination, we believe that this computerized selection process will enable examiners to focus their efforts and spend more time on the actual fair lending review of loan files.

In addition to this "micro" use of the HMDA data, the Federal Reserve has developed (on behalf of the FFIEC) a computerized system for analyzing the expanded data collected under the Home Mortgage Disclosure Act (HMDA). The system is extremely versatile and allows the data to be segmented by demographic characteristics such as race, gender, and income levels, or geographic boundaries. Examiners can now sort through

vast quantities of data to focus attention on specific lending markets and draw comparisons between an individual HMDA reporter's performance and of all lenders in the area. With these capabilities, examiners can more readily determine whether a bank is effectively serving all segments of its market, including low- and moderate-income and minority neighborhoods. We have been holding HMDA training sessions on how to use this system around the country for our examiners, as well as those from other agencies.

The Federal Reserve has also developed the capability to map by computer the geographic location of a bank's lending products, including mortgage loans. This mapping includes demographic information for the bank's local community. We believe that this type of analysis and presentation will enhance our ability to assess a bank's CRA performance in meeting the credit needs of its local community, including minority areas. It should also be helpful in evaluating a bank's geographic delineation of its local CRA service area to ensure that it does not exclude low- and moderate-income neighborhoods.

Consumer Complaint Program

The Federal Reserve's consumer complaint program is an important element in our overall effort to enforce fair lending laws. The investigation procedures in this regard provide special guidance with respect to complaints involving loan discrimination. Such complaints can prompt an on-site investigation by Reserve Bank personnel at the state member bank

accused of discrimination. We have a referral agreement with HUD for mortgage complaints and we have referred a number of complaints to that agency for further investigation. Like our examinations area, we are devoting considerable attention to strengthening our complaint processing system by increasing oversight, tightening deadlines for investigation, assuring more personal contact and making the public more aware of our procedures.

Educational Efforts

We believe that education is an important part of our coordinated approach. We have distributed a brochure to all the institutions we supervise entitled "Home Mortgage Lending and Equal Treatment." The brochure identifies and cautions lenders about lending standards and practices that may produce unintended discriminatory effects. It focuses on race and includes examples of subtle forms of discrimination, such as unduly conservative appraisal practices in minority areas; property standards such as size and age which may exclude homes in minority and low income areas; and unrealistically high minimum-loan amounts. More recently, a comprehensive booklet was published by the Federal Reserve Bank of Boston entitled "{Closing The Gap:} A Guide To Equal Opportunity Lending." It too has been widely circulated. It is another useful tool for lenders that suggests adjustments in institutional behavior to correct racially disparate loan practices that may be occurring in spite of bank policies to the contrary. We have also published a brochure, entitled "Home

Mortgages: Understanding the Process and Your Right to Fair Lending," to inform consumers about the mortgage application process and about their rights under fair lending and consumer protection laws.

Community Affairs Program

The Board believes that the goal of ensuring fair access to credit can also be advanced by focussing on positive actions that a lender may take to address such concerns. Consequently, through its Community Affairs program, the Federal Reserve conducts outreach, education, and technical assistance activities to help financial institutions and the public understand and address community development and reinvestment issues. We have increased resources devoted to Community Affairs activities at the Reserve Banks--now staffed with more than 50 people--to enable the Federal Reserve System to respond to the growing number of requests for information and assistance from banks and others on the Community Reinvestment Act, fair lending, and community development topics. Efforts have been expanded to work with financial institutions, banking associations, governmental entities, businesses, and community groups to develop community lending programs that help finance affordable housing, small and minority business, and other revitalization projects. Overall the Reserve Bank's Community Affairs programs sponsors or cosponsors about a hundred programs a year involving thousands of participants as a way to encourage economic development and assure fair lending.

Conclusion

Our commitment to fair lending has been emphasized by Chairman Greenspan and the heads of each of the other federal financial institutions supervisory agencies in a letter to every bank and thrift in the country. That letter dated May 27, 1993, expressed the agencies' concern that some minority consumers and small business owners may be experiencing discriminatory treatment when trying to obtain credit. The letter put the institutions on notice of our very serious concern, and urged financial institutions to aggressively undertake lending programs. Various suggestions were provided on how institutions could help assure fair lending.

In spite of these efforts, I am well aware of the concern about whether our enforcement--indeed our overall program--has been vigorous enough. I can only assure you of our commitment to routing out every instance of unfair treatment and helping to assure more opportunities for all our citizens. The actions we are taking to augment our traditional examination techniques through new computer assisted analysis should help us considerably. Moreover, our many efforts to encourage and instruct banks in ways to broaden their lending to low- and moderate-income borrowers should provide more open access. It is my goal and it is the goal of the Federal Reserve System to ensure that all our citizens are being treated fairly.