FEDERAL RESERVE BANK OF MINNEAPOLIS

Did the CRA cause the mortgage market meltdown?

Two Federal Reserve economists examine whether available data support critics' claims that the Community Reinvestment Act spawned the subprime mortgage crisis.

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As the current financial crisis has unfolded, an argument that the Community Reinvestment Act (CRA) is at its root has gained a foothold. This argument draws on the fact that the CRA encourages commercial banks and savings institutions (collectively known as banking institutions) to help meet the credit needs of lower-income borrowers and borrowers in lower-income neighborhoods.[1/] Critics of the CRA contend that the law pushed banking institutions to undertake high-risk mortgage lending.

This article discusses key features of the CRA and presents results from our analysis of several data sources regarding the volume and performance of CRA-related mortgage lending. On balance, the evidence runs counter to the contention that the CRA lies at the root of the current mortgage crisis.

Assessing banks in context

The CRA directs federal banking regulatory agencies, including the Federal Reserve, to use their supervisory authority to encourage banking institutions to help meet the credit needs of all segments of their *local* communities. These communities, referred to hereafter as *CRA assessment areas*, are defined as the areas where banking institutions have a physical branch office presence and take deposits, including low- and moderate-income areas. The banking agencies periodically assess the performance of banking institutions in serving their local communities, including their patterns of lending to lower-income households and neighborhoods, and take the assessments into consideration when reviewing the institutions' applications for mergers, acquisitions, and branches.

The CRA emphasizes that banking institutions fulfill their CRA obligations within the framework of safe and sound operation. CRA performance evaluations have become more quantitative since 1995, when regulatory changes were enacted that stress actual performance rather than documented efforts to serve a community's credit needs. However, the CRA does not stipulate minimum targets or even goals for the volume of loans, services, or investments banking institutions must provide. While it is fair to say that the primary focus of CRA evaluations is the number and dollar amount of loans to lower-income borrowers or areas, the agencies instruct examiners to judge banks' performance in light of 1) each institution's capacity to extend credit to lower-income groups and 2) the local economic and market conditions that might affect the income and geographic distribution of lending.

Timing and originations

Before we turn to our analysis of CRA lending data, we have two important points to note regarding the CRA and its possible connection to the current mortgage crisis.

The first point is a matter of timing. The current crisis is rooted in the poor performance of mortgage loans made between 2005 and 2007. If the CRA did indeed spur the recent expansion of the subprime mortgage market and subsequent turmoil, it would be reasonable to assume that some change in the enforcement regime in 2004 or 2005 triggered a relaxation of underwriting standards by CRA-covered lenders for loans originated in the past few years. However, the CRA rules and enforcement process have not changed substantively since 1995.[2/] This fact weakens the potential link between the CRA and the current mortgage crisis.

Our second point is a matter of the originating entity. When considering the potential role of the CRA in the current mortgage crisis, it is important to account for the originating party. In particular, independent nonbank lenders, such as mortgage and finance companies and credit unions, originate a substantial share of subprime mortgages, but they are not subject to CRA regulation and, hence, are not directly influenced by CRA obligations. (We explore subprime mortgage originations in further detail below.)

The CRA may directly affect nonbank subsidiaries or affiliates of banking institutions. Banking institutions can elect to have their subsidiary or affiliate lending activity counted in CRA performance evaluations. If the banking institution elects to include affiliate activity, it cannot be done selectively. For example, the institution cannot "cherry pick" loans that would be favorably considered under the law while ignoring loans to middle- or higher-income borrowers.

In the next section, we discuss the data analysis we undertook to assess the merits of the claims that the CRA was a principal cause of the current mortgage market difficulties. The analysis focuses on two basic questions. First, what share of subprime mortgage originations is related to the CRA? Second, how have CRA-related subprime loans performed relative to other loans? We believe the answers to these two questions will shed light on the role of the CRA in the subprime crisis.

CRA-related lending volume and distribution

In analyzing the available data, we consider two distinct metrics of lending activity: loan origination activity and loan performance. With respect to the first question posed above concerning loan originations, we determine which types of lending institutions made higher-priced loans, to whom those loans were made, and in what types of neighborhoods the loans were extended.[3/] This analysis therefore depicts the fraction of subprime mortgage lending that could be related to the CRA.

Using loan origination data obtained pursuant to the Home Mortgage Disclosure Act (HMDA), we find that in 2005 and 2006, independent nonbank institutions—institutions not covered by the CRA—accounted for about half of all subprime originations. (See Table 1.) Also, about 60 percent of higher-priced loan originations went to middle- or higher-income borrowers or neighborhoods, populations not targeted by the CRA. (See Table 2.) In addition, independent nonbank institutions originated nearly half of the higher-priced loans extended to lower-income borrowers or borrowers in lower-income areas (share derived from Table 2).

In total, of all the higher-priced loans, only 6 percent were extended by CRA-regulated lenders (and their affiliates) to either lower-income borrowers or neighborhoods in the lenders' CRA assessment areas, which are the local geographies that are the primary focus for CRA evaluation purposes. The small share of subprime lending in 2005 and 2006 that can be linked to the CRA suggests it is very unlikely the CRA could have played a substantial role in the subprime crisis.

To the extent that banking institutions chose not to include their affiliates' lending in their CRA examinations, the 6 percent share overstates the volume of higher-priced, lower-income lending that CRA examiners would have counted.[4/] It is possible, however, the examiners might have considered at least some of the lower-income lending outside of CRA assessment areas if institutions asked that it be considered in their CRA performance evaluations. No data are available to assess this possibility; however, the majority of the higher-priced loans made outside of assessment areas were to middle- or higher-income borrowers. In our view, this suggests it is unlikely that the CRA was a motivating factor for such higher-priced lending. Rather, it is likely that higher-priced lending was primarily motivated by its apparent profitability.

It is also possible that the remaining share of higher-priced, lower-income lending may be indirectly attributable to the CRA due to the incentives under the CRA investment test. Specifically, examiners may have given banks "CRA credit" for their *purchases* of lower-income loans or mortgage-backed securities containing loans to lower-income populations, which could subsequently affect the supply of mortgage credit.

Although we lack definitive information on banks' CRA-induced secondary market activity, the HMDA data provide information on the types of institutions to which mortgages are sold. The data suggest that the link between independent mortgage companies and banks through direct secondary market transactions is weak, especially for lower-income loans. (See Table 3.) In 2006, only about 9 percent of independent mortgage company loan sales were to banking institutions. (Figure not shown in table.) And among these transactions, only 15 percent involved higher-priced loans to lower-income borrowers or neighborhoods. In other words, less than 2 percent of the mortgage originations sold by independent mortgage companies in 2006 were higher-priced, CRA-credit-eligible, and purchased by CRA-covered banking institutions.

Analyzing loan performance

To assess the relative performance of CRA-related, higher-priced loans, we use data from First American LoanPerformance (LP) on subprime and alt-A mortgage securitizations to compare delinquency rates for subprime and alt-A loans in lower-income neighborhoods relative to those in middle- and higher-income neighborhoods. The LP data do not provide information on borrower income or the type of originating institution, but do indicate the ZIP Code of the property, which we use to group loans into neighborhood income categories.[5/] The results indicate that the 90-days-or-more delinquency rate as of August 2008 for subprime and alt-A loans originated between January 2006 and April 2008 is high regardless of neighborhood income, with delinquency rates comparable across neighborhood income categories. (See Table 4.)[6/]

In order to gauge more precisely the possible effects of the CRA, we use the LP data again and focus attention on the subset of ZIP Codes that are similar, in principle, except for their relationship to the CRA. Specifically, we focus only on ZIP Codes right above and right below the CRA eligibility threshold. (A neighborhood meets the CRA threshold if it has a median family income equivalent to 80 percent or less of the median family income of the broader area.) As such, the only major difference between these two sets of neighborhoods should be that the CRA focuses on one group and not the other. This analysis indicates that subprime loans in ZIP Codes that are the focus of the CRA (those just below the threshold) have performed virtually the same as loans in the areas right above the threshold.[7/] (See Table 5.)

To gain further insight into the risks of lending to lower-income borrowers or areas, we also compared the performance of first mortgages originated and held in portfolio under the nationwide affordable lending programs operated by the NeighborWorks® America (NWA) partners to the performance of loans of various types as reported by the Mortgage Bankers Association of America. Many loans originated through NWA programs are done in conjunction with banking institutions subject to the CRA, so the performance of these loans provides another basis to address the relationship between the CRA and the subprime crisis. Along any measure of the severity of loan delinquency or the incidence of foreclosure, the loans originated under the NWA program have performed better than subprime loans.[8/] (See Table 6.) Although the performance of loans in the NWA portfolio provides one benchmark to compare the performance of CRA-related loans with other loans, it is only one portfolio of such loans; further research of this type could provide a stronger base from which to draw conclusions.

Another way to measure the relationship between the CRA and the subprime crisis is to examine foreclosure activity across neighborhoods that are classified by income. Data made available by RealtyTrac on foreclosure filings from January 2006 through August 2008 indicate that most foreclosure filings (e.g., about 70 percent in 2006) have taken place in middle- or higher-income neighborhoods. More important, foreclosure filings have increased at a faster pace in middle- or higher-income areas than in lower-income areas that are the focus of the CRA.[9/] (See Table 7.)

Two basic points emerge from our analysis of the available data. First, only a small portion of subprime mortgage originations is related to the CRA. Second, CRA-related loans appear to perform comparably to other types of subprime loans. Taken together, the available evidence seems to run counter to the contention that the CRA contributed in any substantive way to the current mortgage crisis.

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1/ Lower-income households are determined by comparing the income of the household to the median family income of the metropolitan statistical area (MSA) or statewide non-MSA in which the property being purchased or refinanced is located. "Lower" is less than 80 percent of the median, "middle" is 80 to 119 percent, and "higher" is 120 percent or more. Lower-income neighborhoods are determined by comparing the median family income of the census tract where the property being purchased or refinanced is located to the MSA or statewide non-MSA median family income. Income categories for census tract classification have the same numerical thresholds as those applied for households.

2/ The change in the CRA rules in 2005 focused primarily on reducing burden for smaller lenders and expanding the focus of the CRA to include some middle-income census tracts in distressed rural areas. No changes were made that encouraged lenders to relax their underwriting standards.

3/ A higher-priced loan is defined as a loan where the spread between the annual percentage rate on the loan and the rate on Treasury securities of comparable maturity is above designated thresholds. For first-lien loans, the focus of attention in this article, the designated threshold is 3 percentage points. For junior-lien loans, the threshold is 5 percentage points. The definition was adopted as part of Regulation C (the regulation that implements the Home Mortgage Disclosure Act) and was intended to identify loans that fell in the subprime portion of the mortgage market.

4/ About one-fifth of the higher-priced loans extended in the banking institutions' local communities were extended by their affiliates.

5/ We classify ZIP Code-based delinquency data by relative income in two different ways. First, we use information published by the U.S. Census Bureau on income at the ZIP Code Tabulation Area (ZCTA) level of geography. Because the ZCTA data provide an income estimate for each ZIP Code, delinquency rates can be calculated directly from the LP data based on the ZIP Code location of the properties securing the loans (see www.census.gov/geo/ZCTA/zcta.html). Second, we calculate delinquency rates for each relative income group (lower, middle, and higher) as the weighted sum of delinquencies divided by the weighted sum of mortgages, where the weights equal each ZIP Code's share of population in census tracts of the particular relative income group. Relative income is based on the 2000 census and is calculated as the median family income of the census tract divided by the median family income of its MSA or a nonmetropolitan portion of the state. The two approaches yield virtually identical results.

6/ A virtually identical relationship across neighborhood income groups is found if the pool of loans evaluated is expanded to cover those originated between January 2004 and April 2008. The only material difference is that the levels of delinquency are lower for both subprime and alt-A loans for the larger sample of loans. Such a relationship is expected, since loans that are relatively long-lived tend to perform well over time.

7/ See footnote 6.

8/ No information was available on the geographic distribution of the NWA loans. The geographic pattern of lending can matter, as certain areas of the country are experiencing much more difficult housing conditions than other areas. Also, no information was available on the age of the loans, which can have an important effect on performance.

9/ These data are reported at the ZIP Code level. We calculate the statistics by relative income group in Table 7 as before; see footnote 6. Foreclosure filings have been consolidated at the property level, so separate filings on first- and subordinate-lien loans on the same property are counted as a single filing.

Data Tables

Strengthening the Earned Income Tax Credit: Alternatives to refund anticipation loans

A collaborative effort in the Ninth Federal Reserve District has created an alternative to traditional refund anticipation loans that gives workers fast access to tax refunds at little cost.

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Since its inception in 1975, the Earned Income Tax Credit (EITC) has been lauded as one of the most important income-enhancement programs for low-wage workers. The program provides refundable tax credits to people who are working but whose earnings fall below a certain level. For tax year 2008, the eligibility threshold for a married couple filing jointly, with two or more children, was more than $41,000. The amount of the credit was up to $4,824, depending on a worker's income, marital status, and number of qualifying children. In 2007, almost 24 million working families and individuals received EITC refunds, which provided close to $48 billion in additional income.[1/]

The EITC provides a direct, measurable, and often substantial increase in the income of low-wage-earning households. However, during the past decade, the impact of the EITC has been affected by the development of the refund anticipation loan, or RAL. RALs are short-term loans backed by the EITC and other refunds that are forthcoming from the Internal Revenue Service (IRS).

RALs enable tax filers to receive refunds quickly, which makes them appealing to people who rely on their refunds to pay for pressing needs like rent, food, and utilities. However, the speed comes at a cost. RALs often entail high interest rates and fees that subtract from the full value of the EITC and other tax refunds. To help tax filers keep more of the EITC money they have coming to them, several organizations have developed alternative refund loan products. This article describes the costs of traditional refund loans and explains how some interrelated partnerships among organizations in the Ninth Federal Reserve District led to the development of a promising alternative to RALs.

The lure of RALs

By the end of the 1990s, financial service companies, including H&R Block, Jackson Hewitt, Liberty Tax Service, and independent tax preparers, were marketing RALs to people who wanted immediate access to their refund money. The companies that provide RALs do a high-volume business with low- and moderate-income clients, many of whom are eligible for the EITC. In 2006, 85 percent of all taxpayers who applied for RALs had adjusted gross incomes of $37,300 or less, and 63 percent of RAL consumers were EITC recipients.[2/]

Tax preparation firms that offer RALs screen potential clients, collect the necessary paperwork, complete the tax returns, and file them with the IRS. The preparers also inform the clients about the possibility of getting their refunds quickly—for an additional cost—via a RAL.

The RAL industry includes commercial lenders that are associated with the tax preparation firms. The lenders issue the actual refund loans, because IRS rules prohibit preparers from making loans. The lenders also provide bank accounts for many RAL borrowers. These are usually temporary accounts, established for the sole purpose of collecting tax refunds and dismantled immediately after the refunds are claimed.[3/]

The tax preparers and lenders profit through the various fees connected with issuing the RAL, and the lenders also profit from the interest on the refund itself. In 2006, the average EITC refund was $2,600. Average RAL fees on a refund of that size were $140. Combined with an average tax preparation fee of $163, total average fees for a RAL borrower came to $303, or nearly 12 percent of the average refund.[4/] The national total of EITC-related RAL fees and tax preparation fees paid in 2006 is estimated at $1.6 billion.

That figure does not include any of the interest payments that RAL borrowers make while waiting for their IRS-issued refunds to arrive. Typically, borrowers pay interest on the combined dollar amount of the RAL and any related fees. In 2006, the effective annual percentage rates for RALs, based on a ten-day loan period, ranged from 83 to 161 percent.[5/]

For low-income taxpayers, the appeal of RALs rests on the promise of receiving their loans in 24 to 48 hours—as soon as the IRS approves their tax returns—instead of waiting nine to fifteen days for a direct deposit refund or one to six weeks for a refund check. However, the use of RALs results in these taxpayers paying out a portion of their EITC refunds that could have been put to other uses.

An alternative to RALs

The appearance of RALs has motivated the development of a better, lower-priced way to provide speedy tax refunds to low-wage earners. Coalitions of nonprofit organizations, philanthropic foundations, and financial institutions have been involved in these efforts in different parts of the country over the past several years. In one state in the Ninth District—Minnesota—a collaborative came together in 2005 to design an alternative to traditional RALs. Two community-based organizations—along with four credit unions, a community development bank, and two philanthropic foundations—recently completed their third year of offering the Express Refund Loan and Savings (ERLS) Program, a pilot program that provides a lower-cost alternative to RALs.

The goals of the ERLS are twofold. The first goal is to help taxpayers establish a relationship with a mainstream financial institution, beginning with opening a savings account. The second is to save taxpayers an average of $200 to $300 in tax preparation fees, loan fees, and interest. The ERLS contains several significant components: the loan is offered at a low cost, with fees ranging from $5 to $25, and is linked to free tax assistance; the refund is directly deposited in a savings account; and customers are encouraged to save part of their refunds either in their savings accounts or through other financial products like Individual Development Accounts or Individual Retirement Accounts.

The ERLS was born out of an initial partnership between AccountAbility Minnesota (AAM) and US Federal Credit Union (USFCU). AAM is a 37-year-old community-based organization dedicated to serving low- and moderate-income Minnesotans through high-quality, affordable tax services. USFCU is a community-focused financial cooperative based in the Twin Cities.

In addition to serving thousands of individual clients, AAM operates free tax preparation sites in cooperation with the IRS's Volunteer Income Tax Assistance (VITA) program. (For more on VITA sites and other free tax preparation assistance sites, see the sidebar below.) For several years starting in the mid-2000s, AAM had partnered with the IRS and USFCU to sponsor VITA sites at some of USFCU's branch offices.

Through years of intense involvement with low-income tax filers, AAM staff members were aware of people's need to receive their refunds quickly. They also saw the costs that RALs were imposing on the people they served. Meanwhile, USFCU's involvement in VITA sites, along with its demonstrated practice of providing accessible financial services to underserved members of the community, laid a natural foundation for participating in a partnership to create an alternative to RALs. In 2005, staff members from AAM and USFCU decided to work together to design a refund loan product that would help tax filers keep more of their EITC money.

In a grant proposal submitted to the McKnight Foundation later that year, AAM described the plan it developed in collaboration with USFCU: The two partners would undertake a demonstration project that would initially be located at two of USFCU's VITA sites in Minneapolis, and then expand it to additional sites in Greater Minnesota by the end of a three-year period. The McKnight Foundation decided to fund the project. A second funder was added when the Annie E. Casey Foundation, a national philanthropic organization focused on low-income families and children, came on board in 2006.

Inside the ERLS Program

The pilot ERLS Program was designed to build on the free tax preparation services provided at VITA sites. The program worked like this: When people came to an AAM-sponsored VITA site to have their taxes done, trained volunteers completed the tax returns, informed clients about the pilot refund program, and screened them for eligibility if they expressed interest in participating. Any tax filers whose incomes fell at or below the EITC program's income threshold were eligible to participate in the pilot program.

If clients were interested and eligible, AAM volunteers helped them fill out paperwork to open savings accounts and have their EITC refunds directly deposited into the new accounts. Next, AAM filed their tax returns with the IRS. Once the IRS accepted a return and AAM verified that the client's refund would not be garnished for debt, AAM informed USFCU that the client planned to open a savings account and take out a refund loan, and the client could then visit a branch of the credit union to complete the process and receive the loan. Since no refund loans were issued until the tax returns were approved by the IRS, the pilot program was very low-risk. In addition, the loans would arrive in the taxpayer's bank account within 24 to 48 hours, which was just as quickly as the taxpayer would have received a refund from a traditional RAL-issuing establishment.

Thanks in part to the recruiting efforts of USFCU, four more financial institutions joined on after the pilot program was initially launched: City & County Credit Union in St. Paul, City-County Federal Credit Union in Minneapolis, Northern Communities Credit Union in Duluth, and Community Development Bank of Ogema.

According to Eva Song Margolis, financial services partnership manager at AAM, and Bonnie Esposito, executive director of AAM, "US Federal played an instrumental role. They went out of their way to counsel other financial partners and make calls to interested credit unions in other places to tell them directly about how the program works and how to deal with issues."

The pilot ERLS Program began operating in early 2006. At the end of the 2006 tax season, the program fell short of its goal of 100 loans. In actuality, 23 loans were issued and 73 savings accounts were opened. By the end of the 2007 tax season, however, the program exceeded its expectations. The goal was to issue 400 loans, but 733 were issued instead, at an average amount of $2,375. More than 950 savings accounts were opened; 81 percent of them were still open at the end of 2007, with an average balance of $163. One explanation for the surge in service between the first and second years was the elimination of a first-year requirement that program participants had to have been previous RAL users.

Of the clients served in the pilot program, over 80 percent were people of color and 32 percent had previously been unbanked. The average annual gross income of the clients was $14,121. By taking advantage of the ERLS Program, clients saved an average of $296 compared to the cost of a rapid refund loan at a commercial preparer.[6/]

At VITA sites in the Twin Cities area and a few communities in Greater Minnesota, the ERLS Program helped many families and individuals get the most out of their EITC refunds. For a further demonstration of how the ERLS works in practice, it's helpful to look how the program operated in one specific community: the White Earth Indian Reservation in northern Minnesota.

The White Earth experience

In 2004, a Children's Defense Fund report noted that more than half of the taxpayers in one ZIP Code on the White Earth Indian Reservation in northern Minnesota claimed the EITC. More than three-quarters of that group used for-profit tax preparers and RALs, which resulted in an estimated total cost of $22,000 for these working-poor households.[7/]

In response to the report findings and their own experiences of working in White Earth communities, the staff of the White Earth Investment Initiative (WEII) decided to change the situation by expanding free tax preparation services for reservation residents. The mission of WEII, a subsidiary of Midwest Minnesota Community Development Corporation in Detroit Lakes, Minn., is to engage in community, economic, and housing development on the White Earth reservation with the aim of alleviating poverty and enhancing the standard of living for individuals residing there.

WEII staff members began their involvement in free tax preparation services in 2004 and 2005 by working collaboratively with an AARP-sponsored tax preparation site in Detroit Lakes. Following the 2005 tax year, WEII staff members decided to establish an independent VITA site focused exclusively on the needs of White Earth residents. WEII staff members had an existing partnership with AAM, having made use of AAM-sponsored training and other resources. After making the decision to establish an independent VITA site on White Earth, WEII staff members turned to AAM for guidance, and AAM provided training, technical assistance, materials, and fundraising support as WEII moved forward in developing the site. In 2006, in a joint effort with White Earth community leaders, WEII established an independent VITA site for White Earth residents. It operates primarily out of the Shooting Star Casino in Mahnomen, the largest city on the reservation, but also provides services in remote reservation locations.

Despite the offer of free tax assistance, usage of the site was low during the 2006 tax season. According to Sarah Ruppel, asset building coordinator for WEII, many potential customers wanted to get their taxes done in a place that provided RALs, even if it meant they had to pay for tax preparation.

Following the 2006 tax season, AAM approached WEII to ask if the organization would be interested in replicating the ERLS Program on the White Earth reservation. Recognizing that the offer of a rapid refund loan would help bring more clients to the VITA site, WEII decided to take AAM up on its offer. Working in partnership with AAM and the nearby Community Development Bank of Ogema (CDB), WEII established an alternative RAL program for the White Earth reservation.

The program, which is modeled closely on the ERLS, is called the White Earth Express Refund Loan and Savings Program. It contributed to an increase in the number of residents seeking free tax preparation services—a jump from 380 in 2006 to 500 in 2007. During the 2007 tax season, the program made 100 loans and clients opened 115 new savings accounts. By the end of the season, only seven of the accounts had been closed. The amount of savings in the remaining accounts ranges from a few dollars to a couple of hundred dollars. WEII made a commitment to encourage White Earth residents to remain "banked"; even if they withdrew all their money from their savings accounts, CDB waived the minimum balance requirement so that the accounts would remain open.

According to calculations based on the 500 tax returns that were completed in 2007, use of the White Earth VITA site resulted in substantial financial benefits for reservation residents. The total amount of EITC refunds claimed was $431,062 and the total refunds returned amounted to $1,015,266. Based on the average amounts that a for-profit tax preparer would have charged per return and per RAL, WEII estimates the alternative RAL contributed to a total savings of $129,500 in service charges and loan fees.

Expanding the program

At the end of 2008, the ERLS program concluded the last year of its three-year pilot phase. AAM staff members are in the process of summarizing their findings and making recommendations about how to expand. Their goal is to take the model to scale without the need to rely on philanthropic foundations for funding.

Bonnie Esposito points out that AAM staff would welcome an expansion of the circle of financial institutions that participate in the alternative RAL program, beyond credit unions and community development banks. But they've found that other Minnesota banks they've talked to feel hamstrung by two factors. The first involves a Minnesota regulation that prohibits banks from opening new checking accounts for people who have written bad checks in the past and had their previous checking accounts involuntarily closed. However, Esposito notes that there are no such regulations prohibiting the opening of savings accounts.

"So, aside from their own internal policies, there is no reason that banks can't open savings accounts for any Minnesotan with a photo ID and Social Security Number or Individual Tax Identification Number," Esposito says.

The second factor contributing to banks' hesitation concerns ChexSystems, a national database of people who have had difficulties managing checking accounts. According to Esposito, one of AAM's partner nonprofit agencies reported that 40 percent of the taxpayers AAM referred to them during the 2008 tax season were on ChexSystems. Another partner reported a figure of 20 percent.

"That's not surprising," Esposito observes. "AAM targets the unbanked for its alternative RAL service, and there's a reason they're unbanked. Usually, it's because they have a blemish on their credit history or they're on ChexSystems. They're turned away from mainstream financial institutions, so they go to fringe banking services that often offer predatory products."

However, Ruppel of WEII notes that the bank affiliated with WEII—CDB—opened savings accounts for all of its customers who used the White Earth ERLS Program. Since CDB was not creating transactional checking accounts for White Earth refund loan clients, the appearance of any of those clients in ChexSystems was less of a concern. AAM staff members say it would be a major breakthrough to find a way to enable a broader range of financial institutions to fully participate in the ERLS Program, perhaps by emulating CDB's example.

The growing national interest in RALs

Although the development of alternative RAL programs is still relatively rare, AAM's and WEII's achievement in creating alternative RALs has inspired and informed work in other states. For example, AAM has been called upon to assist in developing similar programs in Newark, N.J., and Baltimore, Md.

Two other noteworthy alternative RAL programs are also operating in the U.S. Alternatives Federal Credit Union in Ithaca, N.Y., runs one of the oldest and most well-established programs in the country; AAM based much of its pilot program on the Alternatives model. An effort in San Antonio, Tex., is summed up by Skip Loudermilk, vice president of sales and lending for the San Antonio City Employees Federal Credit Union. The credit union is establishing new branches to "take on, head-to-head, payday lenders and check-cashing institutions by offering a low-cost alternative to these products to the underserved and unserved market."[8/] Among these products is an alternative RAL.

Programs like the ERLS have demonstrated their effectiveness in helping low- and moderate-income people keep their full EITC refunds instead of diverting a large share of them to pay fees and interest. Though these initiatives are still in their early stages, their growing success provides an example to other organizations that serve low- and moderate-income clients.

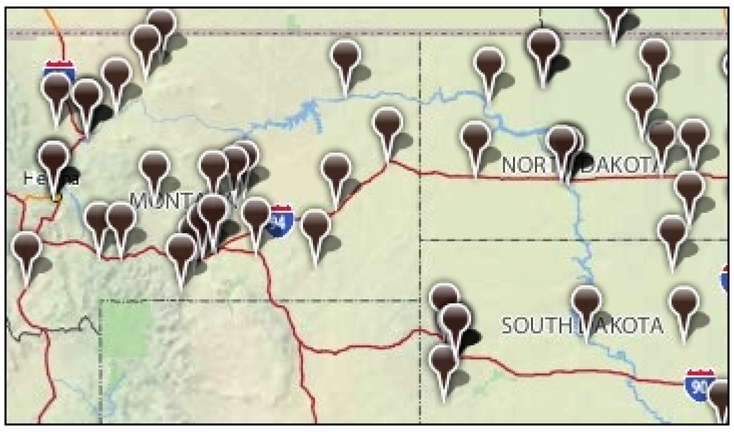
Find a free tax preparation site in the Ninth District

Free tax preparation assistance (FTPA) programs help low- and moderate income, elderly, or disabled people prepare and file their tax returns free of charge. The assistance is provided by trained volunteers who ensure that tax returns are filed correctly so clients will receive all the credits and refunds they deserve. The use of FTPA minimizes errors and saves filers money they would otherwise spend on fees at a for-profit tax preparation firm. In addition, FTPA prevents filers from taking out costly refund anticipation loans.

Government agencies or nonprofit organizations sponsor FTPA programs, often in partnership with local community coalitions or financial institutions. Assistance is delivered at convenient locations, such as senior centers, shopping malls, libraries, and schools. Most sites operate from early February through April 15.

The Internal Revenue Service (IRS) sponsors most of the FTPA sites in the U.S. through its Volunteer Income Tax Assistance (VITA) program, which serves low- and moderate-income people. Another IRS program called Tax Counseling for the Elderly provides FTPA to people at any income level who are age 60 or older. Through a grant from the TCE program, AARP offers FTPA at thousands of sites nationwide.

For the 2009 tax season, there are nearly 400 FTPA sites operating in the Ninth Federal Reserve District. To see where the sites are located, visit our interactive map titled VITA & Other Free Tax Preparation Sites in the Ninth District or click the image below. Each pointer on the map represents one FTPA site. Click on a pointer to reveal a site's street address, phone number, dates of operation, and sponsorship information. To zoom in or out, click the +/- slider bar in the upper left corner of the map.



1/ Internal Revenue Service.

2/ Chi Chi Wu, National Consumer Law Center, and Jean Ann Fox, Consumer Federation of America, *Coming Down: Fewer Refund Anticipation Loans, Lower Prices from Some Providers, But Quickie Tax Refund Loans Still Burden the Working Poor*, The NCLC/CFA 2008 Refund Anticipation Loan Report, March 2008, pp. 11–13.

3/ *An Evaluation of the 2007 Tax Season Express Refund Loan and Savings Program*, Children's Defense Fund Minnesota, October 2007, p.4.

4/ Wu and Fox, pp.11-13.

5/ Ibid.

6/ *A Minnesota Experiment: AccountAbility Minnesota's Express Refund Loan and Savings Program—Fact Sheet*, AccountAbility Minnesota, 2008.

7/ *Keeping What They've Earned: Working Minnesotans and Tax Credits*, Children's Defense Fund Minnesota, February 2006 (revised), p. 5.

8/ Tamarind Phinisee, "City Employees Credit Union is Beefing up Local Branch Presence," *San Antonio Business Journal*, February 29, 2008.